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
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
High-Cost Universal Service Support	)	WC Docket No. 05-337
Developing an Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92

REPLY COMMENTS OF

THE FREE STATE FOUNDATION*

These reply comments are submitted in response to the Commission's proposals for reforming and modernizing the Universal Service Fund (USF) and intercarrier compensation (ICC) systems. The Commission proposes near-term changes while simultaneously proposing long-term reforms leading to a simpler, unified system.

I. Introduction and Summary

These reply comments emphasize that the Commission's end game for its comprehensive USF and ICC reforms should be the eventual elimination of all high-cost fund and related subsidies. Placing a hard cap on the high-cost fund and lowering it over time in tandem with a decreasing fund size constitutes a realistic means for achieving that end. Critical to ensuring this

* These comments express the views of Randolph J. May, President of the Free State Foundation, and Seth L. Cooper, Research Fellow of the Free State Foundation. The views expressed do not necessarily represent the views of others associated with the Free State Foundation. The Free State Foundation is a nonpartisan, non-profit free market-oriented think tank.

outcome is the establishment of a date-certain deadline, say, approximately ten years, for sunsetting all high-cost and related subsidy programs. This does not mean that, after appropriate review, the Commission could not renew such programs for a limited period. But a firm sunset date would shift the evidentiary burden for renewing the program to proponents of an extension.

Once the Commission sunsets all high-cost subsidies, any remaining universal service subsidies should be provided exclusively through programs that are transparent, explicit, and targeted to individual consumers, not telecommunications companies. Lifeline and Link Up are two existing programs targeted to individual consumers that should be looked to as model vehicles for the provision of universal service subsidies in a post-high-cost fund 21st Century.

The reform efforts' importance should dictate that the Commission avoid distractions from issues extraneous to fiscally responsible USF and ICC reforms. Thus, the Commission should reject calls to use such reforms as a vehicle for imposing a broad array of regulation, such as network neutrality regulation. Imposing extraneous regulations would be completely counterproductive to achieving universal service goals because such regulations impose costs that discourage new network investment.

II. The Commission Should Impose a Cap and a Sunset Date on the High-Cost Fund

The overarching, long-term goal of Commission's universal service reforms should be the eventual abolition of all high-cost fund subsidies to telecommunications providers. The goal of universal service in voice and information service is laudable. But as the Commission's reports indicate, telephone service penetration rates are at 96%.[1] And as the National Broadband Plan

[1] Wireline Competition Bureau, Federal Communications Commission, "Telephone Subscribership in the United States (Data through March 2010)" (August 2010), at 1.

points out, 95% of the U.S. population has access to broadband.[2] In short, even granting an expansion of universal service goals to include broadband Internet, existing build-out and continuing trends for voice and information services show that the outdated, costly, and often financially wasteful USF and ICC systems we have today should be subject to immediate limitation, ongoing reduction, and eventual but date-certain elimination.

The universal service system as it stands today is already in significant tension with the basic underpinnings of our constitutional system, including separation-of-powers principles, democratic accountability, and the limits of government power over the private sector and private actors. The USF high-cost fund is part of a multi-billion dollar subsidy system that operates outside the Congressional appropriations process. It is peculiarly overseen by an agency independent of all three branches of government that has delegated the program's administration to yet another independent entity – the Universal Service Administrative Company (USAC).[3] Thus, an entity doubly-removed from democratic accountability sets surcharges or *de facto* tax rates on private consumers, the funds from which are transferred directly to private companies. (That tax on telecommunications consumers' monthly bills now stands near fifteen percent.[4]) The Commission should seize this opportunity to not only limit the size of high-cost program subsidies, but also reduce the size of such subsidy amounts, and eventually end all such subsidies.

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[2] FCC, National Broadband Plan (March 16, 2010), at 20 ("Today, 290 million Americans—95% of the U.S. population— live in housing units with access to terrestrial, fixed broadband infrastructure capable of supporting actual download speeds of at least 4 Mbps. Of those, more than 80% live in markets with more than one provider capable of offering actual download speeds of at least 4 Mbps. Meanwhile, 14 million people in the United States living in 7 million housing units do not have access to terrestrial broadband infrastructure capable of this speed.") Of course, almost all American households have access to satellite broadband service. Although not presently comparable to terrestrial offerings with respect to speed, satellite broadband offerings are expected to be increasingly robust.

[3] *See* Comments of Comptel, WC Docket No. 10-90, *et al.*, (April 18, 2011), at 17-19 (describing flaws in the fiscal management of USF).

[4] Office of Managing Director, FCC, "Public Notice: Proposed Second Quarter Universal Service Contribution Factor," CC Docket No. 96-45 (March 10, 2011).

