Supporting Universal Access to Telecommunications Services: Lessons and Challenges

Remarks by FCC Commissioner Kathleen Q. Abernathy
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Thank you for that kind introduction. It is a pleasure to be here among so many friends, including several of my colleagues on the Federal-State Joint Board on Universal Service.

Yesterday, I had the privilege of testifying before the U.S. Senate regarding the health and status of universal service. I thought I would share with you some of the observations I made to the Subcommittee and describe how the FCC is attempting to strengthen the federal support mechanisms for high-cost areas, schools, libraries, and rural health clinics, and low-income consumers. I know that broadband deployment and local competition are also on the agenda today, so I will also discuss some of my thoughts on those subjects.

Universal Service

While policymakers may have a wide range of views on how best to promote the universal service principles embodied in section 254 of the Communications Act, there is nearly unanimous agreement that universal service is a critical policy objective. In fact, long before the enactment of section 254, regulators at the state and federal level had pursued the goal of providing high-quality telecommunications services at affordable rates to all Americans. I am proud to serve on the Joint Board with such able and dedicated colleagues as Lila Jaber, Bob Rowe, and Billy Jack Gregg — each of whom is participating today — so that we can continue to protect and preserve universal service.

The Telecommunications Act of 1996 was a watershed event for many reasons, one of which was that it changed the way we think about universal service. In the past, when local telephone companies had legally protected monopolies, regulators could promote universal service by setting rates in rural areas well below cost, and allowing the carriers to make up the difference by charging above-cost prices in urban areas. Regulators also built subsidies into business rates and interstate access charges imposed on long distance carriers.

The introduction of competition into local markets changed all of this. Competition meant that implicit subsidies would be eroded as new entrants undercut rates that were set well above cost, such as business rates in urban areas. Congress accordingly directed the FCC to adopt *explicit* support mechanisms that would be sufficient to ensure that rates remain affordable and reasonably comparable throughout the nation. In response to this mandate, the FCC has developed several explicit support mechanisms for carriers that provide service in high-cost areas.

The 1996 Act also expanded the scope of universal service by directing the FCC to establish support mechanisms for schools and libraries and for rural health care

facilities. The schools and libraries program (often called the e-rate), which provides up to $2.25 billion in annual support, has enabled millions of school children and library patrons to gain access to advanced telecommunications and Internet services. While the rural health program generally has been underutilized, the FCC is currently considering a variety of measures to strengthen it.

In addition to the high-cost support mechanisms and the programs supporting schools, libraries, and rural health clinics, the FCC's Lifeline and LinkUp programs provide discounts off monthly service charges and connection fees to ensure that low-income consumers have access to basic telephone service. Last year, these programs provided approximately $647 million in support.

All of these programs promote the universal service goals set forth in section 254(b) of the Act, including the availability of quality services at affordable rates; access to advanced services in all regions of the Nation; comparable access to telecommunications services for all consumers, including low-income consumers and those living in rural areas; and access to advanced services for schools, libraries, and rural health care facilities.

Shortly after Congress's enactment of the 1996 Act, the FCC adopted rules regarding the collection and distribution of universal service support. Now, with several years of experience under our belts, we are engaged in a reexamination of many aspects of the program to ensure that each component is administered as efficiently and effectively as possible. A host of marketplace and technological developments have already prompted some course corrections, and may ultimately cause us to reassess certain fundamental policy choices made in the initial implementation period.

Therefore, I thought it might be useful to provide a backdrop for today's panels by describing the universal service proceedings we have underway at the FCC and the Joint Board. In doing so, I will try to highlight some of the challenges confronting universal service and, where possible, share my views on the direction we should be taking.

High-Cost Support

The Commission has two pending rulemakings that focus on the distribution of support to high-cost areas, and the Joint Board also is conducting a proceeding in this area.

