Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	

Comments of the ICORE Companies

The consulting firm of ICORE, Inc. ("ICORE"), on behalf of many small rural local exchange Companies ("RLECs),[1] hereby submits its comments in response to the Notice of Inquiry ("NOI") and Notice of Proposed Rulemaking ("NPRM") in the above-captioned proceedings.[2] The ICORE Companies believe the provision of broadband services serves a vital national economic interest. The Federal Communications Commission's ("FCC" or "Commission"), proposed two-step plan, as outlined in its NOI, NPRM, and National Broadband Plan ("NBP"), will destroy currently successful "legacy" universal service mechanisms while searching to fund the Holy Grail of 100,000,000 homes with 100 MBPS broadband service. In attempting to reach even interim goals on the way to 100 MBPS, the Commission's proposals

[1] ILECs participating in this filing include: Citizens Telephone Corporation (Warren, IN), Citizens Telephone Company of Kecksburg (Mammoth, PA), Doylestown Telephone Company (Doylestown, OH), Dunbarton Telephone Company (Dunbarton, NH), Fishers Island Telephone Company (Fishers Island, NY), Home Telephone Company (Jacob, IL), Hot Springs Telephone Company (Kalispell, MT), Ironton Telephone Company (Coplay, PA), Killduff Telephone Company (Killduff, IA), Lynnville Telephone Company (Lynnville, IA), McClure Telephone Company (McClure, OH), Palmerton Telephone Company (Palmerton, PA), Reasnor Telephone Company (Reasnor, IA), Searsboro Telephone Company (Searsboro, IA), Sully Telephone Association (Sully, IA), Sycamore Telephone Company (Sycamore, OH), Van Horne Co-op Telephone Company (Van Horne, IA), and Venus Telephone Company (Venus, PA).

[2] *In re Connect America Fund*, WC Docket No. 10-90, *A National Broadband Plan for Our Future*, GN Docket No. 09-51. *High-Cost Universal Service Support*, WC Docket No. 05-337, Notice of Inquiry and Notice of Proposed Rulemaking, FCC 10-58 (April 21, 2010) ("*NBP USF NOI NPRM*").

could have unintended consequences, many of which are not in the public interest. In addition, the FCC lacks the legal authority to fund broadband service, violating both Section 254 and Title II of the Communications Act of 1934, as amended ("Act").

Table of Contents

I. Introduction and Background

The NOI and NPRM propose a two-step plan in which the FCC would raid the current high-cost universal service fund ("USF") that supports voice-based telecommunications services, and use the bulk of those monies to fund broadband providers in a new, "Connect America Fund" ("CAF").[3] The FCC has tentatively concluded to "cap and cut"[4] the current, historically successful high-cost universal service mechanism in order to begin funding the provision of broadband to over 100 million homes at speeds of over 100 MBPS. Step 1 of the plan seeks to eliminate "universal service" as we know it today and Step 2 seeks to transfer these funds to the broadband CAF. Tremendous policy decisions like this require thorough and careful review of not just the intended consequences, but also any unintended consequences. ICORE believes the FCC's tentative conclusions on these important policies may be detrimental to rural consumers, the Companies that serve those customers, and rate of return RLECs that have recently deployed broadband services. The inability of these carriers to recover their investments made under the existing regulatory regime will punish these "early adapters". Worse yet, under the revenue-based CAF support approach, broadband providers will have no incentive to introduce new services which use their advanced network. Investing time and capital to generate revenues from new services would result in a dollar for dollar reduction in CAF support.

The Federal statutes that guide the FCC in its implementation of the universal service programs—Sections 254 and 214(e)—have not been repealed or amended. The FCC cannot choose to ignore the plain language of Section 254 nor does the FCC have the authority to drastically shift the universal service emphasis from telecommunication services to broadband services. By the same token, the FCC cannot choose to ignore the Title II tangles associated

[3] *NBP USF NOI NPRM* at ¶ 1.
[4] *Id*. at ¶ 13.

with Step 2 of its "Availability"[5] plan – funding the CAF and broadband providers with the old, "legacy" USF.[6] The FCC lacks the legal authority to fund broadband services under Section 254 (including the authority to apply universal service funding principles to broadband). This lack of authority, combined with the potential crippling impact that dismantling the "legacy" universal service system raises many questions about the FCC's proposed approach to broadband deployment. Not only does it seem unjustifiable, it comes with a high risk of causing immense harm to rural businesses and rural consumers.

[5] The FCC appears to have abandoned the term "universal service" in the NBP and latched onto the vague term, "Availability."
[6] *NBP USF NOI NPRM* at ¶ 13.

