A DISCUSSION DRAFT OF THE UNIVERSAL SERVICE REFORM ACT OF 2009

HEARING

BEFORE THE

SUBCOMMITTEE ON COMMUNICATIONS, TECHNOLOGY, AND THE INTERNET

OF THE

COMMITTEE ON ENERGY AND COMMERCE

HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

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A DISCUSSION DRAFT OF THE UNIVERSAL SERVICE REFORM ACT OF 2009

TUESDAY, NOVEMBER 17, 2009

SUBCOMMITTEE ON COMMUNICATIONS,
TECHNOLOGY, AND THE INTERNET,
COMMITTEE ON ENERGY AND COMMERCE,
HOUSE OF REPRESENTATIVES,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:39 a.m., in Room 2123, Rayburn House Office Building, Hon. Rick Boucher [chairman of the subcommittee] presiding.

Present: Representatives Boucher, Markey, Eshoo, Stupak, Doyle, Inslee, Butterfield, Matsui, Christensen, Castor, Space, McNerney, Welch, Dingell, Stearns, Shimkus, Blunt, Buyer, Walden, Terry, Blackburn, and Barton (ex officio).

Staff Present: Roger Sherman, Chief Counsel; Greg Guice, Counsel; Shawn Chang, Counsel; Amy Levine, Counsel; Pat Delgado, Waxman Chief of Staff; Phil Barnett, Staff Director; Bruce Wolpe, Senior Advisor; and Sarah Fisher, Special Assistant.

OPENING STATEMENT OF HON. RICK BOUCHER, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF VIRGINIA

Mr. BOUCHER. The subcommittee will come to order.

Good morning to everyone, and thank you for your attendance today.

This morning, our hearing focuses on the Universal Service High-Cost Fund and the reforms to it that are proposed in a legislative discussion draft that is now before us.

Having affordable telephone rates for all Americans is essential to our national wellbeing. At a time when electronic commerce and communications are central to national economic performance, keeping all Americans connected should be a priority for rural and metropolitan residents alike.

While the universal service support is largely targeted to the rural areas where costs are high because of terrain, low-population density, and the long distances the communications lines have to traverse, the benefits of having everyone connected flow to urban and rural areas alike. And I hope that members will not lose sight of that reality as we consider the reforms that are needed to ensure the sustainability of the Universal Service Fund.

It is now under tremendous pressure, and a comprehensive reform is clearly called for, and I think it is urgently needed. New technologies and business models that make local and long-distance

telephone traffic essentially indistinguishable are combining to diminish the long-distance revenues that are relied upon to support universal service.

Since the universal service long-distance surcharge is being imposed on a declining revenue base, the surcharge rates are rapidly raising. Today, the contribution rate is 12 percent of long-distance revenues. And, in January, that contribution rate is set to rise to a record-breaking 14.2 percent. And unless we enact comprehensive reforms, further escalation will continue after that.

This status quo is simply not acceptable and sustainable. New controls must be placed on costs so that the level of universal service support can be contained. The bill before us caps the High-Cost Fund. It requires competitive bidding for the provision of support to wireless carriers. It imposes rigorous auditing and reporting requirements on the carriers that receive support. We also expand the contribution base to intrastate services and to all entities that provide a connection to the network as a means of relieving pressure on the declining-revenue long-distance base. These changes on both the contribution and the expenditure sides should produce a sustainable Universal Service Fund.

The bipartisan discussion draft that we now have before us I circulated with our colleague from Nebraska, Mr. Terry. And it results from almost 4 years of consultations that Mr. Terry and I have undertaken with literally dozens of stakeholders having competing interests with respect to universal service. We have sought and now we have achieved a consensus among these parties that have competing views with regard to universal service.

Our draft bridges the divide on universal service issues between large carriers, such as Verizon and AT&T, that are net contributors into the Universal Service Fund and the smaller rural carriers that are net recipients of universal service funding. As we will hear from our witnesses this morning, stakeholders on both sides of this classic divide are now united in their support for the bill before us.

The draft makes a broad range of other changes, such as qualifying broadband as an eligible subject for universal service expenditures for the first time. Other elements in our measure include a better targeting of support to high-cost areas by switching from statewide to wire center averaging; fixing the phantom traffic problem by requiring carriers to pass through call identifying information; eliminating traffic pumping, which has become a major problem of late, by prohibiting carriers from sharing access charges with third parties that offer free or reduced-cost services; making rural exchanges more marketable for telephone companies that desire to sell them by eliminating the parent trap; and making permanent the Antideficiency Act exemption for universal service so that annual waivers are not required on appropriations bills on an ongoing basis.

We welcome this morning the views of our witnesses and members of the subcommittee as we seek to broaden the consensus on the reforms that are needed in order to make sustainable the Universal Service Fund.

That completes my opening statement, And I am pleased to recognize at this time for 2 minutes the gentleman from Nebraska, Mr. Terry, for his opening statement.

I might just note, if you will excuse me for a moment, Mr. Terry, for the benefit of our witnesses that our Republican colleagues are having a conference at the moment, and that is urgent business for them, I am sure. And that accounts for the fact that on our side of the aisle we are somewhat better represented here than on the Republican side. But they are embarked, I am sure, on a good mission.

Mr. Terry is recognized for 2 minutes.

[The prepared statement of Mr. Boucher follows:]

STATEMENT OF CONGRESSMAN BOUCHER

Subcommittee on Communications, Technology and the Internet Hearing
Discussion Draft of the Universal Service Reform Act of 2009

November 17, 2009

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Having affordable telephone rates for all Americans is essential to our national well being.

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I hope members will not lose sight of that reality as we consider the reforms needed to ensure the sustainability of the universal service fund.

It's now under tremendous pressure and a comprehensive reform is called for.

New technologies and business models that make local and long distance telephone traffic indistinguishable are combining to diminish the long distance revenues that are relied on to support universal service.

Since the universal service long distance surcharge is being imposed on a declining revenue resource, the surcharge rates are rapidly rising.

Today the contribution rate is 12 percent of long distance revenues. In January, it will rise to a record breaking 14.2 percent, and unless we enact comprehensive reforms, there will be continued escalation after that.

This status quo is not sustainable.

New controls must be placed on costs so that the level of universal service support can be contained.

The bill before us caps the high cost fund, requires competitive bidding for the provision of support to wireless carriers, and imposes rigorous auditing and reporting requirements on the carriers that receive support.

We also expand the contribution base to intrastate services and to entities that provide a connection to the network as a means of relieving pressure on the declining long distance revenue resource.

These changes on both the contribution and expenditure sides should produce a sustainable universal service fund.

The bipartisan discussion draft I have circulated with our Nebraska colleague Mr. Terry results for almost four years of consultations he and I have conducted with dozens of stakeholders.

We have sought and have now achieved consensus among parties that have competing interests.

Our draft bridges the divide on universal service issues between large carriers such as Verizon and AT&T that are net contributors into the universal service fund and the smaller rural carriers that are net recipients of universal service funding.

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Other elements in our measure include a better targeting of support to high-cost areas by switching from statewide to wire center averaging, fixing the phantom traffic problem by requiring carriers to pass through call identifiers, eliminating traffic pumping by prohibiting carriers from sharing access charges with third parties that offer free or reduced-cost services, making rural exchanges more marketable for telephone companies that may desire to sell them by repealing the parent trap and making permanent the Anti-Deficiency Act exemption for USF so that an annual appropriations rider is no longer required for that purpose.

We welcome this morning the views of our witnesses and of members of the Subcommittee as we seek to broaden the consensus on the reforms needed for the universal service fund.

OPENING STATEMENT OF HON. LEE TERRY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEBRASKA

Mr. TERRY. Thank you, Mr. Chairman, for everything.

Reform of the Universal Service Fund has been a long time coming, and, under your leadership and dedication to this issue, I am confident that meaningful reform is within the consumers' reach.

Over 4 years ago, when we set out to introduce the first comprehensive universal service reform bill since 1996, we agreed that the principles and goals of universal service are still as relevant today as they were in the 1930s. However, the USF has failed to keep up with the changing telecommunications landscape, and today's draft legislation is needed more than any time before.

Our draft legislation improves many of the existing USF mechanisms. Specifically, we target USF support to high-cost areas to ensure that USF is meeting its goal of making telecommunication services available to all rural high-cost consumers. The targeting provision is especially important to address the equity issue of ensuring that all customers living in rural America receive the benefits of USF regardless of the carrier that serves them.

The draft legislation also makes broadband a supported service. Including broadband as a supported service is commonsense and brings the fund into the 21st century. For those that fear adding broadband as a support service will subsidize competition, I would like to highlight that the targeting provision in our legislation will move support outside the town centers into the high-cost areas where support is needed the most.

And, finally, I would like to highlight that the draft legislation addresses important issues of cost, accountability, and fairness. The draft legislation broadens the base of contributors while placing a cap on the overall High-Cost Fund. I recognize that the cap has caused some heartburn with some of our witnesses and appreciate your support throughout the process. As the process moves forward, it is my hope that we can continue to work together.

I yield back.

Mr. BOUCHER. Thank you, Mr. Terry.

The chairman emeritus of the full Energy and Commerce Committee, the gentleman from Michigan, Mr. Dingell, is recognized for 5 minutes.

OPENING STATEMENT OF HON. JOHN D. DINGELL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Mr. DINGELL. Mr. Chairman, I thank you. I commend you for holding today's hearing—it is important—and also for you and Mr. Terry in your fine work on the discussion draft of the Universal Service Reform Act of 2009. This is an important piece of legislation.

Due to the explosive growth in the use of Internet and wireless services for communications, the revenues of telecommunications subject to universal service fees have declined, thus leading to increased fees on consumers to allow companies to meet their required universal service contributions.

Lamentably, the Universal Service Fund has not been modified to reflect this market dynamic. And, further, by reason of this inaction, the fund has within denied the necessary streams of revenue

that could be derived from assessments on nontraditional communication providers, such as Voice over Internet Protocol, VoIP, which are now competitive players in the telecommunications industry.

Consequently, now, more than ever, it is incumbent on the Congress to make the necessary changes to the Universal Service Fund's structure so as to preserve as well as to modernize its ability to facilitate the provision for high-quality telecommunication services at affordable rates to all Americans regardless of geography or income.

As I have pointed out in the past, I believe that three principles should guide our efforts in this matter. First, all providers of telecommunications should contribute equitably to support universal service. Second, all communications, and not simply interstate and foreign communications, should be subject to assessments to support universal service. Finally, we should not play favorites with new communications technologies when it comes to Universal Service Fund contribution requirements. This would have the undesirable effect of shortchanging the fund, to which I have just alluded, as well as picking winners and losers in the marketplace. Indeed, it would constitute an exercise in unfairness.

I am pleased that your draft, the Boucher-Terry draft legislation, incorporates these principles. Moreover, in keeping with Chairman Waxman's and my belief that reform in this area should be forward-looking, the draft bill recognizes broadband as a universal service and makes provisions to support the expansion of its infrastructure. In brief, this legislation is a much-needed step in the right direction for universal service reform, and I am proud to extend my support for it.

Mr. Chairman, I thank you for your courtesy, and I commend you for the congenial, bipartisan process that has produced this bill pending before the committee's consideration today. This matter of collaboration has always been a hallmark of this committee's finest work, and I look forward to further improvement to this legislation under your auspices and under these principles.

Thank you, Mr. Chairman, and I yield back the balance of my time.

Mr. BOUCHER. Thank you very much, Chairman Dingell.

The gentleman from Florida, Mr. Stearns, the ranking Republican member of our subcommittee, is recognized for 5 minutes.

OPENING STATEMENT OF HON. CLIFF STEARNS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. STEARNS. Good morning. And thank you, Mr. Chairman. This is a very important hearing. It is nice to see a lot of folks here, a very distinguished group of witnesses here.

I am encouraged that your view towards reforming the broken Universal Service Fund is a high priority. There are many different ideas on how to best achieve this, as we can see from the number of witnesses we have today, so I look forward to their testimony.

The Universal Service Fund needs to be reformed, and quickly, if possible. We can all, perhaps, agree on that one point. The system is fraught with waste, fraud, and abuse. A major overhaul is

necessary. So the question before us is, what are the appropriate goals of the program and, obviously, how do we best achieve that?

The 1996 Telecom Act codified universal service, but the concept goes back decades earlier to a time when there was only one phone company. Now the landscape looks a whole lot different, yet the fund is still administered by outdated rules.

Among the impacts of the growth of the Universal Service Fund have been the growing universal service fees. This contribution factor is a percentage of interstate end-user revenue that telecom companies must pay and changes quarterly, depending upon the needs of the program. Now, in the second quarter of 2000, the fee was 5.7 percent. It has since grown to 12.3 percent. That means that consumers are paying fees in excess of 12 percent of their monthly phone bills. And that fee is expected to go up to 14 percent next year.

Accordingly, there is a need to reform the program away from subsidies that may no longer be necessary as technology and services improve and, of course, become more widespread. Instead, we need to move towards a solution that ensures the goals of universal services but minimizes consumer cost. Throwing additional money at this crumbling program makes little sense at this time.

The purpose of this hearing is to examine the discussion draft of the Universal Service Reform Act of 2009. This draft takes several positive steps towards reform, but it also contains some questionable direction. In particular, it is not clear that this draft restrains costs in any real significant way. In fact, the size of the fund, perhaps, will ultimately increase.

More can and should be done to rein in costs and to improve transparency. First, we need to impose a firm cap to prevent uncontrolled growth in the fund. While this draft bill would cap the high-cost portion of the fund, the cap is subject to several significant exceptions that would grow the fund, in my opinion.

These exceptions include: an annual growth factor; changes to increase support for certain nonrural carriers and carriers that buy other local carriers; and an upward adjustment if the FCC adopts an alternative recovery mechanism for intercarrier compensation revenues that increases demand for Universal Service Fund support.

So, it is not clear how much these exceptions would cost the fund and consumers. The FCC and other sources have given us, recently, an estimate that the changes to nonrural support alone range from an increase of $200 million to $700 million. This is only if no additional carriers request this type of support and if the support is for voice service, not broadband service.

In addition, reforming intercarrier compensation, as this draft would require, could cost upwards of $1 billion. While some of that increase would be offset, I understand, by reductions in other charges, some customers are likely to see their overall phone bills obviously go up.

I think we ought to know the price tag before we start handing out subsidies. So I question the reform that is proposed, and I am hoping that we can find out from our witnesses today how this would work.

Moreover, we need to institute competitive bidding procedures that apply to all carriers. This type of process will help ensure that we are getting the most out of the subsidies. Otherwise, we will continue to see an inefficient use of consumers' money.

We also need to target the money to the places and the people who obviously really need it. Cable companies, for example, suggest that we eliminate subsidies anywhere there is an unsubsidized wireline provider. It certainly seems to make good sense that we eliminate subsidies where the market has demonstrated clearly service can be offered without subsidies.

So, again, thank you, Mr. Chairman, for holding this hearing. It is important to examine the goals, and I look forward to hearing from our witnesses.

Mr. BOUCHER. Thank you, Mr. Stearns.

The gentleman from Massachusetts, Mr. Markey, is recognized for 2 minutes.

Mr. MARKEY. Thank you, Mr. Chairman.

It is long overdue that we fix the bloated system that likely overpays eligible telecommunications carriers more than what is warranted. When approaching reform proposals, I believe that we should harness advances in technologies and insist on administrative efficiencies to first drive down costs and create savings wherever and whenever possible. And, second, we must also shift over time to more rational, stable sources of funding while embracing broadband as a supported service.

Broadband will be indispensable in the 21st century. It will provide our ability to be able to manage energy-efficiency technologies, lower health-care costs, along with other social and economic benefits. And that is why I successfully amended the American Recovery and Reinvestment Act in February and required the FCC to develop a national broadband plan for the country that is due next February.