First, the FCC is reconsidering aspects of the non-rural high-cost support mechanism. "Non-rural" is really a misnomer, however, because this fund supports carriers operating in rural areas — the name is intended to distinguish the "non-rural" carriers, such as the Bells and other large independent LECs, from the smaller rural telcos, which receive support from different mechanisms. The non-rural mechanism provides support where the forward-looking costs of providing service in a particular state exceed the national average cost by more than 35%. The U.S. Court of Appeals for the Tenth Circuit remanded the FCC's order that established this mechanism, because the Commission did not adequately explain how the mechanism would be sufficient to enable states to set affordable rates that are reasonably comparable in both rural and urban areas. In particular, the court directed the Commission to consider how to induce states to develop their own support mechanisms to fund high-cost areas within their borders, since

the federal mechanism aims primarily to equalize cost differentials *among* the states. The Joint Board issued a Recommendation last October. A majority of the Joint Board, including myself, suggested preserving most of the existing structure but also adopting some new safeguards to act as a safety valve and ensure that rates in high-cost rural areas remain reasonably comparable to those in urban areas. The Commission will complete its consideration of the Joint Board's recommendations later this year.

The second FCC proceeding relating to high-cost support focuses on the definition of services that are eligible for universal service support. Today, supported services include voice-grade local service, access to 911, access to interexchange services, and other basic local services. In a Recommended Decision issued last July, the Joint Board recommended maintaining the existing list of supported services.

One issue that was hotly contested was whether equal access to interexchange services should be added to the list. Since wireline carriers already are required to provide equal access, this was really a debate about whether to require *wireless* carriers who qualify for support as ETCs to provide equal access.

Another key issue in the definitions proceeding was whether to provide direct support for broadband services, in addition to the support for the underlying loop facilities that carriers receive today. The Joint Board recognized the increasing importance of broadband services in the lives of American consumers, but concluded that broadband fails to satisfy most of the eligibility criteria set forth in the statute. Specifically, the Joint Board stated that broadband services are not yet *essential* to education, public health, or public safety, because such resources are readily accessible through alternative means, such as voice service or dial-up Internet service. In addition, broadband services have not been subscribed to by a substantial majority of residential customers. The Joint Board further concluded that providing direct support for broadband services would not serve the public interest, because it would place enormous financial burdens on American consumers and threaten the sustainability of the universal service fund. The Commission is currently considering this Recommended Decision and will issue a final order later this year.

The high-cost proceeding that is now before the Joint Board focuses on the intersection of competition and universal service in rural areas. The Commission referred this proceeding to the Joint Board in November 2002, and the Joint Board issued a public notice seeking comment in February. The issues for comment include the impact of providing support to competitive eligible telecommunications carriers (ETCs) on the sustainability of the universal service fund, the manner in which competitive ETCs receive support (often called "portability"), and the consequences of supporting multiple lines per household. The public notice also sought comment on the process the states use to designate ETCs and whether the FCC should establish guidelines for the states to consider. Following the close of the comment period, the Joint Board intends to organize a public forum involving rural LECs, wireless carriers, consumer groups, and other interested parties to gather additional information. This rulemaking is only in its preliminary stages, but its importance is undeniable and it will therefore be the Joint Board's primary focus in 2003. While it is true that, of the 1,400-plus ETCs that received high-cost support in the fourth quarter of 2002, only 63 were competitive ETCs (including a number of mobile wireless carriers), we expect significant growth in the funds going to CETCs.

Schools and Libraries and Rural Health Care Facilities

In addition to these proceedings on the high-cost support mechanisms, the Commission is examining the support mechanisms for schools and libraries and for rural health care providers. Now that the Commission has had significant experience overseeing these support mechanisms, we are seeking to capitalize on this experience by making these programs more effective and efficient.

The schools and libraries proceeding rulemaking aims to streamline the application and appeals processes by eliminating red tape and needlessly burdensome requirements. At the same time, this rulemaking will look at potential rule changes that will address issues that have been identified in the course of the Commission's ongoing oversight over the e-rate program. For example, there is concern that some applicants may have manipulated the process. The Commission is fully committed to taking actions where necessary to address potential waste, fraud, and abuse, and we will consider initial rule changes based on the record in the very near future. I have also announced that I am organizing a public forum on May 8 focusing on several of the oversight issues raised in the rulemaking. To the extent that these issues remain outstanding following the Commission's upcoming Report and Order, I hope that the public forum will enable us to quickly develop a consensus on additional means of protecting against gaming of the system.