II. Reducing Legacy Support Will Harm the Public and Is Inconsistent With Section 254

A. Capping and reducing current high cost mechanisms will jeopardize in-place rural broadband infrastructure.

As the Commission notes, broadband capable networks have been indirectly funded, in part, by legacy high-cost programs[7]. With many companies having already invested in broadband networks, the industry sits at the edge of sweeping reform of the systems which have historically funded this network investment. Changes to the current high cost mechanism, intercarrier compensation structure, and the potential new CAF support will create a telecommunications environment unlike any we have seen. Like any other mid-course change, there will be winners and losers in this process. LECs who were early adapters to broadband deployment, together with their rural customers will be the losers if the FCC takes steps identified in the NOI and NPRM.

As rate of return carriers deploy broadband, they incur significant investments to upgrade network infrastructure. These investments drive settlement levels and universal service support. For a company that deployed broadband during 2009 and 2010, interstate settlements would likely have increased during that period. Universal service support however lags two years behind the investment time frame. Universal service payments received in 2010 are typically based on investment and expense levels incurred in 2008. An RLEC that spent the last two years building a network capable of providing voice and advanced services will not receive universal service support reflective of these investments. Worse yet, if the rural LEC's investments created a network capable of meeting the FCC's initial guidelines, that company would not qualify for CAF support.

[7] NBP USF NOI NPRM at ¶ 53

RLECs that have made significant investments to provide broadband service have likely done so by taking on debt. If a company cannot obtain the settlement and universal service support to help pay for the network investment, defaults on these loans become a significant risk.

B. Broadband support should be based on the embedded cost of deploying the broadband capable network.

The ICORE Companies have significant concerns that any forward looking cost model will accurately reflect the cost of bringing broadband service to markets served by rural carriers. When last evaluated for use in rural markets, the forward looking cost model failed:

> "The aggregate results of this study suggest that, when viewed on an individual rural wire center or individual Rural Carrier basis, the costs generated by the Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs. As a result, it is the opinion of the Task Force that ***the current model is not an appropriate tool for determining the forward-looking cost of Rural Carriers***."[8]

At this time, the actual model has not been released to the public for testing or analysis. Once that takes place, the ICORE Companies intend to review the model to evaluate its effectiveness in predicting the cost of building a broadband network. While the ICORE Companies still believe forward looking models will not work for rural carriers, further evaluation will be performed once the model and underlying data is available for review.

[8] Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service , CC Docket No. 96-45, released September 29, 2000, Page 18. (emphasis added)

C. The Cost-only approach to CAF support is consistent with past practice and would encourage continued deployment of new services.

As the Commission notes, except for very limited circumstances, none of the current high-cost support mechanisms consider expected revenue.[9] If implemented, the purpose of the CAF should be to fund the investment necessary to deploy a broadband network. Services offered over the broadband pipe can be provided by the broadband builder, an affiliate of the builder, or any non-affiliated entity such as Vonage. If the builder of the broadband network is required to reduce their CAF every time it introduces a new service, that company has no incentive to spend the capital necessary to bring these services to rural America. This is bad public policy and any review of the funding of broadband investment should be based on the cost of providing the broadband pipe.

D. The "Net Gap" methodology presented in the National Broadband Plan is flawed and will be detrimental to rural broadband consumers.

Comparing revenues to the expenses incurred in deploying broadband services might make sense on the surface, but it will ultimately create a disincentive for Companies to deploy new services. Presume that to serve all customers with broadband service, an RLEC incurs costs of $200 per line per month. Revenues from all services represent $120 per line per month leaving a net gap of $80 per line per month. If this LEC qualifies for the Commission's CAF, it would receive this $80 per line per month from the new federal support mechanism. What would that company's incentive be to deploy new services? Perhaps by spending millions of dollars, this LEC could deploy a head-end and begin offering video service to its broadband customers. To illustrate the flaws of capturing this

[9] NBP USF NOI NPRM at Footnote 77.

revenue in CAF calculations, the following hypotheticals are presented for ABC Telephone Company based on the assumptions set forth below:

ABC Telephone Company	Per Sub
Broadband cost per subscriber	$200
Total revenue	$120
CAF payment	$ 80
"New" Video Revenue	$ 80
"New" Video Expense	$ 40
"New" EBITDA from Video	$ 40

Developing CAF support based on all revenues earned from broadband capable network infrastructure will negatively impact the deployment of new services in rural markets. In the table above, ABC Telephone Company qualifies for $80 of CAF support. If the CAF were calculated under an all-inclusive revenue approach, the $80 of video revenue would completely eliminate the need for CAF support. However, the introduction of video services creates "new" video expense of $40 per line per month. Revenues in total are unchanged; expenses are increased.