While the U.S. lags behind other countries in the world in several key broadband metrics, there is one area where the United States leads the world: connections to classrooms. Why? Well, because in the 1996 Telecom Act we had a plan. As the primary House author of the E–Rate program in that landmark bill, I have seen firsthand what we can do when we actually have a plan. And the 90-percent-plus of classrooms today connected to the Internet is testimony to a forward-leading approach.

With the national telecommunications broadband plan, the Federal Communications Commission has a chance to give the country a blueprint for our broadband future. I urge the Commission to give a plan to us that is practical but consistent with our history of tackling the big infrastructure challenges with big ideas and a commitment to action.

Without question, any national broadband plan focused on deployment to all Americans and on addressing affordability must include universal service and related issues of intercarrier compensation as a key ingredient. I congratulate Chairman Boucher and Mr. Terry for their work on this issue.

And I yield back the balance of my time.

Mr. BOUCHER. Thank you very much, Mr. Markey.

The gentleman from Illinois, Mr. Shimkus, is recognized for 2 minutes.

Mr. SHIMKUS. Thank you, Mr. Chairman.

It is good to see so many friends here. And I applaud you and Lee for your bulldog approach to this.

The Universal Service Fund should always be about the customers, not the companies. And I focus on bringing broadband to the rural areas, and I think there has been a lot of support for that. I agree, we need to target waste, fraud, and abuse. And we need to legislate, and we do not need the FCC to regulate on this.

On a side note, I don't want to throw a wrench in this whole debate, but, as we focus on pushing out, I hope, broadband connectivity to places that don't have it, or high-speed, this Net neutrality debate could come in here because it could change the business plan. And so, it is not explicitly written in this bill, but it is of concern that if we cannot make a decision on issues like telemedicine, then you have another problem with the whole Net neutrality debate.

And I yield back my time.

Mr. BOUCHER. Thank you very much, Mr. Shimkus.

The gentlelady from California, Ms. Eshoo, is recognized for 2 minutes.

Ms. ESHOO. Thank you, Mr. Chairman, for holding this hearing and providing us with your discussion draft of the Universal Service Reform Act of 2009.

The draft is a springboard for a healthy discourse on the next step for the fund. And we have held more than a few hearings on this subject, and I think that it is time to develop a workable piece of legislation.

I welcome all the witnesses and, certainly, Mr. Rosston, who is a constituent and a good friend. It is wonderful to see you here.

There are myriad range of problems with the Universal Service Fund based, in part, on changes in the telecommunications industry. In 1996—which is only 13 years ago in regular years, but in telecommunications years it might as well be a century. During that time, we have seen a virtual explosion of new services and products.

The current system reflects the mid-20th century's telecommunications economy, when long-distance calls were defined as distinct from local calls and classified as a more expensive service. This is the age of broadband and mobile telephony, and national and international packages have made this system a relic fit for the national history museum.

The program as it now stands is inefficient and fragmented, with episodes of corruption. But we know that the fund would cost too much even if its administrative problems are solved because the ways it collects revenue and compensates vendors doesn't make sense anymore.

We heard arguments at our last hearing about the need for change and whether that change should come in the form of a reverse auction or request for proposals when picking recipients. We heard ideas about how to fix intercarrier compensation and the identical support rule. A discussion draft should take us to the next level, to concrete solutions. I think it is time to integrate broadband

into the fund base for contribution purposes, and I am pleased that the draft bill does so.

But I am concerned about issues related to minimum speed and broadband rollout. I signed on to Congresswoman Matsui's bill because I want to discuss the next steps for utilizing the fund to support broadband access. Unfortunately, the bill before us does not address the Low-Income Lifeline Program that would support universal broadband deployment under Ms. Matsui's bill. So I am interested in alternative methods that you would have for addressing this issue.

It also does not discuss the Schools and Libraries Program. That leaves a lot out of the equation. Schools and libraries are our anchor institutions, and I have voiced my concern for funding their broadband access. And the last mile of broadband needs to go to urban as well as rural areas quickly, both in terms of time and speed.

So I look forward to working on the bill, Mr. Chairman, with you and Mr. Terry, on developing this important piece of legislation that, I believe, needs to be comprehensive and holistic in its approach.

And I yield back.

Mr. BOUCHER. Thank you very much, Ms. Eshoo.

The ranking Republican member of our full committee, the gentleman from Texas, Mr. Barton, is recognized for 5 minutes.

OPENING STATEMENT OF HON. JOE BARTON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. BARTON. Thank you, Mr. Chairman.

I want to thank all of our witnesses.

I think we need a few more, Mr. Chairman. I don't think you have quite covered the total spectrum. My next-door neighbor wasn't invited, and we need to get them out here.

I am going to submit my opening statement for the record.

To put it in terms that average people understand, I like the bill. I am ready to take you to the prom, but I am not ready to marry you. You know? There is still work that needs to be done, cosmetic touchups, you know, a little better attitude maybe. But you are on the right track, Mr. Chairman.

It is obvious that the fund is broken. I mean, you know, more people have cell phones than have hardline phones. The United States is the most wired country in the world. Those of us that have all the ideocentric laws that we have to deal with have two BlackBerrys, three cell phones, plus all the hardline phones.

At my condo here in Washington, in Virginia, I basically just have a phone there to have a phone in case there is some emergency or something. My USF fee is probably 20 to 30 percent of my bill because I pay the absolute minimum each month. I just think that is not appropriate.

You and Mr. Terry's bill, which you have worked with me on and Mr. Terry has worked with me on, I really, really want to support. But it does concern me that, under this bill, the size of the fund could actually increase and not decrease. I think we need a firm cap. Obviously, that is something that we need to work on or discuss.

There are some things that we could do that are not in the bill to make it more competitive in the service fund. I think it is ridiculous that some areas have 30 different phone companies that get subsidies. I don't buy that. I can buy two, maybe, or three for competitive purposes, but 30? I just think that is wrong.

And while you and I have discussed this at some length, having a mandate is a difficult concept for somebody like me to swallow for broadband. I am not saying it is—it may not be appropriate, but it is something that I have to think about.

So, overall, great prom date, marriage proposal possible.

And, with that, I yield back, Mr. Chairman.

Mr. BOUCHER. Well, thank you very much, Mr. Barton. Given the distance that we have traveled, a prom date is good enough for today, and I am happy to get the invitation.

The gentleman from Pennsylvania, Mr. Doyle, is recognized for 2 minutes.

Mr. DOYLE. Thank you, Mr. Chairman. I am still trying to get that image of Mr. Barton taking you out to the prom out of my head.

Mr. BARTON. That is just metaphysical. It is not literal.

Mr. DOYLE. Even that is scary.

Thank you, Mr. Chairman, for holding this hearing. I am pleased that you are holding a hearing on your bill to reform the Universal Service Fund.

I think we have to rethink what "universal service" means and how the Universal Service Fund implements these goals. I have said many, many times that we need an overhaul for the broadband age, a "Universal 2.0." "Universal Service 2.0" shouldn't build on the current structure just because it is what we have. That structure should undergo a thorough review to make sure that every dollar spent is a dollar that the private sector isn't competing against and that every dollar spent enables low-income consumers to choose the communication services they need.

I think the bill takes a number of steps in the right direction, but I have some concerns that I believe have to be addressed before I can support it. Today, my constituents pay a lot of money into that fund, and I want to make sure that the fund just doesn't take from those in urban areas just to hand it over to rural areas who are capable of paying for themselves.

I think that Ms. Matsui's bill that allows for low-income Americans to qualify for a broadband lifeline subsidy is a good start, and I intend to add my name as a cosponsor.

However, although it is critically important in many cases, monthly price isn't always the biggest reason that people aren't online at home. There is the other program, Link-Up, that needs to be addressed also in "Universal Service 2.0," because there are other barriers, like access to a computer or even a lack of understanding the benefits of broadband.

Some people suggest that we shouldn't be subsidizing telephone service for upper-income communities in areas like Aspen, Colorado. Perhaps we need to consider legislation that will move the Universal Service Fund to a voucher system for low-income consumers that will allow them to communicate in the ways that they

want to. I am interested in learning if that is a viable solution to meet the goals of "Universal Service 2.0."

I look forward to hearing from our panelists today, and I look forward to asking some questions, Mr. Chairman. Thank you.

Mr. BOUCHER. Thank you very much. I appreciate your comments this morning.

The gentlelady from Tennessee, Mrs. Blackburn, is recognized for 2 minutes.

Mrs. BLACKBURN. Thank you, Mr. Chairman. I do thank you for the hearing. I know that you and Mr. Terry are hard at work on this issue.

And I want to say welcome to all of our visitors here today. It looks like, with the large number of you, we are going to be spending the day together talking about this issue. But I am glad that you are here.

And I hope that, as we go through this hearing today, that we are going to touch on a number of issues that really need to be addressed: the intercarrier compensation, competitive bidding, caps on the USF distribution, the reverse auctioning, cost of this to the consumer. Several of us have mentioned these, and, as you know, they are of concern to us.

I am concerned that the legislation in its current form is—we are not really addressing hitting the problems that we are hearing from our constituents. We are just not hitting them head-on. And I think the American people have grown ill and fatigued of lots of talk. They want to see some action on some issues.

I am hearing from some of my constituents who would be affected by this, why is it not going to dramatically increase access or improve access? Exactly what is going to happen with the broadband plan and expansion; how are you going to handle that?

Mr. Shimkus mentioned Net neutrality. I term it "fairness doctrine for the Internet." Indeed, there is concern about complications and how that would be handled.

People are concerned that we put taxes on the books and then we don't take taxes off the books, but we cannot always define what is a better use or a fair distribution for those taxes.

So there is plenty for us to look at and talk about. And I do hope we are going to have some good common sense coming from all of you.

I want to say a special welcome, Mr. Chairman, if I may, to Mr. Greer, who is from Tennessee and is someone that I enjoy my conversations with when we talk about how this affects our rural areas and as we look at the telecommunications issues in the rural areas.

I also want to say a special welcome to Mr. Graham, who graduated from Mississippi State University and, like me, a fellow bulldog. Looking at you, I can tell you were there much later in life than was I and that you probably graduated many years after I had left. But welcome. We are glad you are here.

I yield back.

Mr. BOUCHER. Thank you, Mrs. Blackburn.

The gentlelady from California, Ms. Matsui, is recognized for 2 minutes.

Ms. MATSUI. Thank you, Mr. Chairman. And thank you very much for holding this hearing today on reforming the Universal Service Fund. I would also like to commend your efforts to expand broadband access to more Americans in your draft USF reform legislation.

And I would like to thank the witnesses for joining us today.

I would also like to thank Ms. Eshoo and Mr. Doyle for their supportive comments on my Broadband Affordability Act.

In today's economy, the Internet has become a necessity, not a luxury. Americans need it to obtain emergency information for educational purposes, to find low-cost health-care options, and to seek employment assistance. In fact, about 75 percent of all large U.S. employers now require applicants to apply online, creating a significant disadvantage for those without broadband.

We need to not only expand broadband access but also to address the fact that millions of Americans simply cannot afford to pay up to $60 a month for broadband. A recent ITIF study found that 96 percent of Americans have access to broadband services, while less than 65 percent actually subscribe.

Other current prominent studies by the Pew Institute and PPIC have strongly suggested that broadband adoption rates are largely associated with income. Lower-income families in urban and rural areas are severely disadvantaged in large part by the lack of access to affordable broadband services.

To help close the digital divide, I have introduced the "Broadband Affordability Act," which would direct the FCC to create a program for universal broadband adoption similar to the current USF Lifeline assistance program. The bill will ensure that lower-income Americans living in urban and suburban and rural areas all have access to affordable broadband services. In doing so, households who currently possess broadband options but have not subscribed because of cost would no longer be unserved or underserved.

It is my hope that any USF reform legislation helps bridge this Nation's digital divide by addressing affordability barriers.

I look forward to working with Mr. Chairman and Mr. Terry and all my colleagues, looking forward. And I yield back the balance of my time.

Mr. BOUCHER. Thank you very much, Ms. Matsui.

The gentleman from Oregon, Mr. Walden, is recognized for 2 minutes.

Mr. WALDEN. Thank you very much, Mr. Chairman.

The topic of today's hearing, Universal Service Fund reform, is one that it appears everyone has something to say about, judging by the panel of 10 witnesses. And we welcome you all. This is a complex matter, So I appreciate your assembling such a thorough complement of witnesses, Mr. Chairman. This should be most helpful.

It isn't often that there are two Oregonians in the room for one of our subcommittee hearings, but today is one of those times. And I welcome my friend, Ray Baum, who is commissioner with the Oregon Public Utility Commission and chair of the National Association of Regulatory Utility Commissioners' Committee on Telecommunications.

Wearing both these hats and as the State chair of the FCC's Joint Board on Universal Service, Ray will share his insight with us on USF reform. And I appreciate his testimony, which I read through last night.

During my years as a State legislator, I worked alongside Ray, and I found his perspective to be both thoughtful and comprehensive. And I am pleased that he is here to help this subcommittee in its efforts to reform the USF.

Congress continues to discuss the issue of ubiquitous broadband deployment and how best to achieve it. The FCC, USDA, and Commerce Department are engaged in this topic, as well. With the Nation's unemployment rate at a 26-year high, Oregon's unemployment rate at 11.3 percent, and some counties in my district pushing 20 percent, the economic development potential that broadband service provides cannot come fast enough.

I am interested to learn more about the implications, however, of using USF to support broadband service. I would like to hear from our witnesses about how this would functionally work in a district as rural as mine that has several counties with population densities less than one person per square mile. If you overlaid my district over the East Coast, it would start at the Atlantic and end in Ohio.

I realize that none of our witnesses here today can speak to specific problems within, for example, the USF Schools and Libraries Program. However, I would like the hearing record to reflect that we should address the challenges that applicants face in navigating this very complex program. My office has been working with the Baker County, Oregon, library district for a year and a half on delays it has experienced with receiving E–Rate funds. If it is the intent of the USF program to support schools and libraries through the E–Rate program, then let's make sure it functions properly and remove roadblocks which cause applicants to give up completely on that program.

So I welcome the witnesses here today, and I yield back my time.

Mr. BOUCHER. Thank you very much, Mr. Walden.

The gentlelady from the Virgin Islands, Mrs. Christensen, is recognized for 2 minutes.

Mrs. CHRISTENSEN. Thank you, Chairman Boucher. And thank you and Ranking Member Stearns for holding this hearing to receive testimony on the draft of the Universal Service Fund act.

I also want to commend you, Mr. Chairman and Congressman Terry, for your work in drafting the bill and your long-term legislative efforts to try to keep the Universal Service Fund program in sync with a rapidly changing technology landscape.

I am pleased that today we will have an opportunity to have a meaningful discussion of the issues that are important to reforming the USF, including the overall budget for the High-Cost Fund, new contribution methodology, and expanding the USF support broadband adoption, among others.

I think everyone is in agreement on the need for reform but also on preserving the intent codified in the 1996 act, which is to provide affordable telecommunication services across the United States.

As a representative of a district that is a high-cost, insular area which reportedly received an estimated $22.5 million in high-cost support in 2007, we have benefited from the program. However, in some areas, like the Virgin Islands, funding has been declining for wireline carriers, which represents a serious threat to the need for increased investment in the telecommunications infrastructure in rural areas. It is important that places like the Virgin Islands, rural areas with minimal-level competition and a small market, that they are not left out or left behind or underserved by this critical industry.

So I look forward to our discussion today on challenges to reforming and taking the USF into the 21st century. And I want to welcome the panelists, and look forward to the testimony and their views on the bill.

Thank you.

Mr. BOUCHER. Thank you very much, Mrs. Christensen.

The gentleman from Missouri, Mr. Blunt, is recognized for 2 minutes.

Mr. BLUNT. Thank you, Mr. Chairman.

I have a statement for the record. Let me just quickly summarize that statement, which is really: How do we bring down the rapidly growing cost to customers, to consumers here? The whole topic of unserved versus underserved is of concern to me. And how do we control the cost of the program? And is the definition of "underserved" and "served" part of that?