Low-Income Support

The third component of the federal universal service regime is Lifeline/LinkUp, which is a support mechanism for low-income consumers. The Joint Board has just completed a Recommended Decision on proposals to bolster the effectiveness of this mechanism. This Recommended Decision suggests new ways for low-income consumers to qualify for support and also address questions regarding states' verification of eligibility and outreach efforts. As with the e-rate and rural health care programs, the goal of the rulemaking is to remove impediments to beneficiaries' receiving support while simultaneously preserving the integrity and enhancing the efficiency of the program.

Contribution Methodology

Each of the programs I have just described above draws support from a pool of carrier contributions that are made pursuant to section 254(d) of the Act. In a series of related proceedings, the Commission has been actively exploring changes to the methodology for assessing contributions on carriers. Since 1997, contributions to the explicit support mechanisms have been assessed on carriers as a percentage of their revenues from end-user interstate telecommunications services. Several trends have combined to put upward pressure on the contribution factor (which is currently 9.1%), and in turn increased the funding burden on consumers. While long distance revenues grew between 1984 and 1997, they have since been flat or in decline as a result of price competition and substitution of wireless services and e-mail. Because federal universal

service contributions by law may be assessed only on interstate revenues, this shrinking of the revenue base has caused the contribution factor to rise steadily. Another important trend has been the increasing prevalence of bundled service plans. For years, wireless carriers have offered buckets of any-distance minutes at flat rates, and now wireline carriers such as MCI and Verizon are offering packages that include local and long distance for a single price. In addition, many carriers offer business customers bundles that include local and long distance voice services, Internet access, and customer premises equipment. Such bundling has been a boon for consumers but has made it difficult to isolate the revenues from interstate telecommunications services. And the problem is likely to get worse as bundling becomes more and more popular.

In December 2002, the Commission adopted a number of measures to stabilize the universal service contribution factor in an effort to mitigate the growing funding burden on consumers. But more fundamental reform may be necessary to ensure the sustainability of universal service funding in the long term. For this reason, the Commission is continuing to consider whether a contribution methodology incorporating a component based on end-user connections, in addition to or in lieu of our revenue-based methodology, may create a more sustainable model for funding universal service in the future. The number of end-user connections has been more stable than the pool of interstate revenues, and connection-based charges can be adjusted based on the capacity of each connection to ensure an equitable distribution of the funding burden among business and residential customers. The Commission has sought comment on several different proposals and will consider additional changes to the contribution methodology based on the record now being developed. During the previous comment round, the state members of the Joint Board generally endorsed the notion of moving to a connection-based contribution methodology. I look forward to hearing from the public and from my state colleagues on the latest proposals in the record.

Broadband and Local Competition

Well, that's probably more than you wanted to know universal service. But before I conclude my remarks, I know I probably cannot avoid saying *something* about the Triennial Review proceeding. While we remain in our sunshine period, I am limited to discussing my own take on the issues, so let me offer a brief summary of my views on two of the key issues decided in that proceeding. One of these issues concerns the imposition of unbundling obligations on fiber loop facilities used to provide broadband services, and the other concerns UNE-P, which even my seven-year-old daughter now knows stands for the unbundled network element platform.

As most of you probably know, the Commission decided not to impose unbundling obligations on new investment in fiber loop facilities. Specifically, the Commission will not require incumbent LECs to unbundle fiber-to-the-home loops. Nor will incumbent LECs be required to unbundled a packetized broadband channel over hybrid fiber/copper loops. What this means is that CLECs will continue to get exactly what they get today — access to copper loops, and access to high-capacity loops over fiber, using a non-packetized technology called TDM. In addition, I want to make clear that when I say incumbents are not required to unbundle these fiber facilities, I mean that they need not provide them at TELRIC prices. But the Bell operating companies still

must make the facilities available to competitors on a wholesale basis, because section 271 requires them to provide competitive access to their loops.