ABC Telephone Company	Status Quo	Adding Video	Net Impact
Broadband cost per subscriber	$200	$200	$ 0
Total revenue	$120	$200	+$ 80
CAF payment	$ 80	$ 0	-$ 80
Total Revenue	$ 200	$200	$ 0
Broadband cost per subscriber	$ 120	$ 120	$ 0
"New" Video Expense	$ 0	$ 40	+$ 40
EBITDA[10]	$80	$40	-$40

The "benefit" to the LEC for introducing new services over their broadband connection is a reduction in EBITDA of $40 per line per month. In addition, the LEC would be required

[10] EBITDA is an acronym for Earnings Before Interest, Taxes, Depreciation and Amortization. It is a widely used financial indicator reflective of pre-tax cash flow.

to repay the debt incurred to purchase and install a head end. If the Commission were to consider the video expense in calculating the CAF, the LEC would remain "EBITDA neutral". That is, regardless of whether they deploy video services or remain simply a broadband provider, their cash flow is the same. In what business environment does a company, investor, or lender move forward with funding a project that contributes no additional cash flow? Of course that question is rhetorical, but a plan that moves in this direction is obviously flawed. It may ensure that American consumers receive a broadband network, but they will likely miss out on the applications or new services which make broadband such a necessary core product.

E. Reverse auctions are bad policy and have no place in national broadband planning.

The use of reverse auctions for universal service funding was vetted in the Rural Task Force's White Paper #3, "Alternative Mechanisms for Sizing a Universal Service Fund for Rural Telephone Companies", released August 2000 ("White Paper #3"). The Rural Task Force identified certain weaknesses in this type of funding, including the fact that this is not the type of competition envisioned in the 1996 Act.

> "It has been argued that competitive bidding is, in fact, anti-competitive, at least in terms of the customer's access to competitive alternatives. Under competitive bidding, carriers are only on an equal footing once every bidding cycle. After the successful bidder is selected, the winning entity has a support level advantage over the unsuccessful bidders which may be a barrier to competition."[11]

Worse yet, the reverse auction would create delays in the deployment of new services which fall under the universal service umbrella. Presume that reverse auctions are used to

[11] White Paper #3 @ Page 18.

determine the provider that will be funded to deploy the broadband network envisioned in the National Broadband Plan. Subsequent changes to supported services could not be immediately deployed. As the Rural Task Force concluded, "…these changes could only be incorporated in the statement of work at the beginning of each bidding cycle. This means there could be a built-in delay before these new supported services could be brought to the rural area."[12] Reverse auctions should not be used for CAF support.

[12] White Paper 3 @ Page 18.

III. The FCC Does Not Have the Authority to Fundamentally Alter Universal Service Emphasis from "Telecommunications Services" to Broadband

A. Universal Service is Defined as Telecommunications Service

The legal parameters of the FCC's universal service program are set primarily by Section 254 of the Act. Universal service is defined in Section 254(c)(1) as "an evolving level of *telecommunications services* that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services."[13] This first sentence of section 254(c)(1) clearly establishes that unless a service is a ***telecommunications*** service, it does not fall within the definition of universal service. Although Congress has "recognize[d] that ***telecommunications*** services would evolve over time, and that universal service should adapt to reflect those changes,"[14] neither Congress nor the FCC has ever suggested that such services would evolve into non-telecommunications services. Information services and telecommunications services are mutually exclusive.[15] Telecommunications services are distinguishable from information services and the Act unmistakably intended to make this distinction between the two services for regulatory treatment by the FCC.[16] Though not defined in the Act, broadband has been established as an information service, and not a

[13] 47 U.S.C. § 254(c)(1) (emphasis added).
[14] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, FCC 98-67, Report to Congress, ¶ 144 (1998) ("*1998 Report to Congress*") (emphasis added).
[15] *1998 Report to Congress* at ¶¶ 13, 39, and 43 (where the FCC determined "that Congress intended the categories of 'telecommunications service' and 'information service' to be mutually exclusive").
[16] In discussing the definition of "information services," the FCC concludes that when an entity offers the "capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information," it is not offering telecommunications "even though it uses telecommunications" to offer such information services (*e.g.*, voicemail). *Id*. at ¶ 39.

telecommunications service.[17] Accordingly, a broadband service may not be regulated as a universal service.