And I will submit my full statement for the record, Mr. Chairman. And thank you.

[The prepared statement of Mr. Blunt follows:]

Blunt Statement on Subcommittee on Communications, Technology, and the Internet Hearing on Universal Service Fund Reform
November 17, 2009

Mr. Chairman:

Thank you for holding this hearing on this important issue. I think our large panel of witnesses can teach us a lot about the Universal Service Fund and offer some insights on the piece of legislation that you are working to introduce.

Every American who has a phone or an internet connection has a stake in the outcome of legislation to reform the Universal Service Fund. This fund, which is nominally intended to ensure that phone service is available in rural areas or areas that are too costly for a service provider to build into, has ballooned in cost to consumers. This fund reminds us that, whatever the good intentions of a government program, we must always be mindful of its costs and its effectiveness. I think it's hard to find anyone who believes this particular government subsidy isn't in serious need of reform.

I applaud you, Mr Chairman, as well as my friend Mr Terry for crafting a draft piece of legislation that examines both the costs of the program and its effectiveness. I want to work with both of you moving forward to see if this is the right bill that resolves the structural deficiencies of the USF while reining in costs and staying true to the original intent of the program and, if not, what work we can undertake to improve it.

I'm interested in learning three important things from our witnesses today, although I'm sure there will be plenty of useful ground covered:

First, how does the draft legislation impact a company's willingness to build-out into unserved areas? Will the legislation, as it's written, duly target areas of the country that are truly unserved? Or will it provide more subsidies to companies to compete with unsubsidized entities that are already serving areas that are considered "underserved?"

Second, how does this bill rein in costs? With the cost of the program nearing 14% of a subscriber's monthly phone bill, how do our panelists anticipate these costs being controlled in the future? Will the "soft cap" on wireline service be sufficient to rein in costs, or will exceptions negate the bill's savings?

Three, will the bill's efforts to open up broadband to universal service fees be a net gain or a net loss for consumers? I'm concerned that billing consumers on their broadband service could spread the cost of the program around without actually saving them money if we're not careful.

With all that in mind, Mr Chairman, I'll reiterate that I believe your bill is a good faith effort to reach across the aisle and work with a respected member of our committee, Mr Terry, on fixing a government program badly in need of reform. I'm hopeful that today's hearing is a productive opportunity to learn more about the specific impacts of the bill and I'll look forward to working with you and other members of the subcommittee on this issue as we move forward.

Mr. BOUCHER. Thank you very much, Mr. Blunt.

The gentlelady from Florida, Ms. Castor, is recognized for 2 minutes.

Ms. CASTOR. Good morning. Thank you, Mr. Chairman, for holding this important hearing and for the progress that you and Representative Terry have made in beginning to craft a bill.

My State of Florida has a particular interest in universal service reform because, out of all the States in the Union, Florida is the single largest contributor to the fund. In 2007, Florida consumers made a net contribution of $297 million to the Universal Service Fund. Floridians paid in about $480 million and received $180 million of that back in support, largely, for schools and libraries.

The overriding goal of the USF is laudable, but it is unclear that the draft adequately addresses inequities in distribution or modernizes the USF with concepts like those contained in Congresswoman Matsui's bill relating to broadband and low-income consumers.

Florida's disproportionate contribution has only been exacerbated by the out-of-control growth in the High-Cost Fund. So I am pleased that the discussion draft contains a cap on the High-Cost Fund and other measures to hold down the growth in the fund.

I am interested in the witnesses' opinions regarding the auction mechanisms and whether such auctions will be effective in reducing the growth in wasteful and duplicative spending that has been driven by the identical support rule.

And, Mr. Chairman, prior to markup, it would be helpful to see an analysis, monetarily, of the effect of these changes. Several of the changes proposed in this bill have the potential to further grow the fund. And, while I understand the importance of some of these changes, I do not believe we should expand the fund except in the context of a solution to the inequities in the contribution and distribution methodologies that exists today.

Thank you, and I look forward to the testimony of the panel.

Mr. BOUCHER. Thank you very much, Ms. Castor.

Is Mr. Buyer here? No, he has not arrived.

The gentleman from Michigan, Mr. Stupak, is recognized for 2 minutes.

Mr. STUPAK. Mr. Chairman, I will waive and ask for an extra 2 minutes for questions.

Mr. BOUCHER. Thank you, Mr. Stupak. Two minutes will be added to your questioning time.

The gentleman from Ohio, Mr. Space, is recognized for 2 minutes.

Mr. SPACE. Thank you, Chairman Boucher and Ranking Member Stearns, for convening today's hearing.

I would also like to thank our witnesses for taking their time to be here today, as well.

Mr. Chairman, I applaud your efforts, along with those of Mr. Terry, to reform the Universal Service Fund through the draft legislation that we are considering today. As I have shared many times before, the 18th Congressional District is largely rural. Fourteen of my 16 counties are within Appalachian proper. And, that said, we are the poster child for the Universal Service Fund support.

Many of our towns are small, insular, and expensive for providers to serve, and much of my district, consequently, lacks access to broadband. And as my colleague from Oregon stated, this has an extremely significant effect on our economic development and the potential afforded by the advent of new and diverse technology.

It also has an extremely detrimental effect on our ability to deliver health care and education. What we are seeing now is really the beginning of the integration of technology into those processes, and we can no longer afford to remain so far behind in such a vital area.

I am extremely pleased to see that Chairman Boucher and Congressman Terry's draft bill explicitly authorizes the coverage of broadband under the Universal High-Cost Fund. I believe that, coupled with the investment we have made through the American Recovery and Reinvestment Act, we are on the path to ensuring that Americans everywhere, regardless of how rural their hometown is, may have equitable access to vital infrastructure.

I further support the efforts of my colleagues to restore some accountability and cost containment to the Universal Service Fund through sensible auditing and oversight provisions and through capping the fund with built-in accommodations for future changes.

I look forward to continuing to work on Universal Service Fund reform with my colleagues on this committee. And I think we all agree that such reform is long past overdue and that rural areas of our country have, in the meantime, gone shortchanged.

Thank you, and I yield back.

Mr. BOUCHER. Thank you, Mr. Space.

The gentleman from Vermont, Mr. Welch, is recognized for 2 minutes.

Mr. WELCH. Thank you. I am going to reserve my time.

Mr. BOUCHER. That is fine. Thank you, Mr. Welch.

The gentleman from California, Mr. McNerney, is recognized for 2 minutes.

Mr. MCNERNEY. Thank you, Mr. Chairman. I will waive my opening statement.

Mr. BOUCHER. Thank you, Mr. McNerney.

The gentleman from North Carolina, Mr. Butterfield, is recognized for 2 minutes.

Mr. BUTTERFIELD. Let me thank you, Mr. Chairman, for your outstanding work on this issue and for the work you and your staff have put into developing your Universal Service Reform Act discussion draft.

As a member of this committee who represents a particularly rural district in my State of North Carolina, I am acutely aware of the need for the USF and to ensure telecommunication services are made available to the high-cost remote areas of our country. At the same time, should we do nothing to reform USF, we put ourselves on an unsustainable path, a path that already projects the contribution factor rising to over 14 percent in the coming year.

I am pleased to see much-needed provisions addressed in the Boucher-Terry universal service draft, including requiring USF recipients to include broadband Internet access; broadening the base of contributors to help bring down the rising contribution factor; directing the FCC to address the intercarrier compensation system;

and targeting support to rural wire centers as opposed to a formula based on statewide averaging. And these are steps in the right direction. And I look forward to hearing the comments from the witnesses before us today and also from my colleagues about these and other proposals.

Finally, I remain particularly interested in the comments of Dr. Rheuban regarding much-needed reforms in the Rural Health Care Program. That is very special to me. We have not been able to achieve the full effectiveness of this program, and I look forward to discussing how the addition of broadband services in USF will potentially enhance broadband telehealth infrastructure and deployment in the Rural Health Care Program. I have been an advocate of telehealth and telemedicine, and I believe these health-care delivery tools will be vital in rural communities across America.

And so I want to thank the 10 witnesses. I sat here and counted all of you. I want to thank the 10 witnesses on the panel, and I look forward to hearing your testimonies today.

I yield back.

Mr. BOUCHER. Thank you, Mr. Butterfield.

The gentleman from Washington State, Mr. Inslee, is recognized for 2 minutes.

Mr. INSLEE. Thank you. And I will pass. Thank you, Mr. Chair.

Mr. BOUCHER. Thank you, Mr. Inslee.

All members now having had an opportunity for opening statements, we welcome our panel of witnesses. And we thank each of you for taking time to join us here this morning.

I will say just a brief word of introduction about our witnesses today.

Mr. Peter Davidson is senior vice president of public affairs, policy, and communications for Verizon.

Mr. Leslie Greer is the chief executive officer of DTC Communications, testifying this morning on behalf of the National Telecommunications Cooperative Association, a very large organization representing rural carriers.

Mr. Michael Rhoda is the senior vice president for government affairs at Windstream Communications.

Mr. Joel Lubin is a vice president of public policy for AT&T Services, Incorporated.

Ms. Catherine Moyer is the director of legal and regulatory affairs for Pioneer Communications, testifying today on behalf of OPATSCO.

The Honorable Ray Baum is a commissioner of the Oregon Public Utility Commission, testifying today on behalf of NARUC.

Kyle McSlarrow is president and chief executive officer of the Cable Television Association.

Mr. Eric Graham is vice president of government relations at Cellular South, Incorporated, testifying today on behalf of the Rural Cellular Association.

Dr. Karen Rheuban is a professor of pediatrics and the medical director of the Office of Telemedicine at the University of Virginia Health Systems. She also serves as president of the American Telemedicine Association and as board chair of the Virginia Telehealth Network.

Mr. Gregory Rosston is a deputy director at the Stanford Institute for Economic Policy Research at Stanford University.

Without objection, all of your opening statements will be made a part of the record, and we would encourage your oral summaries. And, given the number of you this morning, we would ask that you try to hold those statements to approximately 5 minutes.

Mr. Davidson, we will be happy to begin with you.

STATEMENTS OF PETER DAVIDSON, SENIOR VICE PRESIDENT OF PUBLIC AFFAIRS, POLICY, AND COMMUNICATIONS, VERIZON; LESLIE GREER, CHIEF EXECUTIVE OFFICER, DTC COMMUNICATIONS; MICHAEL RHODA, SENIOR VICE PRESIDENT FOR GOVERNMENT AFFAIRS, WINDSTREAM COMMUNICATIONS, INC.; JOEL LUBIN, VICE PRESIDENT OF PUBLIC POLICY, AT&T SERVICES, INC.; CATHERINE MOYER, DIRECTOR, LEGAL AND REGULATORY AFFAIRS, PIONEER COMMUNICATIONS; HON. RAY BAUM, CHAIRMAN, NARUC COMMITTEE ON TELECOMMUNICATIONS, STATE CHAIR, FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE, COMMISSIONER, OREGON PUBLIC UTILITY COMMISSION; KYLE MCSLARROW, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL CABLE AND TELECOMMUNICATIONS ASSOCIATION; ERIC GRAHAM, VICE PRESIDENT OF GOVERNMENT RELATIONS, CELLULAR SOUTH, INC.; KAREN RHEUBAN, SENIOR ASSOCIATE DEAN FOR CME AND EXTERNAL AFFAIRS MEDICAL DIRECTOR, OFFICE OF TELEMEDICINE, UNIVERSITY OF VIRGINIA; AND GREGORY ROSSTON, DEPUTY DIRECTOR, STANFORD INSTITUTE FOR ECONOMIC POLICY RESEARCH

STATEMENT OF PETER B. DAVIDSON

Mr. DAVIDSON. Thank you. Good morning, everyone. Thank you, Chairman Boucher, Ranking Member Stearns, and members of the committee. Thank you for the opportunity to address the committee this morning on the new Universal Service Reform Act of 2009 circulated recently by Chairman Boucher and Mr. Terry.

This committee has always been a leading voice on universal service reform, and today we endorse the Boucher-Terry legislation because we believe it embraces policies to reform and sustain the fund. It directs funds to meet the true communications needs of consumers. We will continue to work with the sponsors and this committee to ensure that this legislation accomplishes the objectives of modernizing the universal service program so that it meets the needs of Americans in the 21st century.

In the past decade, the communications industry has invested hundreds of billions of dollars in private capital to deploy new, innovative broadband technologies. Recently, Congress passed mapping legislation, funded broadband grants for unserved areas, and now we have a full complement of FCC commissioners focusing on broadband adoption and deployment policies.

Encouraging deployment and adoption of next-generation networks will keep America competitive in our global economy and will help address some of our most pressing challenges, such as health-care reform, education, and energy conservation.

We also believe that there should be a role for the Universal Service Fund related to broadband. But right now the fund is in trouble and, left unchanged, is in no shape to contribute to the broadband solution. The USF contribution factor is near an all-time high and, just to pay the fund at today's levels, as everyone has noted this morning, is projected to rise again next year to more than 14 percent. When added to other communications charges and fees, these assessments really hit consumers hard, especially in these economic times, and this trend is simply unsustainable.

The problem with universal service is not that we spend too little money; it is that we do not spend it on the right services in the right places. We cannot put off any longer the tough choices on major issues. We must fix the broken universal service framework before layering on additional priorities.

Verizon supports the draft Universal Service Reform Act because it takes a big step toward addressing five of the most pressing issues: one, an overall budget for the High-Cost Fund; two, a contribution methodology; three, competitive bidding for wireless support; four, a date certain for related reform of intercarrier compensation; and, five, an end to traffic pumping.

Allow me to briefly—and I will be brief—address each of these points.

First, the bill recognizes the need to set an overall budget for the High-Cost Fund. This is important because consumers pay for the fund, and consumers have limited resources. The High-Cost Fund is already at a tipping point, having grown to about $4.5 billion from less than $3.5 billion only 5 years ago while the assessable revenue base declines rapidly. Without some restraint, the USF contribution factor will surely rise to 15 percent, perhaps even 20 percent or more. We simply must have the discipline at the outset of any overhaul of the High-Cost Fund to define some reasonable funding boundaries.

Second, the way that we fund the fund, through an assessment on interstate revenues, is a mess. This system may have worked in the days of one network and only two services—local and long-distance calls—but it is not practical with the converged, any-distance services consumers expect today. The draft bill acknowledges the need to update the universal service contribution system and would commit the FCC to take a hard look at an alternative contribution system. For many reasons, the best contribution method is one mentioned in the bill, a flat charge on each working phone number, to pay for all or part of the USF contribution base.

Third, a competitive bidding system is the best way to distribute high-cost support to wireless carriers. The draft bill recognizes the benefits of this market-based approach and sensibly puts in place a forward-looking competitive bidding system to support and expand the reach of wireless networks. The FCC will need to address quality-of-service requirements and rules in a competitive bidding system, but that is manageable through legally enforceable contracts signed with those wireless carriers that win the bid to provide service in high-cost areas, just as the Federal Government does in hundreds of procurement areas to ensure quality of goods and services.

Fourth, we must fix the broken intercarrier compensation system at the same time that we update the Universal Service Fund. All that is needed is the resolve to get this done. And the draft Universal Service Reform Act requires the FCC to act on intercarrier compensation reform within 1 year. That is certainly workable.

And, fifth, we have to stop the so-called "traffic-pumping schemes" that have plagued the industry the last several years. The draft Universal Service Reform Act would help do that by making it illegal for traffic pumpers to charge other carriers for access on traffic subject to those revenue-sharing agreements.

Mr. Chairman, with your and the committee's leadership, the Universal Service Reform Act, we can get the fund back on the path of sustainability and focused on meeting the telecommunications needs of our country. And I thank you for the opportunity to testify here this morning.