Our initial comments urge the Commission to meet its "fiscally responsible" principle by reducing the financial burden on consumers of telecommunications services.[5] This requires the Commission impose a cap on the overall size of the high-cost fund at a level no higher than $4.3 billion per year, if not less. Setting a hard cap extending to all high-cost fund-related programs provides the Commission a pathway for future reductions in the overall size of the fund, corresponding to incrementally lower levels for the cap.

Comments submitted by other parties in this proceeding similarly recognize the importance of placing an overall cap on the size of the high-cost fund and related subsidies.[6] But in every or nearly every instance such calls for a cap fail to emphasize the importance of reducing the size of the high-cost fund over time and eventually eliminating it. Rather, several comments proposing caps appear to presume the Commission's reforms will nonetheless further a perpetual voice and broadband subsidy system that has no end in sight.[7] In other words, many of the comments calling for a cap on the size of the fund effectively divorce such a cap from any overarching plan for significantly reducing and eventually ending all high-cost fund subsidies themselves. Comments that oppose or are ambivalent to caps or which simply encourage expanding the pool of subsidy recipients also fail to recognize the importance of reducing and eventually eliminating high-cost subsidies to telecommunications providers.[8]

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[5] *See* Comments of the Free State Foundation, In the Matter of Connect America Fund, WC Docket No. 10-90, (April 18, 2011), available at: http://www.freestatefoundation.org/images/USF-ICC_Comments_041811.pdf.
[6] *See, e.g.*, Comments of State Members of Universal Service Joint Board, WC Docket No. 10-90, (May 2, 2011), at 11; Comments of the National Association of State Utility Consumer Advocates (NASUCA), WC Docket No. 10-90 (April 18, 2011), at 10; Comments of CBeyond, Inc., Integra Telecom, Inc., and TW Telecom Inc., WC Docket No. 10-90 (April 18, 2011), at 17.
[7] *See, e.g.*, Comments of State Members of Universal Service Joint Board, at 11; Comments of NASUCA, at 9-10.
[8] *See, e.g.*, Comments of the Independent Telephone & Telecommunications Alliance, WC Docket No. 10-90 (April 18, 2011), at 14-15 (opposing caps on high-cost fund); Comments of New America Foundation, Consumers Union, and Media Access Project, WC Docket No. 10-90 (April 18, 2011), at 5-11 (urging expansion of eligible recipients for subsidies).

It would be a mistake for the Commission to treat a high-cost fund cap as a mechanism for preserving *status quo* levels for high-cost area provider subsidies that now amounts to a fifteen percent tax burden on consumers' monthly bills. The Commission should not set its sights so low. Rather, it is crucial that the Commission impose a cap on the fund as a critical part of an overall effort to bring all high-cost subsidies to an eventual end as prior subsidies – and competitive forces – achieve universal service goals.

To ensure the eventual end of all high-cost fund subsidies to telecommunications providers serving high-cost areas, the Commission should adopt a date certain, say, approximately ten years, by which all high-cost program and related subsidies should sunset. The Commission could also establish a series of progress benchmarks to guide its incremental reduction of the size of the fund prior to the sunset date.

Setting an explicit sunset date for all high-cost subsidies will make the goal of ending such subsidies concrete. A cap on the high-cost fund will keep the fund from growing in size amidst near-term reforms and an incrementally lowered cap will lead to a steadily reduced fund size that will culminate in the end of fund subsidies entirely. Announcing a sunset date for ending high-cost subsidies will signal the Commission's seriousness of purpose in transitioning the USF and ICC systems to greater reliance on market forces. And such an announcement will crystallize the expectations of high-cost area providers, particularly those subject to guaranteed rate-of-return regulation: they should not rely on such subsidies in perpetuity. A reasonable sunset date will allow them time to make adjustments as needed to transition operations to a more market-oriented approach to providing services.

As important as the specific date set for sunsetting high-cost subsidies is the actual establishment of a sunset date to serve as the overarching goal of high-cost fund reform that will relieve consumers of a significant tax burden and mark the federal government's exit from its operation of a public-to-private transfer subsidy system in favor of a market-based approach. If, at the expiration of the subsidy program, the Commission deems that it is necessary to renew the program for a limited period, it could do so upon a proper showing.

III. The Commission Should Rely Exclusively on Explicit Individually-Targeted Subsidy Programs Such as Lifeline and Link Up Once It Ends All High-Cost Subsidies

Following the sunset of high-cost subsidies for voice and broadband service providers, any ongoing universal service objectives necessitating subsidies could be met by programs that are transparent, explicit, and targeted to individual voice and broadband users. The obvious upshot to subsidies targeted to individual users who meet eligibility criteria is that the subsidies go to those that actually need them. Individually-targeted subsidies allow the consumers themselves to choose a voice and broadband service that best serves their needs. Such an approach avoids the unseemliness of government subsidizing private telecommunications providers with money taken from the consuming public. Subsidies targeted to individual users can also be more reliably monitored for accountability, given the difficulties inherent in allocating and distinguishing different costs of business incurred by telecommunications providers.