I believe this decision strikes the appropriate balance between the goals of providing incentives to invest in new infrastructure and of giving competitors access to bottleneck facilities. As I mentioned, CLECs will not lose access to any existing UNEs. But we are refusing to *extend* new unbundling obligations to the advanced networks of tomorrow, because they do not exist yet. Why? First, because I generally do not support adopting regulations based on what *might* happen, because it is difficult to make accurate predictions about impairment. Second, I believe that those next-generation networks may never get built if incumbents are required to turn over the fruits of their investment at TELRIC prices.

I did disagree with one aspect of the broadband analysis, which was the decision by the majority to eliminate line sharing over copper loops. Unlike new fiber investment, copper loops are already in place. So giving competitors like Covad the ability to share those loops does not deter investment at all. In fact, allowing competitors to offer DSL through line sharing promotes competition *and* investment. If the incumbent wants to find a way to differentiate its service offerings, it can built new fiber loop facilities without being subject to the TELRIC unbundling regime. I recognize that, in time, intermodal competition from sources like cable, wireless, and satellite will be very beneficial for consumers, but in the short term, as some of these new broadband platforms are still getting off the ground, I think line sharing would have provided a much-needed competitive alternative.

Finally, let me say a few words about UNE-P. I know that some of you may disagree with me, but I believe the majority's decision to allow each state commission to decide the fate of unbundled switching, based on a largely subjective analysis, was bad for the telecom market and, in the long term, will be bad for consumers. The majority concluded that, even though CLECs have deployed more than 1,300 switches nationwide — in some 86% of all wire centers — they could reach any conclusions about whether competitors are impaired in the absence of unbundled switching.

I believe that the Commission had a legal obligation to take on the challenge of deciding the circumstances in which impairment exists. For example, all the Commissioners believe that certain operational issues surrounding the hot cut process needed to be addressed through performance metrics and other rules. The Commission also could have determined that *economic* impairment exists in markets where fewer than a particular number of switches have been deployed, or in markets with fewer than a set number of lines, or based on a variety of other tests in the record. But I believe we were not permitted to throw up our hands and turn over the entirety of the job to the states. The FCC and state commissions have an important partnership in promoting local competition, but each has a statutorily defined role to play in that partnership. Section 251(d)(2) of the Act makes clear that the FCC — not the states — must decide which network elements must be unbundled.

While I believe the decision is legally indefensible, I am equally concerned about its impact on the marketplace. What this market needs is certainty. A better approach, which I would still have dissented from, would have been to make an actual *finding* that impairment exists. But instead the majority established a *presumption* that will give CLECs and ILECs no indication of whether UNE-P will be available in a given state.

Rather than adjusting business plans to a new federal regime and investing in facilities-based competition, carriers will now spend the next several years litigating before each state commission, and then litigating in federal district court, and ultimately litigating in the courts of appeals. To be sure, any decision by the FCC would have been appealed as well, but there is an enormous difference between the timing and uncertainty involved in a single federal appeal and 50 separate litigation tracks.

I am disappointed by this outcome, because the FCC had an opportunity to put us on a path towards more sustainable facilities-based competition and, ultimately, a greater reliance on market forces. Instead, the majority opted for an extraordinary degree of regulatory oversight and uncertainty. And my position is in no way intended to impugn the professionalism of my state colleagues. I have no doubt that state commissions will attempt in good faith to make economically sound decisions, but I also know that different states will reach diametrically opposed conclusions based on the same underlying facts. That can't be a good outcome. But my sincere hope is that the state commissions can salvage some rationality and certainty in this process, although I am concerned that the structure adopted by a majority of the FCC may preclude that from happening.

Thank you for the opportunity to discuss these important issues. I would be happy to take some questions.