[The prepared statement of Mr. Davidson follows:]

Prepared Testimony of Verizon Senior Vice President Peter B. Davidson
U.S. House of Representatives Committee on Energy and Commerce,
Subcommittee on Communications, Technology, and the Internet
"Universal Service Reform Act of 2009"
Tuesday, November 17, 2009

Chairman Boucher, Ranking Member Stearns, and Members of the Committee: Thank you for the opportunity to discuss reform of the Universal Service Fund (USF) and the new Universal Service Reform Act of 2009 circulated recently by Chairman Boucher and Representative Terry. The Committee has always been a leading voice on universal service policy, and this legislation is a good starting point to put policies in place to sustain USF and direct the funds it collects to the real communications needs of consumers.

Over the past year, there has been a great deal of discussion about the importance of innovative wireline and wireless communications networks and services to consumers. We also have talked a lot about encouraging deployment and adoption of next generation networks and discussed how these networks will help keep America competitive in our global economy and address some of our most pressing challenges, such as health care reform, education, and energy conservation.

These are all critical goals, and, with the help of the Committee, we have made great progress with policies that will result in the ubiquitous deployment of wireline and wireless broadband networks: Congress passed mapping legislation last year and the economic stimulus bill this year. And we now have a full complement of FCC commissioners, all of whom are committed to a broadband agenda and are working hard on creating a national broadband plan.

In achieving the overarching and worthy goal of bringing broadband to everyone, we now have different tools to address different facets of this challenge. We should ensure that those funds and programs targeted for broadband mapping, deployment, and adoption have a chance to work. We will

then need to figure out what worked well, where we still have challenges, and what solutions are best suited to getting all Americans access to broadband services.

There will no doubt continue to be an important role for the Universal Service Fund to play going forward. But right now the fund is in trouble and in no shape to contribute to the broadband solution. The high cost fund is literally at a tipping point – having grown from $3.5B to $4.5 billion in only five years. At the same time, the revenue base which funds USF is shrinking rapidly – declining almost $2 billion dollars between fourth quarter 2008 and fourth quarter 2009. As a result, the USF "contribution factor" is near an all-time high and is projected to rise again the first quarter of next year to *more than 14%* just to pay for the fund at today's level. These fees are really hitting consumers hard, especially in these economic times, and this trend is simply unsustainable.

The problem with universal service is not that we are spending too little money; it's that we are not spending it on the right services in the right places. We cannot put off the tough choices on the major issues any longer. We have to fix the broken universal service framework before layering on additional priorities, broadband or otherwise. The draft Universal Service Reform Act takes us a big step forward by addressing five of the most pressing matters:

- An overall budget for the high cost fund;
- A new contribution methodology;
- Competitive bidding for wireless support;
- A date certain for related reform of intercarrier compensation; and
- An end to traffic pumping.

Allow me to address each of these issues.

The draft Universal Service Reform Act would bring broadband directly into the universal service fold. Broadband creates quality jobs and increases the competitiveness of the communities it reaches; makes it easier for citizens to engage with their communities and government officials; and helps to address critical social challenges like healthcare, education, and energy efficiency. So it makes sense to provide some kind of targeted support for broadband in unserved areas. If we make broadband part of the Universal Service Fund, however, we have to figure out a way to create a smart and sensible relationship between the two.

The essential first step is to set a budget for high cost universal service funding. This seems simple, and it is. It's no different than, for example, buying a car. Nobody would sign an agreement to buy a new car with all of the latest features automobile technology can offer without knowing the price of the car. Likewise, we cannot ask consumers, who contribute to the fund through charges on their bills, to write a blank check to pay for a redesigned high cost program. Some suggest that any limit on high cost funding could be harmful to consumers in rural America. Just the opposite is true. A high cost program with no ceiling would harm rural America. Consumers in rural areas pay for the Universal Service Fund just like everybody else. It's their money, and if the fund grows, they will pay more. Policymakers should appropriately balance the obligation to fund service in high cost areas with the need to ensure that the fund is sustainable for everyone.

The debate is not theoretical. We know from the sea change in communications technology and services over the last few years that only imagination constrains the potential for new, better, and faster services. And we also know from the tremendous growth in the high cost fund over the same period that the USF is not suited to meet the demands of its existing programs, much less new broadband programs. Without some restraint the USF contribution factor will surely rise to 15%, even 20% or more. We simply must

have the discipline at the outset of any overhaul of the high cost fund to define some reasonable funding boundaries.

Second, the way we "fund the fund" through an assessment on interstate revenues from telecommunications services is a mess. This system may have worked in the old days of one network and only two services – local and long distance voice calls – but it's not practical with the converged, any-distance services consumers expect today. The draft Universal Service Reform Act acknowledges the need to update the universal service contribution system and directs the FCC to figure out the best way to pay for the fund.

It is particularly important to get the USF contribution system right in the broadband era. The current system is another example of how technology can outstrip regulation. A contribution system based on revenues derived from particular types of services will always produce competitive inequalities. For example, so-called "over-the-top" VOIP providers such as Vonage did not pay into the USF until 2006. Today, Google Voice is not paying into the fund. And tomorrow there will be another next-generation service that competes with assessable services for the same customers but does not pay into the fund. This situation skews the market by delivering a double blow to services that pay into the fund. Not only do these services have to pay USF themselves, they also have to "make up" for the contributions that the fund loses from migration to certain next-generation products that do not fit into the current contribution system. The system is not equitable for anyone, and it must be changed.

The current contribution system also is not practical. The system is based on the erroneous notion that it is possible in today's world to distinguish between interstate and intrastate services and between telecommunications and information services. Only interstate telecommunications services pay USF. But these distinctions are withering away, and we cannot pretend that they do just for universal service contribution purposes. Today, consumers buy many different

communications services from a variety of providers that rely on different technologies. Consumers have options from wireline, wireless, Internet protocol, satellite, and other providers. Many of these choices include "all distance" bundled offerings that lump together video, voice, data, and other services all for one price. Some, but not all, of the revenues from these offerings may be USF assessable. This forces providers to make different, arbitrary allocations and skews the market toward services and providers that do not contribute to the Universal Service Fund. These complexities are getting worse every day as the same technological advances that policymakers seek to encourage through other federal programs make it impossible to maintain the fiction that a revenue-based USF contribution system is sustainable.

The draft Universal Service Reform Act would commit the FCC to take a hard look at an alternative contribution system. That is a good start. The best contribution methodology is one mentioned in the bill – a flat charge on each working phone number to pay for all or part of the USF contribution base. It is particularly important to fix the contribution system now. As I mentioned, the USF contribution factor next quarter will likely be more than 14%, which is the largest in the history of the fund. Not that long ago the factor was about half that size. The contribution factor has historically jumped around, but its upward trajectory and new peaks have pushed the fund to the brink. Just as troubling, the assessable base of interstate revenues is getting smaller and smaller. Interstate telecommunications revenue, the basis for all universal service funding, is now at the lowest level ever since the FCC began using quarterly revenues in the contribution factor calculation in 2001. That is not surprising given the shift away from traditional, USF-assessable services. But this is a trend that cannot continue if the Universal Service Fund is to survive and meet the new, important communications needs of people and healthcare facilities in rural areas, schools and libraries, and low income consumers.

The problems of a revenue-based system are not fixable by broadening the contribution base or by making other changes to the revenue system itself. Any revenue system will involve unworkable distinctions between what is and is not a contributing telecommunications service. The move away from simple telecommunications services toward more complex services is what's driving dollars out of the funding base. A numbers-based contribution system on the other hand fixes these problems by assessing contributions on an objective and readily measurable basis that is not affected by these shifts in demand. In fact, the "number of numbers" continues to increase steadily. Working phone numbers in the public domain increased by more than 60 percent between 2000 and 2008 to about 650 million numbers.

A numbers-based system with a small, set charge on each working phone number and narrow exceptions is better for everyone. It is better for consumers because many would see a decrease in the USF charges they pay each month, and a flat charge per number is easier to understand than a percentage charge that jumps around every month based on consumption. Frankly, nobody understands the universal service charges on their bills today. Low income consumers receiving assistance under the Lifeline program would also pay no USF, unlike the current system. A numbers system is better for policymakers because it would be easier and cheaper to administer and audit. And a numbers system is better for providers because it fairly spreads the contribution burden around and makes paying into the Universal Service Fund much simpler.

Third, a competitive bidding system is the best way to distribute high cost support to wireless carriers. The draft Universal Service Reform Act recognizes the benefits of this market-based approach and sensibly puts in place a forward-looking competitive bidding system to support and expand the reach of wireless networks.

The time is indeed now to once and for all fix the way wireless carriers draw support from the USF, which today doesn't make any sense. Currently, while wireless funding is capped overall at the state level, the per-handset subsidy amount paid to wireless carriers is calculated based on the per-line amount that is paid to the wireline incumbent serving a high cost area. In some cases, this encourages wireless carriers to serve areas where the incumbent receives substantial high cost funding, not necessarily to build out their networks into unserved areas. In addition, payments to wireless carriers are the same even if there are multiple providers that offer mobile service in the area – including carriers that compete without any USF support at all.

This is not how the system should work, and it is certainly neither an efficient nor effective way to meet the market's current and future mobile broadband needs. Universal service funding should be used to make sure all Americans have access to the services they want and need to be successful in the communications age, not to pay wireless carriers to sell more handsets in areas where there is a viable business case to offer service even without any universal service subsidies.

The right competitive bidding system will fix these problems. Competitive bidding breaks the artificial link between wireline and wireless funding and will bring the Universal Service Fund in line with established procurement procedures at other federal agencies. Many important goods and services such as critical product development work for military equipment and repair work for bridges and roads are purchased by competitive bid contracts. There is every reason to believe competitive bidding can also produce quality services in high cost areas and save consumers some money over the current system at the same time.

Some suggest that competitive bidding will result in low-quality service in rural areas. If we set up the system in the right way, that just isn't true. Quality of service considerations are not unique to the communications industry, and

competitive bidding is the standard way that government, at all levels, makes important procurement decisions. The FCC will need to address quality of service requirements in rules for a competitive bidding system, but that is manageable through legally enforceable contracts signed with those wireless carriers that win the bid to provide service in a high cost area.

The contracts that result from the competitive bidding process should also include wireless network build-out and maintenance obligations. Unlike the current system that subsidizes wireless carriers based on a wireline model, this will ensure that consumers get what they are paying for – that is, expanded reach of wireless networks. Getting wireless infrastructure into those areas where there are needs is essential as policymakers also struggle to fill remaining gaps in broadband access with the right technologies based on individualized facts and circumstances in these areas.

Fourth, we have to fix the broken intercarrier compensation system at the same time we update the Universal Service Fund. The key elements of the multi-year intercarrier compensation reform effort are not in dispute. We all just need a little help mustering up the resolve to get this done. The draft Universal Service Reform Act eliminates inaction as an option by setting a deadline for reform.

Universal service and intercarrier compensation (the charges that companies pay each other when traffic is sent to or received from the traditional phone network) are linked because regulators have in the past seen revenues from intercarrier compensation charges as a tool for keeping local phone rates affordable, something the universal service does expressly through subsidies paid directly to carriers. But supporting universal service with intercarrier compensation charges is not possible any longer in a market based on technologies that do not rely on yesterday's phone network. The current intercarrier "system" relies on the idea that there are meaningful distinctions

between interstate and intrastate services and between telecommunications and information services. As with universal service, migration to next-generation services makes these distinctions meaningless and drives dollars out of the intercarrier compensation system. In fact, high charges by some carriers for access to their networks impedes roll-out of new and advanced services in rural areas that could benefit most from these services.

The draft Universal Service Reform Act requires the FCC to act on intercarrier compensation reform within one year. That's certainly doable. Parties mostly agree that a single, low, uniform charge for terminating traffic on a network is the right solution. Carriers should also have the opportunity to rebalance their end-user rates, and to the extent they cannot recover lost access revenues they would have received going forward from their own customers, carriers could recover part of the difference during a transition period from a new universal service program. The new USF intercarrier compensation program should be expressly transitional and decline over time.

Fifth, we have to stop the so-called "traffic pumping" schemes that have plagued the industry the last several years, and the draft Universal Service Reform Act would help do that. Traffic pumpers game the intercarrier compensation system by exploiting antiquated FCC and state rules through collusive arrangements to drive traffic way up in some rural areas that historically have very low traffic volumes and correspondingly high access rates. Local exchange carriers in these rural areas then partner with chat-line and other providers, who market their services as "free," and share these excessive access revenues. The intercarrier compensation rules that allow LECs to charge other carriers high access rates in rural areas are designed to help ensure that consumers in these sparsely populated areas receive affordable and reliable service. The rules are not supposed to allow for these traffic pumping scams that have cost customers of more reputable carriers millions of dollars. Comprehensive reform of intercarrier compensation by the FCC might take care

of the traffic pumping problem, but that is a long-term effort and these schemes must be stopped once and for all right now. The draft Universal Service Reform Act would make it illegal for traffic pumpers to charge other carriers for access on traffic subject to these revenue-sharing agreements.

* * *

There are no perfect or easy solutions to the many universal service and related issues facing the Committee and the new FCC, and we cannot predict all of the many more innovations and changes that will surely take place in the communications marketplace. But we share the commitment to the goal of bringing these transformative technologies to all Americans and encouraging widespread broadband adoption. We also know that the Universal Service Fund and the universal service programs many of our fellow citizens count on are too important to let the fund slide further and further into crisis.

With the help of the Universal Service Reform Act we can get the Universal Service Fund moving down the path of sustainability and toward meeting the communications needs of our country. Thank you.

Mr. BOUCHER. Thank you very much, Mr. Davidson.
Mr. Greer.

STATEMENT OF LESLIE GREER

Mr. GREER. Chairman Boucher, Ranking Member Stearns, members of the subcommittee, good morning, and thank you for the invitation to participate in today's discussion regarding the Universal Service Reform Act of 2009.

My name is Leslie Greer. I am the CEO of DTC Communications in Alexandria, Tennessee. As a resident of Tennessee, I would like to take this unique opportunity to thank Representative Gordon and Representative Blackburn for their service on the subcommittee and to our great State.

My remarks today are on behalf of DTC Communication, as well as NTCA and its other 580-plus community-based members that serve rural areas throughout our Nation. NTCA would like to recognize Chairman Boucher and Representative Terry for their longstanding focus and awareness of the critical need for continued universal service support for our Nation's telecommunication network, which will help usher in the new era of advanced communication.

The Universal Service Reform Act contains many program modifications we have advocated for many years. I will briefly outline our position on some of the most critical positions of the bill from a rural provider's perspective. However, I would like to remind the subcommittee that further analysis of these provisions and others can be found in my written testimony.

Government policies and programs, including universal service, are instrumental to the realization of affordable and comparable telephone service for all. The United States public switched telecommunication network remains the envy of the world. The same should be true for the United States national broadband network.

The Universal Service Reform Act takes many important steps toward making this a reality. However, to achieve truly ubiquitous broadband, much more needs to be done. Therefore, NTCA looks forward to continue working with the FCC in the coming months to develop a national broadband plan to meet the needs of broadband networks in high-cost rural areas throughout the country to ensure Americans living in these areas are not denied the opportunity to realize the full promise of the Internet.

The bill would expand assessments of contributions. NTCA supports this change and believes all broadband access providers should contribute to the Universal Service Fund. This change alone will dramatically reduce the quarterly contribution factor on all providers while simultaneously ensuring that all those who utilize and benefit from the network are, in fact, supporting it.

The bill gives the FCC the authority to determine whether to use a contribution methodology based on revenues, numbers, or a combination of the two and requires a study and findings in support of the method chosen.

Telephone numbers have nothing to do with broadband Internet access, which will be the basis for all communication services in the future. With this in mind, as well as other provisions that ensure all revenues may be assessed, it is clear the FCC study will have

to arrive at the correct conclusion that the tested and proven revenues approach must be used.