The FCC and the Federal-State Joint Board are required to work in tandem when reviewing or altering the telecommunications services that may be designated as universal services.[18] Section 254(c)(2) allows that "the Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms."[19] However any recommendation for changes to the make-up of universal services is limited by the clear language of Section 254(c)(1), which states that "the Joint-Board, in recommending, and the Commission in establishing, the definition of the services that are supported by Federal universal service support mechanisms shall consider the extent to which such ***telecommunications*** services are being deployed in public ***telecommunications*** networks by ***telecommunications*** carriers."[20]

Today's universal service support mechanisms are based on the consistent application of Section 254(c) of the Act, and nowhere in the Recovery Act's requirement for the FCC to develop the NBP[21] did Congress suggest jettisoning Section 254. Neither Section 254(c)(1), nor Section 254(c)(2), give the FCC power to use support intended for

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[17] *See in re Inquiry High-Speed Access to the Internet Over Cable and Other Facilities*,17 F.C.C. Rcd. 4798 at 4820-4824 ¶¶ 34-41, Declaratory Ruling (2002) ("*Cable Modem Declaratory Ruling*") (designating cable modem service to be an interstate "information service" and not a cable TV service or a telecommunications service); *See also in re Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, 20 F.C.C. Rcd. at 14,853 ¶ 102 ("*Wireline Broadband Order*") (affirming "that wireline broadband Internet access service is an information service").

[18] 47 U.S.C. § 254(c)(1).

[19] 47 U.S.C. § 254(c)(2).

[20] § 254(c)(1)(C) (emphasis added).

[21] *American Recovery and Reinvestment Act of 2009*, Pub. L. No. 111-5, § 6001(k), 123 Stat. 115, 515 (2009) ("*Recovery Act*").

"legacy" funding to create a broadband-based USF as the FCC has suggested doing with its new CAF plan.[22] The limitation on the FCC's ability to define the services supported by universal service has been confirmed in *TOPUC v. FCC*.[23] Specifically, in discussing "supported services" pursuant to Section 254(c)(2), the Fifth Circuit called the FCC's attempt to redefine "services" to include services unrelated to telecommunications "an implausible reading of Congress' intent."[24] The FCC's CAF plan abandons this structural limitation with its heavy, if not exclusive, concentration on broadband services.

The plain statutory language does not give the FCC the authority to drastically alter Section 254 and wholly redefine universal service to include broadband service as the Commission has proposed in the NBP generally, and in the NOI and NPRM.[25]

B. Only Telecommunications Carriers are Eligible to Receive High-Cost USF Support

Section 254(e) of the Act establishes the general eligibility requirement for receipt of universal service support. The eligibility criterion, "adopted without expansion"[26] by the FCC, unambiguously states that "only an eligible ***telecommunications*** carrier ("ETC") designated under section 214(e) shall be eligible to receive specific Federal universal

[22] *See NBP USF NOI NPRM* at ¶ 13 (concluding that "legacy" high-cost programs should be capped and cut in order to shift those investments to "broadband infrastructure.")
[23] *Texas Office of Pub. Util. Counsel (TOPUC) v. FCC*, 183 F.3d 393 (5th Cir. 1999).
[24] *Id*. at 442. In *TOPUC*, the Fifth Circuit concluded that the FCC could not use the Act's "additional services" term in Section 254(c)(3) to expand supported services to schools and libraries subject to Section 254(h) beyond additional services that were also telecommunications services. The court went on to discuss this limitation pursuant to Section 254(c)(2) and 254(c) generally, determining that the FCC did not have the authority to redefine services to include services unrelated to telecommunications.

[25] *See NBP USF NOI NPRM* at ¶ 53.
[26] *1998 Report to Congress* at ¶ 150.

service support."[27] Section 214(e) declares that "[a] common carrier designated as an eligible ***telecommunications*** carrier under [Section 214(e)] shall be eligible to receive universal service support in accordance with section 254 and shall, throughout the service area for which the designation is received, offer the services that are supported by Federal universal service support mechanisms under section 254 (c), either using its own facilities or a combination of its own facilities and resale of another carrier's services (including the services offered by another eligible ***telecommunications*** carrier); and advertise the availability of such services and the charges therefore using media of general distribution."[28]

In short, section 254(e) explicitly states that only an ETC designated as such under Section 214(e) shall be eligible to receive Federal universal service support. The law is simple: only ETCs are allowed to receive USF support, and only ***telecommunications*** carriers may be designated as ETCs.[29]