Comments in this proceeding urge the Commission to adopt voucher systems by consumers could obtain one-time payments from universal service funds to the broadband services provider of their own choosing.[9] For the reasons given above, the Commission should not only take such proposals seriously but also make a system based on this

[9] *See, e.g.*, Comments of the Wireless Service Providers Association, WC Docket No. 10-90 (April 18, 2011), at 9-10.

approach the desired end-state for universal service funding once high-cost fund subsidies sunset.

One immediately plausible approach to ensuring universal service in a post-high-cost world is expanded reliance on the Lifeline and Link Up programs. The Lifeline and Link Up programs provide discounts on initial home phone installation fees and monthly service charges, respectively. Discounts are available for qualified low-income subscribers and are subject to audit controls. Those programs could be expanded to low-income users in both remote and urban areas, providing discounts for installation and monthly charges for today's broadband services, in addition to voice services. In fact, the National Broadband Plan endorses this approach, calling for modernization of Lifeline/Link Up that will allow include support for broadband service for qualifying individuals.[10] And in a separate but related proposed rulemaking the Commission is now taking first steps toward allowing discounts be used for bundled voice-broadband service programs.[11]

Of course, even with regard to individual user-targeted subsidies such as Lifeline and Link Up, the best approach is for the Congress to appropriate funds directly from the U.S. Treasury, so that there is greater accountability to constitutional process and to the public. Those principles should hold for all universal service subsidies, regardless of the particular program. But reliance on truly explicit, transparent and individually-targeted subsidy programs would disentangle government from the practice of subsidizing private companies with consumers' money, would reduce waste and inefficiencies, and better serve the cause of universal service by directing subsidies to those who need them.

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[10] National Broadband Plan, at 172.
[11] FCC, NPRM, In the Matter of Lifeline and Link Up Reform and Modernization, WC Docket No. 11-42, CC Docket No. 96-45, WC Docket No. 03-109 (Rel. March 4, 2011).

IV. The Commission Should Not Let Its Urgent USF and ICC Reforms Be Sidetracked By Extraneous Issues

In carrying out its project to put the USF and ICC systems on a modernized, unified, more market-based and fiscally responsible footing, it is critical that the Commission avoid unnecessary distractions. The necessity and urgency of these long-overdue USF and ICC reforms requires that the Commission keep extraneous policy issues out of its reform efforts.

Comprehensive USF and ICC reform is a major undertaking in itself. Injecting issues unrelated to core USF and ICC reform would bog down needed reform with disputes unrelated and unhelpful to achieving such reform. The result would be further delays in achieving reform, or even prevention of any kind of reform.

For these reasons the Commission should reject calls for imposing network neutrality regulation as a public interest obligation for eligible telecommunications carriers.[12] The Commission should refrain from imposing network neutrality regulation in any part of its USF programs or reforms. Network neutrality regulation is extraneous to comprehensive USF and ICC reform goals, and, in fact, would undermine them by discouraging the investment in costly new network facilities.

Moreover, the wide-ranging implications of network neutrality regulation for broadband Internet service providers make it ill-suited for consideration in proceedings focused on voice and broadband subsidies to high-cost areas. As all are aware, the Commission already addressed network neutrality regulation through a highly controversial order issued last year.[13] Significant policy and legal defects with the order's regulation of broadband Internet network management

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[12] *See, e.g.*, Comments of New America Foundation, *et al*., at 11-15; Comments of Public Knowledge and Benton Foundation, WC Docket No. 10-90 (April 18, 2011), at 18-22; Comments of Google Inc., WC Docket No. 10-90 (April 18, 2011), at 16-17.

[13] FCC, Report and Order (Order), *In the Matter of Preserving the Open Internet*, GN Docket No. 09-91, WC Docket No. 07-52 (December 23, 2010).

have already been described at length in other settings.[14] The Commission should keep those ongoing disputes over network neutrality regulation from spilling over to its USF and ICC reform efforts and potentially undermining them.

V. Conclusion

For the foregoing reasons, the Commission should act in accordance with the views expressed herein.

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[14] *See, e.g.*, Written Statement by Randolph J. May, President, Free State Foundation, before the Subcommittee on Intellectual Property, Competition, and Internet, Hearing on "Ensuring Competition on the Internet: Network Neutrality and Antitrust" (February 23, 2011), available at: http://www.freestatefoundation.org/images/Written_Statement_on_House_Net_Neutrality_Hearing_022311.pdf; Seth L. Cooper, "Opening the Internet to Regulation: Assessing Risks of the FCC's Failure to Limit Its New Powers," *Perspectives from FSF Scholars*, Vol. 6, No. 4 (January 21, 2011), available at: http://www.freestatefoundation.org/images/Opening_the_Internet_to_Regulation_Assessing_Risks_of_the_FCC_s_Failure_to_Limit_Its_New_Powers.pdf.