NTCA recognizes the fundamental roles audits play in the oversight of policies and programs if they are conducted appropriately. Unfortunately, the audit process has mostly been a failure. Therefore, we support efforts by Congress and the provisions included in this bill to ensure the FCC uses appropriate audit methodologies.

The solution for intercarrier compensation is a simple one. If a service provider uses another provider's network, that service provider must compensate the other provider for such use at an appropriate rate. We fully support the bill's provisions directing the FCC to reform intercarrier compensation within 1 year.

The Universal Service Reform Act requires carriers to identify all traffic on their network and to pass through traffic identification details. NTCA supports this provision to eliminate phantom traffic, which has become one of the most pervasive problems facing the telecommunications industry today.

NTCA supports the elimination of the FCC's long-standing, arcane and nonsensical identical support rule that allows a competitor in a given market to receive support based on the incumbent's embedded costs, even though the competitor's costs are usually far less because they have not been required to serve all customers throughout the market areas as incumbents have to.

The draft contains other provisions that will help ensure this program's effective operations, including primary line and Antideficiency Act prohibitions, removal of the parent trap, and allowances to accommodate potential future regulatory shifts of intercarrier compensation or access charges within the universal service system.

With these things in mind, we support passage of this bill.

Thank you, and I look forward to answering any questions you may have.

Mr. BOUCHER. Thank you very much, Mr. Greer.

[The prepared statement of Mr. Greer follows:]

Statement by

Mr. Leslie Greer
Chief Executive Officer
DTC Communications
Alexandria, Tennessee

On behalf of the

National Telecommunications Cooperative Association

Before the

United States House of Representatives
Committee on Energy and Commerce's
Subcommittee on Communications, Technology, and the Internet

In the Matter of

Universal Service Reform Act of 2009

November 17, 2009

Introduction

Chairman Boucher, Ranking Member Stearns, members of the Subcommittee, good morning and thank you for the invitation to participate in today's discussion regarding the Universal Service Reform Act of 2009, which was recently drafted by Chairman Boucher and Rep. Terry. I would like to take this opportunity to also thank Rep. Gordon and Rep. Blackburn from my home state of Tennessee for their tremendous work on this Subcommittee.

My name is Leslie Greer. I serve as the CEO of DTC Communications in Alexandria, Tennessee. My remarks today are on behalf of DTC Communications, as well as NTCA and its other 580 plus community-based members that serve rural areas throughout the nation. DTC's top priority has always been to provide every one of its consumers with the very best telecommunications and customer service possible. DTC serves 18,235 access lines across its 759 square mile rural service area that is entirely encompassed in one isolated region of one state. This is about 24 lines per square mile. DTC employs a total of 111 people and our annual revenue is $18.5 million.

Universal service continues to be the cornerstone of our nation's communications policy and ensures our customers in rural Tennessee and those living in other rural areas of the country receive telecommunication services at a rate comparable to those living in more urban areas. Over the course of decades, our national commitment to the concept of universal service has steadily transformed. We encouraged this transformation as both citizens and policymakers to ensure that all Americans have the opportunity to experience the benefits that are offered by a nationwide integrated advanced communications network.

Therefore, as part of this evolution in communications, NTCA would like to thank Chairman Boucher and Rep. Terry for their long-standing focus and understanding of the critical need for continued universal service support for our nation's telecommunications network, which will help usher in the new era of advanced communications. The Universal Service Reform Act of 2009 contains many program modifications we have advocated for years. Among those modifications, the bill:

• Defines universal service to include high speed broadband service and sets build out targets to move the nation in that direction

• Assesses a wider range of providers, which includes all broadband providers

• Eliminates the identical support rule and bases support to providers upon their own costs

• Requires FCC to act on intercarrier compensation in the near term and allows the universal service fund growth factor to accommodate any intercarrier flows directed to it

• Addresses phantom traffic by mandating identification of traffic

• Addresses the traffic pumping issue by clarifying it is a prohibited practice

• Prohibits implementation of a primary line restriction

• Permanently exempts universal service programs from the Anti-Deficiency Act

• Includes performance measurement language and other requirements to ensure the audit process is fair

• Strengthens the eligibility requirements for receiving support and controls the unprecedented growth in support that has flowed to wireless/competitive entities

• Eliminates the so-called parent trap so that providers acquiring exchanges are not stymied from investing in such markets

It could be argued that in many ways our national universal service policy has become the victim of its own success. Too often regulators and competitors alike have viewed the program as little more than a means of inciting artificial competition rather than serving as a cost recovery mechanism for those with a genuine commitment to high-cost markets. Likewise, others have misinterpreted the fact that the program has helped achieve high levels of connectivity as suggesting that the program is no longer necessary. Yet nothing could be further from the truth.

Today, we exist in a global environment where highly advanced communications infrastructure and services intricately intertwine all of the world's citizens, governments and economies. The technological advances and demands by the public that accompany them suggest that the need for this program has never been stronger. Our highest priority must center on crafting policies

that will fully reestablish the value of this program for all consumers and simultaneously restore America's communications preeminence.

Unfortunately, some believe in the elimination or reduction of this support mechanism. This would have dramatic and immediate consequences for NTCA's member companies and the rural communities they serve. Without USF, retail prices would rise - putting telecommunication services out of reach of many Americans. In addition, service quality would drop as carriers would no longer be able to afford necessary upgrades and maintenance. Even worse, some companies would no longer be able to offer service at all – eliminating communication services for those Americans that live in the most rural regions of our country. Everyday these citizens serve as the backbone of our country by growing the food we feed our families, fueling our country with a large variety of traditional and renewable energy resources needed to run our economy, and supplying our military with a disproportionately large number of young men and women in uniform. While the majority of Americans no longer live in rural areas, everyone of us still depends on them. Much like the interstate highway system has done, providing these rural areas with affordable, advanced communication services strengthens our connectivity to each other and benefits the nation as a whole.

The universal service program is not perfect, if it was, we wouldn't be here today discussing the best way to reform it. However, even its detractors cannot deny that the program is a shining example of successful national policy. This program is largely responsible for the extremely high communications connectivity our nation enjoys today. It is due to universal service support that virtually any American that wishes to have voice connectivity is able to. Likewise, it is solely due to this program that such connectivity is uniform in price and scope throughout the nation.

Universal Service Reform Act of 2009

Today, the universal service system is more critical than ever as the nation continues its pursuit of ubiquitous advanced communications systems. While rural telecommunication carriers have

worked hard to increase infrastructure deployment, there is much more that remains to be done to meet our national communication goals.

With the FCC hard at work developing a national broadband plan that will be completed in February 2010, this compromise legislation serves as an important piece of the puzzle as we work to ensure that our commitment to advanced communication services are met. The Universal Service Reform Act gives appropriate recognition to the need for reform by calling for major program modifications which have been sought by the industry for many years, while simultaneously recognizing the concerns of those who have not always advocated on behalf of the program.

Broadband Deployment

Government policies and programs, including universal service, are instrumental in the realization of affordable and comparable telephone service for all. The United States public switched telecommunications network remains the envy of the world. The same should be true for the United States national broadband network. The Universal Service Reform Act takes many important steps toward making this a reality by, among other things, declaring broadband to be a universal service, expanding the contribution base, and by directing the FCC to complete a proceeding to reform intercarrier compensation within one year.

While technological advances are helping to reduce the cost associated with broadband deployment, it is still always going to be more expensive to serve rural America due to low population density, expansive distances, and often-rugged terrain. Without federal policies that put in place additional cost recovery mechanisms, our national goal of universal broadband access may never be realized. To underscore the sizable commitment that will be needed to achieve ubiquitous broadband, according to a recent FCC task force study, preliminary estimates indicate that investments in the range of $20 billion to $350 billion may be needed, depending on the speed of service hoped to be achieved. To overcome these financial barriers, NTCA looks forward to continue working with this Subcommittee and the FCC to develop a national broadband plan to meet the needs of broadband networks in high-cost, rural areas throughout the

country to ensure Americans living in these areas are not denied the opportunity to realize the full promise of the broadband era ahead.

Intercarrier Compensation

The solution for intercarrier compensation is a simple one, if any service provider uses another provider's network that service provider must compensate the other provider for the use of their facilities at an appropriate rate. Carriers that invest millions in network infrastructure should receive compensation from those that utilize it in lieu of building their own network. Today, our industry confronts a situation where more and more entities that need and utilize our networks are refusing to pay for such use. This would be tantamount to my asking you Mr. Chairman, if I could have permanent access to your car, to drive around as I please without compensating you for doing so, and all the while, insisting that you have it tuned up and filled with gas. As ridiculous as that sounds, that is exactly the situation our segment of the communications industry confronts today. Therefore, NTCA fully supports the inclusion of intercarrier compensation reform provisions within the bill. As part of the required proceeding, the FCC should determine the regulatory treatment of interconnected voice over the internet protocol (VOIP) technologies. Since interconnected VOIP is a direct substitute for traditional voice telephone service, it should be treated as such and VOIP providers should pay applicable access charges. We also support the inclusion of a one year deadline placed on the FCC to complete the proceeding to reform intercarrier compensation. This enactment time limit will ensure reform of this important cost recovery mechanism is not further delayed.

Traffic Identification

The Universal Service Reform Act requires carriers to identify all traffic on their networks and requires all carriers to pass through that identification. NTCA supports this provision to eliminate "phantom traffic," which has become one of the most pervasive problems facing the telecommunications industry today. The decline in revenue that phantom traffic now yields for carriers has reached a crucial point and is destabilizing our industry. We have been amazed by the laissez-faire attitude that surrounds the issue of phantom traffic, which is similar to a person

receiving cable television signals without paying for them. While tools are beginning to emerge to help verify the identity of traffic, the fact of the matter is that, for the most part, small, rural carriers are generally at the mercy of others with regard to traffic identification. We believe the time has arrived for policymakers to act on this matter in order to stem any further hemorrhaging of lost access and intercarrier compensation due to the insatiable growth of phantom traffic.

Contribution Expansion

The bill would assess contributions on any entity that currently pays into the USF; any provider of a service that uses telephone numbers or IP addresses to provide voice communications; and any provider that offers a network connection to the public. NTCA supports this change and believes all broadband internet access providers should contribute to the USF. Expanding current USF programs to include broadband without assessing broadband services to contribute to the USF will not provide sufficient levels of support to achieve the goal of affordable Internet access service to all Americans. Therefore, NTCA believes all broadband providers should contribute to future broadband USF support mechanisms.

Contribution Methodology

The bill gives the FCC the authority to determine whether to use a contribution methodology based on revenues, numbers, or a combination of the two. Since telephone numbers have nothing to do with broadband Internet access service, which will be the basis for all communications in the future, NTCA believes that revenues, not numbers, should be assessed for future USF contributions. If USF contributions are limited to traditional voice services, the inevitable migration away from these services will eliminate all future universal service funding.

We believe the contributions assessment methodology must be forward looking. AT&T first proposed a numbers based methodology largely to shift this responsibility away from itself and its interexchange counterparts. Now, several years later, at a time when policymakers and the public alike are demanding that we migrate to a fully broadband and advanced services capable infrastructure, variations of the AT&T numbers concept continue to receive consideration, both

in Congress and at the FCC, despite the concept's backward looking approach to assessing a limited segment of the overall communications industry. The revenues assessment methodology is known, tested, operational, and superior. We should stick with it, and are confident that the study your legislation requires on this subject will show this is the only responsible response to this issue.

Audits

The Universal Service Reform Act directs the FCC to use appropriate audit methodology, using auditors trained in universal service fund program compliance. NTCA recognizes the fundamental role audits can play in the oversight of policies and programs if they are conducted appropriately. Unfortunately, the audit process, which has been underway by the FCC OIG for several years, has been mostly a failure and done little more than lead the program's detractors to cite misleading examples of perceived program weaknesses. This failure was outlined by the February 12, 2009 report from the Universal Service Administrative Company (USAC) that explained the audit's shortcomings in terms of costs, approach, findings, and reporting. The USAC report noted how over the course of approximately three years, tens of millions of USF dollars have been diverted from universal service program objectives to conduct more than 1000 separate audits. Yet even more telling is that all these dollars later, the OIG audit reports have identified no instances of fraud or gross non-compliance with the high-cost portion of the program.

We support the efforts of this Subcommittee, and the provisions included in this bill, to ensure the FCC uses appropriate audit methodologies and processes, and reports factual program information to Congress and the public in the future.

Traffic Pumping

The Universal Service Reform Act prohibits access charge recovery when an entity that has an agreement with a local exchange carrier relating to switched access revenues from such services offers a free or below cost service. NTCA will continue to support narrowly tailored approaches,

such as the approach offered in this bill, to handling allegations of traffic pumping that do not interfere with legitimate business activity.

Parent Trap

NTCA supports the elimination of the FCC's parent trap rule that forces carriers acquiring exchanges to receive support based on the level of support, if any, that the previous owner/carrier received. Elimination of the parent trap may make it more cost effective for carriers, in particular, small, rural carriers to acquire and improve service to areas where quality service is currently not available. As most of us know, the parent trap evolved out of a regulatory realm from several years ago. During that time, the FCC attempted to limit the flow of universal service support related to a number of industry acquisitions involving smaller carriers purchasing exchanges from larger carriers, which were badly in need of upgrading. Today, as we move in a direction that envisions the ubiquitous deployment of a fully advanced capable communications infrastructure, it is appropriate this regulatory hurdle be removed to ensure all Americans are able to partake in the broadband promise of the future.

Permanent Anti-Deficiency Act Exemption:

Prior to 1995, the universal service system was never considered a part of the federal budget because it had always involved transactions of private monies between private sector parties. The only reason it became part of the budget was because the Congressional Budget Office and the Office of Management and Budget made assumptions and interpretations that the flow of support was somehow federally oriented. They made this misinterpretation based on the opinion that following the enactment of the Telecommunications Act of 1996 the statutory directives on contributions and distributions gave an implied suggestion that these were federal associated amounts. Yet the fact of the matter is these monies are still private monies, not funds that are being appropriated from the federal Treasury. Therefore, NTCA supports the bill's provision to explicitly remove the program from the Anti-Deficiency Act to avoid the struggle to renew the annual exemption.

Primary Line Restriction

NTCA supports the bill's prohibition on regulatory attempts to restrict universal service support only to a primary line connection. Limiting universal service support to primary lines is a concept the FCC has rejected on several occasions because it is simply inconsistent with the underlying reality that we are building and maintaining a network – not a patchwork of singular lines and connections. There is an overall cost to building a network, and limiting cost recovery to only a few singular elements of the overall infrastructure would grossly underestimate the actual cost of deployment - leaving carriers and their consumers to make up the dramatic difference.

In rural areas, in particular, such a restriction would preclude second lines and cellular phones from eligibility for USF support. Therefore, rural customers would have the right to only one phone line at the reasonable costs offered to their urban counterparts, while their second and cellular lines would be charged exorbitant rates.

Rural small businesses would be particularly vulnerable to such regulation. Because these businesses generally have fewer than five lines, a primary line restriction would result in exceptionally higher operational costs because of the high cost of providing telecommunications services in rural areas. This puts rural businesses at a distinct disadvantage to their urban counterparts and is unfair to residential consumers as well.

Rural wire line and wireless carriers rely on this support, and the restriction would dramatically reduce incentives for the deployment and upgrade of facilities in rural areas. Not only would such a restriction hinder future deployment, but it could also jeopardize the ability of rural carriers to service debt for already constructed plant facilities.

Eliminating the Identical Support Rule

The FCC's longstanding, arcane and nonsensical "identical support rule," which was put in place all in the name of competitive neutrality, allows a competitor in a given market to receive

support based on the incumbent's imbedded costs – even though the competitor's costs are usually far less because they have not been required to serve customers throughout the market area as incumbents must do. Perhaps the most vexing aspect of this rule is how it motivates competitors to zero in on markets where there is the most money rather than markets where there is the most need.