The FCC's two-step plan abandons the Act's balance and emphasis on telecommunications services and providers. The FCC's shift from "universal service" to "availability" (the catch-all term used in the NBP) does not and cannot eliminate the Commission's responsibilities pursuant to Sections 254 and 214(e) of the Act. The hasty elimination of the current "legacy" fund,[30] absent a legal substitute, is inconsistent with Congress' intent in codifying universal service in 1996. No Section in the Act relating to

[27] 47 U.S.C. 254(e) (emphasis added).
[28] *Id*. (emphasis added).
[29] *Id*.
[30] *See NBP USF NOI NPRM* at ¶¶ 51 and 53 (discussing "specific first steps" to cut legacy high-cost funding).

high-cost universal service authorizes the FCC to perform a reconfiguration of USF on this scale. The FCC simply cannot proceed as if Sections 254 and 214(e) do not exist.

IV. The FCC's NOI and NPRM Harm Rural Areas in Violation of Section 254 of the Act

The majority of high-cost support currently flows to small rural providers located in the communities that they serve. These providers rely on this vital support in order to build modern, high-cost networks, both wireline and mobile, in hard-to-serve rural areas. These rural providers have invested vast amounts of money and have undertaken serious amounts of debt in reliance of being able to pay their debts under the current USF system. These "serious reliance interests," developed over decades under the FCC's "legacy" universal service mechanisms, require the FCC to provide a much better explanation than it has done in its NOI and NPRM for its blatant disregard of current facts, circumstances, and law when it proposes a complete about-face in its universal service policy.[31] Even if the FCC had the authority to decimate legacy USF and transfer this funding to non-telecommunications services (which, as discussed above, the FCC does not), the FCC has not and cannot provide an adequate legal justification for its two-step plan.

47 U.S.C. § 254(b)(3) states:

> *Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.* [32]

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[31] *See FCC v. Fox Television Stations, Inc.*, 129 S. Ct. 1800, 1823 (2009). In *FCC v. Fox Television Stations*, the U.S. Supreme Court found that "when an agency's prior policy has engendered serious reliance interests[,] that must be taken into account." Ignoring such matters by failing to provide a reasoned explanation for disregarding facts and circumstances that underlay or were engendered by the prior policy would be arbitrary and capricious. *Id.* In the instant case, the FCC must show that it has taken into account the serious aspects of rural providers' reliance on current "legacy" mechanisms.

[32] 47 U.S.C. § 254(b)(3).

The NBP's recommendation to first concentrate on less costly areas violates Section 254(b)(3)'s fundamental universal service principle that rural consumers have access to telecommunications services that are "reasonably comparable to those services provided in urban areas."[33] The NBP suggests the FCC first address "those areas that require lower amounts of subsidy to achieve [the] goal" of maximizing the number of households that can be served quickly.[34] Over time, the FCC will then get around to "addressing those areas that are the hardest to serve."[35] Until the FCC concentrates on these harder-to-serve areas, the FCC will be in violation of Section 254(b)(3) as these neglected areas will be lacking in comparable services and rates to urban areas and those areas the FCC's decides can be "served quickly."

The FCC's immediate focus is on "lower-cost", high-cost areas and eventual focus would be on "higher-cost", high-cost areas. Reading between the lines, it appears that the FCC will initially concentrate broadband support payments through the CAF to price-cap carriers serving less "rural" population centers. This design seems to pre-determine the delivery of support to AT&T and Verizon to build out less-costly rural areas near the population centers. Only after this funding is provided, the focus would shift to genuine rural LECs. The prospect of raiding legacy high-cost funding to support the price-cap carrier's broadband cherry-picking is an ugly irony, and is inconsistent with Section 254's principle that consumers nationwide have access to services at reasonable rates.[36]

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[33] *Id.*
[34] Federal Communications Commission, *Connecting America: The National Broadband Plan*, (March 16, 2010), Chapter 8 at p. 141 ("NBP").
[35] *Id.*
[36] 47 U.S.C. § 254(b)(3).

V. Conclusion

The FCC has recognized extreme doubt regarding its legal authority to support funding for broadband services under sections 214(e) and 254. However, the FCC has tentatively concluded to decimate legacy USF anyway. Not only does the FCC lack the legal authority to pursue this plan, its extreme "about face" on universal service will subject it to increased court scrutiny and more regulatory uncertainty. Moreover, the Commission's plan abandons the Act's balance and emphasis on telecommunications services and providers and violates the overall principles of universal service codified by Congress.

For the foregoing reasons, the ICORE Companies respectfully urges the FCC to abandon its two-step plan to reform USF.

Respectfully submitted,

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