This happens because, without a requirement to serve the entire market area, and with a rule that says competitors will receive support based on the incumbent's costs, competitors target markets where universal service support is high because rural incumbents have been working hard to deploy services. Meanwhile the same competitors overlook the rural markets of the large carriers where deployment has typically not been widespread and where, for this and other reasons, universal service dollars are not flowing and thus would not flow under the identical support rule. Obviously, this conundrum is not in the public interest and we are pleased the legislation before us today would eliminate the identical support rule.

Conclusion

Finally, as I alluded to earlier in the testimony, the FCC's National Broadband Task Force recently released a study that confirmed there will be an extremely high cost to achieve ubiquitous broadband deployment. NTCA's work before the FCC, in conjunction with the National Broadband Plan, which will be provided to Congress in February 2010, attempts to appropriately respond to these realities by identifying ways to achieve our national universal service policy objectives – in particular for those challenging rural areas that have for too long been ignored by larger providers that continue to gravitate toward higher-paying urban markets and away from their customer base located in less densely populated markets.

To identify the appropriate solutions that will address these issues and fulfill the broadband promise so many are talking of today, we look forward to working with this Subcommittee, your

House colleagues, your Senate counterparts, and the FCC on long-term solutions to our nation's broadband challenges.

Mr. Chairman, I want to thank you again for inviting me to be here. Your knowledge of the industry and your commitment to strengthening advanced communications in both urban and rural America make us all fortunate to have you serve on this Subcommittee.

I look forward to answering any questions you or your colleagues might have.

Mr. BOUCHER. Mr. Rhoda.

STATEMENT OF MICHAEL RHODA

Mr. RHODA. Chairman Boucher, Ranking Member Stearns and members of the subcommittee, thank you for this opportunity this morning to discuss our views on the draft text of the Universal Service Fund Act of 2009. My name is Mike Rhoda, and I am the Senior Vice President for Government Affairs at Windstream, which provides communications and entertainment services to consumers in 16 States.

Windstream serves more than 3 million voice customers and more than 1 million high speed Internet customers. We provide affordable broadband services at speeds of at least three megs to virtually every community in our service territory and we have deployed high speed Internet access to more than 90 percent of our voice customers. Windstream's service areas are primarily rural, with an average density of 19 customers per square mile.

Mr. Chairman, let me say that I have great respect for your and Mr. Terry's work, and thanks to your bipartisan leadership, the draft bill fairly balances the many conflicting interests in this complex area. Windstream supports passage of this bill.

Unlike other rural carriers, Windstream receives relatively little high cost support on a per line basis. Instead, Windstream must implicitly subsidize service for customers in remote high cost areas with revenues from its customers in larger, more densely populated towns.

More than a decade ago, Congress recognized in Section 254 of the Communications Act that such implicit subsidies would be unsustainable in a competitive telecommunications marketplace, and, unfortunately, universal service regulations remain virtually unchanged since that time.

We have seen the programming's shortcomings up close. A good example is one of our customers residing in rural Nebraska who recently contacted us to ask why he could not purchase broadband at speeds comparable to his rural neighbors down the road. His neighbors are served by a smaller company whose network has been modernized by universal service. His frustration is understandable.

Windstream's commitment to deploying affordable broadband in rural America is undeniable, but existing universal service mechanisms have created drastic imbalances in rural Nebraska and rural America at large. Some high cost areas receive arguably too much support, while many others receive far too little or no support at all. While the neighboring companies in this example receive an average of $800 annually per line in support, Windstream's Nebraska operations receive approximately $10 per line annually.

The Boucher-Terry bill takes a large step toward eliminating these disparities in high cost rural areas by narrowly targeting support to those areas that need it most. The bill's use of targeting eliminates two significant shortcomings of the current system.

First, under the rule mechanism, price kept carriers costs are averaged across study areas, which can cover vast geographies. A single Windstream study area stretches the full width of Texas, a

distance of more than 700 miles, and contains more than 200 exchanges, ranging in size from 44,000 customers to 47. With competitive pressures mounting and lower costs and more densely populated areas, severe strains are placed on a carrier's operations because low cost wire centers no longer generate sufficient revenues to offset costs in remote higher cost areas.

The second problem lies with the non-rural mechanism's classification of entire States as either eligible or not eligible based on statewide average costs. This limitation disqualifies rural areas in a State like California from receiving support, no matter how small, how remote or how costly a community is to serve.

The Boucher-Terry draft establishes a sensible transition path for incorporating broadband into universal service. The strength of the Boucher-Terry draft is that it sets the Nation on a path to universal broadband, but with recognition of the significant costs to achieve this goal and an opportunity to amortize those costs over time.

Finally, Windstream strongly supports the bill's recognition of the important role that revenues from the existing intercarrier compensation mechanisms play in offsetting the high costs in rural areas.

Many on this subcommittee remember that one year ago, the FCC considered a proposal to eliminate most intercarrier compensation revenues. That proposal would have been disastrous for consumers and businesses in high cost rural areas. Windstream recognizes that the current rates and arcane rules of intercarrier compensation are unsustainable and the company has presented practical alternatives to the FCC that would not hobble the ability of mid-sized carriers to serve rural consumers.

In closing, Mr. Chairman, I would like to assure all members of this subcommittee that there is broad agreement within the telecom industry on the need for significant universal service reform and that that reform is long overdue. While reforms carry certain risks, the larger risk is to stand by and watch well-documented problems continue to pull down communities and consumers residing in rural America. Significant change is the only way to save this program and position it to fulfill its mission.

Thank you.

Mr. BOUCHER. Thank you very much, Mr. Rhoda.

[The prepared statement of Mr. Rhoda follows:]

Statement of Michael Rhoda

Senior Vice President, Windstream Communications, Inc.

to the

House Committee on Energy and Commerce

Subcommittee on Communications, Technology, and the Internet

November 17, 2009

Chairman Boucher, Ranking Member Stearns, members of the subcommittee: Thank you for this opportunity to discuss rural communications and, specifically, our views on the draft text of the "Universal Service Reform Act of 2009."

My name is Mike Rhoda, senior vice president for government affairs at Windstream, which provides voice, broadband, and satellite television services to consumers in 16 states. We provide wireline communications and entertainment services to residential and business consumers in rural areas and small towns. Windstream is a publicly traded, S&P 500 company with about 3 million voice customers and more than 1 million high-speed Internet customers. Windstream provides affordable broadband service at speeds of at least 3 Mbps and up to 12 Mbps to virtually every community in our service territory and has deployed broadband to almost 90% of our voice customers.

Before going into detail, Mr. Chairman, let me say that I have great respect for your and Mr. Terry's work on this legislation. You are careful students of telecommunications and clearly have taken the time to understand the challenges of serving high-cost rural areas. Thanks to

your bipartisan leadership, we have a draft that fairly balances the many conflicting interests in this complex area. Windstream supports passage of the bill.

Windstream is well versed in the many reasons for comprehensive universal service reform. Per square mile, Windstream serves approximately 19 voice customers per square mile, compared to more than 100 customers per square mile for the largest, nationwide carriers. Unlike some other carriers, Windstream receives relatively little high-cost support on a per-line basis. Instead, Windstream is left to implicitly subsidize service for customers in remote areas with revenues from its customers in larger, more densely populated towns. More than a decade ago, Congress recognized in Section 254 of the Communications Act that such implicit subsidies would be unsustainable in a competitive telecommunications marketplace. Unfortunately, while competition has raced through one market after another, universal service regulations remain virtually unchanged.

All consumers have a stake in this program, whether they live in Chairman's Waxman's district in Los Angeles or in Buffalo, Texas – a Windstream community in Mr. Barton's district. But few Americans realize how their dollars are being spent. They surely would be unhappy to hear the 2007 assessment of Ray Baum, the State Chair of the Federal-State Joint Board on Universal Service: Universal service has produced "a vast misallocation of public dollars, to the benefit of only a small portion of rural consumers, and to the detriment of the rest." In 2008, Congress received another negative report, this time from the Government Accountability Office (GAO), which said: "The high cost program's structure has contributed to inconsistent distribution of support and availability of services across rural America." The bottom line is,

public funds are not being well utilized and millions of consumers in high-cost rural areas are being left behind as a result.

We have seen the program's failures up close. A good example would be when one of our customers residing in Nebraska – he lives in "the country" – recently contacted Windstream to ask why he cannot purchase access to the Internet at speeds and rates comparable to his neighbors down the road. His neighbors are served by a smaller company whose facilities have been extensively modernized, thanks in no small part to universal service funds. His frustration is certainly understandable. Windstream's commitment to deploying affordable broadband is undeniable. But existing universal service mechanisms have created drastic imbalances in rural Nebraska and rural America at large. Three neighboring companies around us in Nebraska receive a) $200 per customer in annual USF support, b) $600 per customer in annual support, and c) $1,700 per customer in annual support. At the other end of the spectrum is Windstream-Nebraska, which receives about $10 per customer in annual universal service support. This makes little sense. The farms and small towns served by Windstream have similar needs, similar geography, and similar cost profiles. Granted, Windstream-Nebraska can achieve economies of scale that the smaller companies cannot. But our costs are not 20 times, 60 times, or 170 times more efficient! Such disparities in support matter to our customers because they make a real difference in the services we can offer.

The new Boucher-Terry bill would take a large step towards phasing out disparities in high-cost rural areas, by narrowly targeting support to those areas that need it most. Universal service would be targeted on a far more granular basis than at present, and areas with similar,

higher-cost characteristics would be more likely to receive similar levels of support. The bill would make all high-cost areas eligible for forward-looking support – eliminating rules that now limit eligibility to just 10 states. Over time, a more equitable distribution of support across high-cost areas would stimulate further investment in advanced communications networks. We think the draft legislation is prudent to implement this change over a reasonable number of years, to allow companies to modify their business plans.

The bill's use of targeting would eliminate two significant shortcomings of the current universal service system. First, under the "rural" mechanism, mid-size price-cap carriers' costs are averaged across study areas, which can cover vast areas. Consider, for example, a single Windstream study area in Texas. It stretches the full width of Texas, a distance of 717 miles, from the Red River in Texarkana to the Rio Grande River in Fabens. To put this into perspective for non-Texans, that's farther than the trip from this hearing room to Jacksonville, Florida. This single study area contains nearly 200 exchanges, ranging in size from 44,000 voice customers to 47. With competitive pressures mounting in lower-cost areas, severe strains are placed on price-cap carrier operations, because low-cost wire centers can no longer generate revenues that can be shifted to offset costs in remote, high-cost areas. The second serious problem lies with the "non-rural" mechanism's classification of entire states as either eligible or non-eligible, based on statewide average costs. For example, this limitation disqualifies all of California from receiving support, no matter how small, remote, or costly a community is to serve.

Although Windstream has been skeptical of past efforts to include broadband as a supported service within USF, we believe the Boucher-Terry draft has laid out a sensible

transition path. There are many problems with a flash cut to a 100% broadband program, not the least of which is cost. As noted in a recent presentation by the staff of the FCC's Omnibus Broadband Initiative, the incremental cost of making broadband universally available is estimated at $20 billion to $350 billion, depending on the speeds sought. That's the cost for one network – not the overlapping networks associated with current policy. The strength of the Boucher-Terry draft is that it sets the nation on the path to universal broadband, but with recognition of the costs involved and an opportunity for the fund to amortize the most severe costs over time.

Windstream also appreciates the Boucher-Terry bill's recognition of the important role that revenues from the existing intercarrier compensation mechanisms play in offsetting high costs of providing service in rural areas. Intercarrier compensation is a multi-billion dollar payment system, with regulated rates that are paid when one carrier cannot carry a voice call from start to finish and must hand off the traffic to another company to transport and/or complete the call. Many on this subcommittee remember that one year ago, the FCC considered a proposal to eliminate most intercarrier compensation revenues. That proposal, if enacted would have been disastrous for consumers living and/or doing business in high-cost areas and fortuantely rational minds prevailed. Nonetheless, Windstream has long recognized that the current rates and arcane rules of intercarrier compensation are unsustainable, and the company has presented practical alternatives to the FCC that would not hobble the ability of mid-sized carriers like Windstream to serve rural consumers. We are encouraged that the Boucher-Terry bill takes reasonable steps to address much needed intercarrier compensation reform and, in particular, explicitly authorizes the FCC to establish an alternate recovery

mechanism above the existing fund cap. Access revenues in some fashion are vital to sustaining existing service and enabling broadband in high cost areas. We all must recognize that reducing the intercarrier compensation revenues of carriers serving rural consumers in high-cost areas beyond a reasonable level will hinder – not enable – carriers' ability to provide quality voice and broadband service to rural customers.

In closing, Mr. Chairman, I would like to assure all members of this subcommittee that there is broad agreement within the telecom industry on the need for significant universal service reform. There is widespread recognition that reform is long overdue. You and Mr. Terry have crafted a reasonable compromise, and compromises usually leave everyone a little unhappy. And reform does carry risks. But the larger risk is to stand by and watch well documented problems pull down communities and consumers across rural America. Changing universal service is difficult, but significant change is the only way to save this program and fulfill its mission. Thank you.

Mr. BOUCHER. Mr. Lubin.

STATEMENT OF JOEL LUBIN

Mr. LUBIN. Good morning. Thank you, Chairman Boucher, Ranking Member Stearns and other members of the subcommittee, for again including AT&T in this continuing dialogue of universal service reform. AT&T is the largest provider of telephone service to rural America.

This is the second time I have had the opportunity to address this subcommittee this year. The first time was in March of 2009. At that point in time, when we were talking about high cost universal service reform, AT&T identified three critical areas that needed to be addressed.

The first one was contribution reform. Contribution reform is so important because it is all about what customers pay and which customers pay.

The second was intercarrier compensation. Intercarrier compensation is critical because it is just another form of subsidization to rural America.

The third is, once and for all, to identify an explicit endorsement for the use of high cost universal service mechanisms to promote the deployment of next generation broadband and expanded and improved wireless in rural areas.

Mr. Chairman and Representative Terry, I wish to congratulate you, for this legislation when introduced and enacted will address the three items that AT&T highlighted in March of 2009. We support and endorse this legislation.

From AT&T's perspective, universal service, as it exists today at both the Federal and State levels, is fundamentally grounded on a dying business model and a dying regulatory model which no longer serves the foundation of sustainable social policy. The plain old telephone service, POTS, by which local exchange providers provide basic local exchange service with inter-exchange access to long distance service will soon go by the way of a slide rule, an earlier casualty of digital technology.

In today's communication marketplace, the only thing falling faster than subscribers on local basic service called POTS is the switched access minutes on these collective networks. In these circumstances, no government could hope to prop up the POTS model for long, even if it wanted to, in order to sustain universal service. Instead, universal service reform must be forward-looking and policymakers must continue to work on comprehensive national universal service reform policies in order to promote and advance universal service objectives for the 21st century.

The Universal Service Reform Act of 2009 both appropriately reflects the insights of its sponsors and the committee leadership and recognizes the reality of the rapidly eroding implicit subsidies in the disappearing switched access world, as well as the need to establish explicit funding mechanisms in order to ensure universal service objectives are met for the 21st century.

Let me return to the three pressing areas of reform that I described before.

First is with respect to contribution reform. The importance of this provision cannot be overemphasized. According to the preliminary numbers submitted by the Universal Service Administration Company to the FCC a few weeks ago, the assessment rate could approach and exceed over 14 percent of interstate telecommunications revenues. When I was here in March of 2009, that factor was 9.5 percent. In less than a year, we see a 50 percent increase.

We have asked the FCC to act on a long-standing proposal by AT&T and Verizon, which is supported by a number of individual companies and individual associations, to implement a telephone numbers-based contribution mechanism that would address the problem posed by the overall reduction of interstate revenues, which is the basis for the universal service contribution base. This would create a more stable, robust collection mechanism for universal service. This is of critical importance to the goal of providing more explicit support for a broadband deployment.

Second is the section on intercarrier compensation reform, which is also critical for the transition to full deployment of broadband, which will accelerate the complete, underlining the word "complete," complete elimination of access charges as a source of universal service funding. We can debate what the rate is, but a rate times zero minutes is going to generate zero dollars. And ultimately the question is, if that was supporting universal service, how does it work in a broadband world? We have needed intercarrier compensation reform for years, and the importance of this draft measures requirement that the Commission act within one year to complete reform initiatives cannot be overstated.

Further, the bill makes access stimulation charge, some people call it access pumping, an unreasonable practice under the Communications Act and prohibits local exchange carriers from assessing access stimulation or traffic pumping charges.

Third, AT&T is pleased that the bill creates a statutory framework that, once and for all, removes any doubt that it is the policy of the United States that the Federal high cost funding mechanism be used to promote deployment of broadband and expanded and improved wireless in rural areas.

We look forward to hearing from the other panelists and answering your questions. Thank you.

Mr. BOUCHER. Thank you very much, Mr. Lubin.

[The prepared statement of Mr. Lubin follows:]

STATEMENT OF JOEL E. LUBIN

VICE PRESIDENT-PUBLIC POLICY
AT&T SERVICES, INC.

Before:

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON ENERGY & COMMERCE
SUBCOMMITTEE ON COMMMUNIATIONS, TECHNOLOGY AND THE INTERNET

"THE UNIVERSAL SERVICE REFORM ACT OF 2009 [Discussion Draft]"

November 17, 2009

Thank you, Chairman Boucher, Ranking Member Stearns, and members of the Subcommittee for again including AT&T, the largest provider of telephone service to rural America, in this critical step on the path forward to comprehensive Universal Service Reform. We believe this draft legislation is the culmination of a four-year effort to effect meaningful reform, and represents the most significant progress to date. Indeed, the draft in its present form addresses the three pillars of fundamental reform: appropriate contributions methodology; intercarrier compensation reform; and explicit coverage of advanced services, including broadband. Thus, for these reasons, which are more fully explored herein, AT&T is pleased to endorse your thoughtfully crafted bill.

First, with respect to contributions reform, Section 102 of the draft bill would require the Federal Communications Commission to assess contributions to universal service support mechanisms from communications service providers in a manner that is equitable, competitively neutral, nondiscriminatory, and ensures that communications service providers are subject to similar obligations. In doing so, the Commission would be permitted to employ any methodology to assess contributions within these prescribed parameters, including "working

telephone numbers used by communications service providers" and "any other current or successor identifier protocols or connections to the network used by communications service providers."

The importance of this provision cannot be over-stated as it will mandate the creation of a more sustainable and predictable methodology for determining contributions – something for which there is a desperate need. According to preliminary numbers submitted by the Universal Service Administrative Company to the Commission, consumers are expected to pay over fourteen percent of their interstate telecommunications charges in federal universal fees starting next year– well higher than the highest combined state and local sales tax rates. When I testified before this Committee about reformation of the High Cost funds in March of this year, this percentage was 9.5%. This means that consumers will experience an almost 50% increase in this factor in less than a year. Federal policymakers must necessarily ask how a contribution factor that is rapidly approaching 15% and higher can, on its face, be consistent with the historic underpinnings of universal service policy: ensuring that all Americans have access to affordable communications. They should also ask what a 15% contribution factor means to achieving today's policy goal of ensuring that each American has access to broadband. These facts underscore the important observations made by Chairman Waxman when this Committee last convened on this topic: the current funding mechanism neither "spreads responsibility for the program as broadly and equitably as possible," nor, as Chairman Boucher observed, does it identify "other funding sources" that "must be tapped." In the meantime, "[n]ew technologies and new business plans," have in fact combined, as Chairman Boucher has observed, to "diminish the long-distance revenues that have historically been relied upon to support universal

service," while demand for high-cost USF funding has increased 54% in the last five years – and the growth is not slowing.

In light of these circumstances, AT&T petitioned the Commission in July for immediate Commission action to reform its USF contribution methodology. We asked the Commission to act on a long-standing proposal by AT&T and Verizon, which is supported by a number of individual companies and industry associations, to implement a telephone numbers-based contribution methodology that would address the problems posed by the overall reduction in the universal service contribution base. The draft Universal Service Reform Act of 2009 would require the Commission to develop an equitable, competitively- and technology-neutral contribution system that would assess contributions from all communications service providers, and which could clearly include the numbers-based proposal currently before the Commission or a similar numbers and connections contribution methodology. We believe that this provision on contribution reform is of critical importance to the goal of providing more explicit support for broadband deployment.

Second, with respect to intercarrier compensation reform, Title III of the Universal Service Reform Act of 2009 would address the critical problems of intercarrier compensation and access charge distortions. Section 301 of the draft measure would require the Commission to complete an initial intercarrier compensation reform proceeding within one year after enactment. Such reform is critical during the transition to the full deployment of broadband, which will accelerate the complete elimination of access charges as a source of universal service fund revenues. We have needed intercarrier compensation reform for years and the importance of the draft measure's requirement that the Commission act within a year to complete its reform initiatives is therefore obvious. Further, Section 303 of the draft bill would both deem the

assessment of an access stimulation charge to be an unreasonable practice under the Communications Act and prohibit local exchange carriers from assessing access stimulation charges. This is a critical and appropriate legislative response to the vexing problem of traffic pumping, and AT&T salutes your leadership in establishing the patent unlawfulness of this practice.

Third, AT&T is pleased that Title I of the measure would create a statutory framework reinforcing the policy of the United States that federal universal support mechanisms should be used to promote the deployment of broadband, and expanded and improved wireless service, in rural areas. Specifically, Section 101 of the draft bill would establish a fundamental policy that access to advanced telecommunications and information services should be provided in all regions of the nation, and are specifically included in the suite of services that should be made available to low-income consumers and those in rural, insular or high cost areas. Section 103 would further permit the use of universal service support for all rural, insular, or high cost areas to include high-speed broadband service, while Section 104 of the measure would establish a framework for a competitive bidding process for mobile wireless communications service providers to provide service to rural, insular or high cost areas.

AT&T believes that fixed and mobile wireless services, including broadband services, should receive universal service support where appropriate, and that eligibility for such support should be completely detached from the amount of support received by ILECs within those areas. We also believe that fixed-location (wireline) broadband Internet access services should be supported, consistent with Chairman Waxman's call that the USF be "forward-looking."

As the legislative reform process moves forward, AT&T urges the Committee to continue to examine the appropriate role that speed should play in determining broadband eligibility. We

are wary of elevating broadband speed above all other service criteria, particularly in the context of encouraging the deployment of broadband to previously unserved or rural areas where a business case for such service could not normally be made. Statutory codification of a specific downlink speed as the determinative factor for defining broadband eligibility may not be optimum from either a policy or a fiscal perspective, because it could eliminate the use of broadband technologies that would otherwise be appropriate.

We also remain concerned that one aspect of the bill may have the inadvertent consequence of limiting funding for broadband services. The draft legislation would attempt to contain costs through a cap. A cap may be, at best, a blunt instrument – a tourniquet to staunch the bleeding until more organic, fundamental reforms are realized. Long term, we must be cognizant of how a funding cap might limit the vision of ensuring that all Americans -- particularly those in areas unserved by broadband today -- have access to broadband services, regardless of where they live, work or travel, by constraining the ability to fully fund advanced services.

The current regulatory context must also be borne in mind as the Committee continues its work on this measure. The Commission, of course, has open proceedings on universal service and intercarrier compensation reform, and is fully engaged in developing and implementing the national broadband plan called for by Congress in the American Recovery and Reinvestment Act of 2009. Indeed, the Commission will deliver its national broadband plan to Congress in just a little more than three months. Because the goals of the national broadband plan must include the availability of broadband services to every American within the near future, fundamental universal service reform is integrally related to the success of that plan. Legislative and regulatory attempts to reform universal service must therefore be carefully calibrated so as not to

impede the development of the national broadband plan, or to result in wasted resources or inefficiencies.

In addition, AT&T has urged the Commission to transition all high-cost funding supporting the legacy POTS business model to funding business models that are viable in the hyper-connected digital world in which growing numbers of us live. This transition is fully consistent with, and is in fact necessary for, the preservation and advancement of universal service as required by Congress and the courts. In this transition, we urged the Commission to move toward a support mechanism that is narrowly targeted to areas that are currently unserved by broadband and those areas where providing broadband will always be high-cost. In light of your draft legislation, we recommit to working with you, the Commission, and other stakeholders to find the best path forward.

In sum, we believe, Mr. Chairman, that you and Representative Terry have successfully identified the most critical areas of concern. The draft Universal Reform Act of 2009 is a milestone in the ongoing effort to rein-in out-of-control growth and to establish rational guiding principles for prospective universal service reform.

Mr. BOUCHER. Ms. Moyer.

STATEMENT OF CATHERINE MOYER

Ms. MOYER. Chairman Boucher, Ranking Member Stearns and members of the subcommittee, thank you for inviting me to appear before you today. I am Catherine Moyer, Director of Legal and Regulatory Affairs for Pioneer Communications. Pioneer Communications is a rural telephone company headquartered in Ulysses, Kansas.

Mr. BOUCHER. Ms. Moyer, let me get you to move that microphone just a little bit closer and maybe tilt it up a little bit so that you are speaking directly into it. Thank you.

Ms. MOYER. Pioneer provides local telephone service to approximately 14,000 access lines within a 5,000 square mile service area. Of these 5,000 square miles, only about 15 square miles could be considered town. The remainder of our area is truly rural. In addition to phone service, Pioneer Communications provides cable television service, Internet access and wireless phone service.

I testify today as first vice chairman of the Organization for the Promotion and Advancement of Small Telecommunications Companies. OPASTCO represents more than 530 independently-owned local exchange carriers in 47 States. The companies and cooperatives represented by this association provide numerous services to their communities, including voice, broadband Internet access, video and wireless.

First of all, let me state our appreciation to Chairman Boucher and to Congressman Terry for the leadership that both have shown on the reform of the Universal Service Fund. This program has a successful history of assisting communications and network providers in their service to rural and low income consumers. We look forward to working with Congress and the Federal Communications Commission to make the USF a part of a forward looking solution in the ever changing communications arena.

The goal of universal service policy has been to ensure that every American, regardless of their location, has affordable, high quality access to the public switch network and thereby benefits from a variety of telecommunications and information services.

The provision of a robust telecommunications infrastructure in rural America would never have been possible were it not for the Nation's long-established policy of universal service and the Federal USF. To rural incumbent local exchange carriers, high cost universal service support is a cost recovery program designed to promote infrastructure investment in areas where it would not otherwise be feasible for carriers to provide quality service at rates that are affordable and reasonably comparable to urban areas of the country.

I come before you today to endorse and support the draft legislation offered by Chairman Boucher and Congressman Terry. While the membership of OPASTCO has concerns about some of the specifics contained in the text, the draft is a forward looking document. We commend Congressmen Boucher and Terry for their understanding of the ongoing revenue stream the USF provides and how it benefits consumers in rural and hard to reach areas of our country. This ongoing revenue stream keeps rates affordable for

rural consumers as carriers utilize it to pay for switching, transport and network maintenance. This draft transitions the plain old telephone support fund into a new and modern broadband support fund.

The drafts continues the call for universal service support that allows consumers in rural, insular or high cost areas to have services and rates reasonably comparable to those provided in urban areas. Its contribution mechanisms will allow for the continued support of schools and libraries, rural health care and low income consumers.

This draft expands universal service support to include high speed broadband service and any other service that is determined to be a universal service by the FCC.

We applaud this forward-looking move to provide support for the broadband platform. Broadband is rapidly becoming the mode of delivery for practically everything consumers may need or want regarding communications, voice, data, education, health care and entertainment, just to list a few.

Recipients of the high cost fund support would be required to provide high speed broadband service defined as a download rate of 1.5 megabytes per second. This draft mandates that the FCC review that speed requirement by annually and make necessary adjustments. OPASTCO suggests that the FCC also review the USF funding level and ensure that the amount allows for the adjusted speed requirements.

Additionally, OPASTCO supports the eligibility criteria and waiver process included in the draft which takes into consideration the many difficulties experienced by communications providers in rural and hard-to-reach areas.

Additionally, OPASTCO supports, one, broadening the base of contributors to the Universal Service Fund. Expanding this base recognizes our modern broadband world. A broadband network with the most possible connections, regardless of technology, is the most valuable network.

Two, the cost controls included with the limitation of the number of competitive carriers that receive support.

Three, the recognition of the importance of intercarrier compensation and its contribution to the USF with the mandate that the FCC act on intercarrier comp reform within one year.

Four, the permanent exemption ever the USF from the Antideficiency Act.

Five, the prohibition of the primary line rule.

And six, the audit procedures, performance measures and reports to Congress.

In closing, OPASTCO endorses and supports draft legislation offered by Chairman Boucher and Congressman Terry. OPASTCO and its members look forward to working with Congressmen Boucher and Terry, members of the subcommittee and Members of Congress to ensure that consumers in rural America are not left behind and that they have access to services and rates that are reasonably comparable to those provided in urban areas.

I look forward to your questions.

Mr. BOUCHER. Thank you very much, Ms. Moyer.

[The prepared statement of Ms. Moyer follows:]

TESTIMONY

OF

CATHERINE MOYER

PIONEER COMMUNICATIONS

ON BEHALF OF

THE ORGANIZATION FOR THE PROMOTION AND ADVANCEMENT OF SMALL TELECOMMUNICATIONS COMPANIES

BEFORE THE

U.S. HOUSE OF REPRESENATIVES

COMMITTEE ON ENERGY AND COMMERCE

SUBCOMMITTEE ON COMMUNICATIONS, TECHNOLOGY AND THE INTERNET

NOVEMBER 17, 2009

Chairman Boucher, Ranking Member Stearns, and members of the subcommittee, thank you for inviting me to appear before you today. I am Catherine Moyer, director of legal and regulatory affairs for Pioneer Communications. Pioneer Communications is a rural telephone company headquartered in Ulysses, Kansas, a town with a population of about 6,500. Ulysses is the largest town within our service area. Pioneer Communications provides local telephone service to approximately 14,000 access lines within a 5,000 square mile service area. Of these 5,000 square miles, only about 15 square miles would be considered to be "town." The remainder of our area is truly rural. We have 2,700 route miles of copper plant, with only 375 miles being considered to be "town." Our overall subscriber density per square mile of service area is just under 2 subscribers per square mile.

In addition to phone service, Pioneer Communications provides cable television service, Internet access, and wireless phone service. Our Internet access is provided using dial-up, DSL and cable modem technology. We currently have just over 7,000 Internet customers, of which only 500 are dial-up. The other 6,500 Internet customers are high-speed customers that receive at least 6Mbps downstream and 512Kbps upstream. As percentages, high-speed customers account for 39% of our access lines and 57% of our customers. If dial-up is factored in, the total Internet access as a percentage of our access lines is 42%, and as a percentage of customers is 62%.

I testify today as first vice-chairman of the Organization for the Promotion and Advancement of Small Telecommunications Companies - OPASTCO. OPASTCO

represents more than 530 independently owned local exchange carriers in 47 states. The companies and cooperatives represented by this association provide numerous services to their communities including voice, broadband Internet access, video and wireless.

First of all, let me state our appreciation to Chairman Boucher and to Congressman Terry for the leadership that both have shown on the reform of the Universal Service Fund (USF). This program has a successful history of assisting communications network providers in their service to rural and low-income consumers. We look forward to working with Congress and the Federal Communications Commission to make the USF a part of the forward looking solution in the ever changing communications arena.

The goal of universal service policy has been to ensure that every American, regardless of location, has affordable, high-quality access to the public switched network and thereby benefits from a variety of telecommunications and information services. The provision of a robust telecommunications infrastructure in rural America would never have been possible were it not for the nation's long-established policy of universal service and the federal USF. To rural incumbent local exchange carriers, high-cost universal service support is a cost recovery program designed to promote infrastructure investment in areas where it would not otherwise be feasible for carriers to provide quality service at rates that are affordable and reasonably comparable to urban areas of the country. Without high-cost support, this investment would not have occurred in the past and may not occur in the future.

I come before you today to endorse and support the draft legislation authored by Chairman Boucher and Congressman Terry. While the membership of OPASTCO has concerns about some of the specifics contained in the text, the draft is a forward looking document. We commend Congressmen Boucher and Terry for their understanding of the ongoing revenue stream the Universal Service Fund provides and how it benefits consumers in rural and hard to reach areas of our country. This ongoing revenue stream keeps rates affordable for rural consumers as carriers utilize it to pay for switching, transport, and network maintenance. This draft transitions the plain old telephone support fund into a new and modern broadband support fund.

The draft continues the call for universal service support that allows consumers in rural, insular, or high-cost areas to have services and rates reasonably comparable to those provided in urban areas. Its contribution mechanisms will allow for the continued support of schools and libraries, rural health care and low-income consumers.

The draft expands universal service support to include high-speed broadband service and any other service that is determined to be a universal service by the Federal Communications Commission (FCC). We applaud this forward looking move to provide support for the broadband platform. Broadband is rapidly becoming the mode of delivery for practically everything consumers may need or want regarding communications: voice, data, education, health care and entertainment, just to list a few.

Entities that are required to contribute to the funding of the USF in the draft will reflect our modern broadband world. The FCC will be able to consider contributions based on revenues derived from intrastate, interstate and foreign communications by qualified communications service providers; working telephone numbers used by communications providers; and, any other current or successor identifier protocols or connections to the network used by communications service providers. This expansion of the contribution base should keep low volume users from paying more than their fair share into the fund.

Cost controls are included in the draft by providing for a limitation on the number of competitive carriers that receive support from the fund. We also appreciate the draft's recognition of the importance of intercarrier compensation and its relationship to the USF with the mandate that the FCC act on intercarrier compensation reform within one year. OPASTCO supports the removal of impediments to sufficient support mechanisms, including the parent trap.

Recipients of high-cost fund support would be required to provide high-speed broadband service defined as a download rate of 1.5Mbps. The draft mandates that the FCC review that speed requirement biennially and make necessary adjustments. OPASTCO suggests that the FCC also review the USF's funding level and ensure that the amount allows for the adjusted speed requirements. Additionally, OPASTCO supports the eligibility criteria and waiver process included in the draft which takes into consideration the many difficulties experienced by communications providers in rural and hard to reach areas.

We greatly appreciate the draft's permanent exemption from implementation of the Anti-Deficiency Act on the USF and the prohibition of the primary line limitation. The draft also addresses the issue of phantom traffic in a positive manner.

Accountability is addressed in Title II of the draft and we support the audit procedures, performance measures and reports to Congress that are included in the draft. For the Universal Service Fund to continue to serve consumers in a proper manner, accountability initiatives and procedures must be conducted in a way that gets verifiable and cost effective results. Adequate training for auditors using the FCC's prescribed USF criteria must be a priority, and this draft legislation provides for that.

In closing, OPASTCO endorses and supports the draft legislation authored by Chairman Boucher and Congressman Terry. OPASTCO and its members look forward to working with Congressmen Boucher and Terry, members of this subcommittee, and other members of Congress to ensure the consumers in rural America are not left behind, and that they have access to services and rates that are reasonably comparable to those provided in urban areas.

Mr. BOUCHER. Commissioner Baum.

STATEMENT OF RAY BAUM

Mr. BAUM. Chairman Boucher, Ranking Member Stearns, I appreciate the opportunity to testify in front of the committee today.

I want to do a little side note. When Commissioner Walden and I were serving in the Oregon legislature, we were so young we were known as the "pablum twins."

Mr. WALDEN. Thanks for sharing that, Ray.

Mr. BAUM. We have grown up, as you can tell.

Mr. Chairman, I would like to thank you and Congressman Terry for your leadership on this important issue. I am here today in my capacity as a member of the Oregon Public Utility Commission and chair of the NARUC Telecommunications Committee and State chair of the Federal State Joint Board on Universal Service.

It is my personal belief that broadband deployment is essential to the economic development and quality of life for the rural communities of America. Those rural communities who don't have adequate broadband will be just as disadvantaged economically as those rural communities in the first half the 20th Century that didn't have access to electricity or paved highways. Reform of intercarrier comp and USF is essential to that broadband deployment.

I begin by testifying on behalf of NARUC. NARUC specifically endorses the following provisions of the bill: The provision that protects the States' ability to assess USF funds. That that fund generates $1.3 billion for States in 23 different States through that contribution base. We are grateful for the opportunity to continue to assess that.

We also support the Antideficiency Act exemptions. We also support the continued role of the Federal State Joint Board on Universal Service in recommending USF reform and designating supportive services. We would suggest that after the initial 18-month period that the bill requires the FCC to act, that you add an additional 1-year time clock on the FCC to act on any further joint board recommendations.

We are very pleased with the language requiring compliance with applicable State and Federal consumer protections and service quality standards. This is key to consumer protection and it keeps the State consumer cops on the beat.

We do have some concerns about the preemption language in interstate rate setting. We would propose that we use a more cooperative approach, conditioning receipt of USF funds in States that mirror the interstate rate, and in return for the foregone interstate revenues, those funds would be transferred to the Federal fund. In any case, we are committed to working with you on modifying this provision of the bill.

The remaining issues NARUC has not taken a position on, so I will speak to them based on my own opinion as my experience as Chair of the Universal Service Joint Board and as former chairman of the NARUC Intercarrier Compensation Task Force. I note that the draft legislation echoes many of the provisions in the Joint Board's recommendation of 2 years ago. I applaud you for designating broadband as a supported service. Two years ago this month, the Joint Board made that same recommendation.

I would encourage you to make sure that deployment of broadband should be a condition of receiving universal service funding. The high cost fund should be transitioned to a broadband fund and it should focus on unserved areas and anchor institutions.

Mr. Chairman, I believe your 1.5 megabytes is a good start, but let me just suggest to you it might be better to realize what is coming in the future. I want to kind of up the ante. I think that 3 to 5 megabytes for residential customers and 20 to 50 megabytes for anchor institutions has to be the minimum if we are going to face the new broadband world, with appropriate waivers for certain unserved areas. These service levels are already standard in most urban areas and should be comparatively available in check chest as required in the draft legislation.

The wireless auction provisions of the bill are a positive step in the right direction. It is a de facto repeal of the identical support rule. However, there is a seismic shift in the wireless broadband looming on the horizon in open networks. It will be the communication device of choice. People want to be mobile and want to have broadband. This is a looming reality. It is coming upon us and it involves huge amounts of spectrum and exponential increases in backbone capacity.

I would urge you too to encourage the FCC to transition intercarrier compensation rates to zero in a 5- to 7-year period. They are going away anyway and we might as well plan for it, and it won't work at all in the broadband world. We need to focus on the efficient use of the funds.

I also want to add my support to the provisions on phantom traffic, traffic pumping, auditing, capping the fund, which the Joint Board originally recommended, subject to appropriate adjustments based on intercarrier compensation reform, and the repeal of the parent trap. The Universal Service Fund should be based as much as possible on forward-looking cost models and based on a wire center basis as we go forward.

Mr. Chairman, expeditious implementations the major provisions of this draft legislation will greatly mitigate the digital divide that exists today between urban and rural American and will prevent that divide from becoming an irreversible chasm.

I personally support the major provisions of your bill. We cannot address these issues soon enough. The Joint Board is committed to working with you and the FCC in achieving these goals. We thank you again for your leadership.

Mr. BOUCHER. Thank you very much, Commissioner Baum.

[The prepared statement of Mr. Baum follows:]

Testimony of

Ray Baum, Commissioner
Of the
Oregon Public Utility Commission

On behalf of the

National Association of Regulatory Utility Commissioners

before the

United States House of Representatives
Subcommittee on Communications, Technology and the Internet
of the Committee on Energy and Commerce

Hearing on the Universal Service Reform Act of 2009 Discussion Draft
November 17, 2009

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INTRODUCTION

Chairman Boucher, Ranking Member Stearns and members of the Subcommittee, I appreciate the opportunity to testify today on reform of the federal universal service fund (USF) program. I thank you for calling this hearing and commend Chairman Boucher and Representative Terry, the sponsors of the bill, and the members of this Subcommittee for your leadership on this important issue.

My name is Ray Baum. I am a Commissioner with the Oregon Public Utility Commission and the Chair of the National Association of Regulatory Utility Commissioners' (NARUC) Committee on Telecommunications. I formerly chaired a NARUC task force on intercarrier compensation. I am also currently a NARUC representative on the Federal Communications Commission's Federal-State Joint Board on Universal Service. As the State Chair of that board, I have spent hundreds of hours intensely focused upon the issues covered by your draft legislation. No one seriously disputes that reform of the existing mechanisms are long overdue.

I personally believe the issue of broadband deployment is of utmost importance to the economic productivity and quality of life of the entire country. Communities that do not have access to sufficient levels of high speed broadband within the next few years will be just as economically disadvantaged as those communities in the first half of the 20th century that did not have access to electricity and paved highways.

The reform of USF and ICC is integral to achieving that deployment. In certain key areas, this discussion draft is a major step forward. In my personal view, there is no question that, overall, it moves the policy debate much closer to a practical resolution.

I am testifying today on behalf of NARUC, which represents the State public utility commissioners in each of your States that have oversight responsibilities for all the critical utility infrastructures – telecommunications, energy, and water. Your home-State commissions have considerable expertise on the issues raised by this legislation. They are focused on what is best for your State and your constituents. A discussion with your own State's experts can only provide a better basis for each of your decisions on this legislation. It is a contact worth making.[1]

While NARUC does not have a position on every aspect of the *Universal Service Reform Act of 2009 Discussion Draft*, we have endorsed specific approaches on certain key issues. Moreover, where NARUC has not taken a specific position, I have included my personal views on other issues raised by the legislation.

Four sections of the draft adopt solutions NARUC has specifically endorsed: the protection of State program contribution options; the long overdue inclusion of a *permanent* Antideficiency Act exemption; assuring the continued utility of the Joint Board process; and, the expressed recognition of an integral State role on consumer protection and service quality standards. On each of these issues, the draft says the right things. Although NARUC's staff is

[1] To get detailed contact information for experts from your State's public service commission, go to: http://www.naruc.org/commissions.cfm and click on your State.

still analyzing the details of the draft, there is at least one other section addressing intercarrier compensation reform that raises serious concerns for our members. We look forward to working with the Committee on those sections.

Protection of State Universal Service Programs' Contribution Base

NARUC supports efforts to equitably distribute the funding base of the federal Universal Service Fund (USF) in a technology-neutral manner. We appreciate provisions in the *Universal Service Reform Act of 2009 Discussion Draft* that allow the Federal Communications Commission to do so. All service providers should share the responsibility for maintaining universal service.

As Congress indicated in the 1996 legislation, State programs have always been a critical and significant component of cooperative efforts to assure affordable phone service for high-cost areas and low-income individuals and promote Internet connectivity for schools, medical facilities and libraries.

Universal Service is a responsibility States and the federal government share. According to one 2006 report, about 22 State programs distribute at least $1.3 billion, or approximately 17 percent of the overall national commitment to Universal Service.[2] Currently, at least 22 States

[2] Jing Liu & Edwin Rosenberg, *State Universal Service Funding Mechanisms: Results ofthe NRRI's 2005–2006 Survey*, National Regulatory Research Institute (July 2006). ("[T]wenty two jurisdictions, or 43 percent, currently have either a functioning high-cost USF, a functioning high-cost USF under revision, or an approved but not functioning fund . . . All but five . . . require Commercial Mobile Radio Service providers to contribute . . . two . . . require Voice over Internet Protocol service providers to contribute . . . Thirty-three commissions . . . have a state low-income program, which provides a subsidy to basic local residential telephone services . . . Nine . . . have a subsidy program for schools and libraries. Seven . . . have a subsidy program for rural health care facilities . . . five . . . have a subsidy program for advanced telecommunication services [separate from] other subsidy programs for schools, libraries . . ." available online at: <http://nrri.org/pubs/telecommunications/06-09.pdf>.

have high-cost universal service programs, and at least 33 have low-income programs. Others have programs to promote the deployment of advanced services generally and/or rural health care/schools and library programs. Many of these State programs are supported in part or whole by assessments on carriers providing voice telephony services. All advance Congress' goals to promote universal service and deployment of advanced infrastructure.

There is no question these programs reduce the overall burdens on existing federal programs. There is also no question that elimination of these programs will significantly undermine the goals of this draft legislation.

Funding is critical. Like the federal programs, state programs face funding challenges as the telecom industry evolves and contribution requirements fall disproportionately on a shrinking base of services.

This draft, in Section 108, provides a critical step forward by assuring States can require "communications service providers" to contribute to State programs. *The FCC has the authority now to eliminate the need for the new definition of "communications service provider" by making a long overdue final classification of the status of facilities-based and so-called nomadic VoIP providers.* But it is unclear when or if they will do so.

Even so, this section explicitly expands the methods the FCC can consider as funding bases – and critically – also expands the new methods available to the States. This is a

significant improvement. This provision is good for States, good for the federal program and good for consumers.

NARUC looks forward to working with the legislation sponsors on the scope of State assessment authority. We respectfully suggest the best way to guarantee the long-term stability of State programs is to slightly adjust the draft to assure State assessment authority is co-extensive with that of the federal program.

Antideficiency Act Exemption

NARUC strongly supports the permanent exemption of the federal programs from the provisions of the Antideficiency Act (ADA).

The Universal Service Fund must be run efficiently to maximize the public benefit. That is why we support a permanent exemption of the USF from the ADA. An August 2004 decision by the Office of Management and Budget to apply the Act to the federal USF programs was a mistake. That decision requires the Universal Service Administrative Corporation (USAC) to keep cash or government securities on hand for every outstanding work order, as opposed to collecting investment earnings while such orders are pending for a year or more. *This makes the whole program much more expensive and far less efficient.* Fortunately, Congress has, every year since, temporarily exempted USF from the ADA. However, the current exemption expires next month and a permanent fix is long overdue.

The draft's exemption allows the FCC to continue to invest contributions in liquid, interest-bearing, government-backed securities until they are disbursed. Making the exemption

permanent assures no lapse in this efficient use of taxpayer dollars and removes the annual uncertainty of whether the extension will be renewed.

Federal-State Joint Board on Universal Service Reviews of Supported Services

NARUC welcomes the language in the discussion draft maintaining the Joint Board and requiring a referral of the definition of supported services every five years. The previous legislation only required "periodic" reviews of supported services. The FCC has elicited a number of recommendations from the Board since the 1996 legislation – but a definitive timetable for reviews is definite improvement in the governing legislation that will ensure that definitions keep pace with adoption trends and technology.

The legislation also provides the FCC and the Joint Board with a clear outline of issues for deliberation and a deadline for its initial recommendation on both the definition of supported services and the Section 214 inquiries. Aside from NARUC, I would like to add my personal commitment – and that of my State colleagues on the Joint Board – to work with you on this legislation, and with our FCC colleagues on the inquiries Congress designates when the President signs it into law.

States, because of their long history with rates, facility-siting, safety regulation, and consumer protection, and also because of their proximity and knowledge of local markets, demographics and market participants, have crucial insights into the real costs and real benefits of these federal programs. The sponsors were wise to require a Joint Board recommended decision as a prerequisite for FCC action on issues like the definition of supported services.

Here too, there is one area – probably an oversight - where NARUC would like to suggest a minor improvement. The draft eliminates the current provision in 47 U.S.C. § 254(a)(2) that requires the FCC to "complete any proceeding to implement …recommendations from any joint board on universal service within one year after receiving such recommendations." That section provides some impetus for the FCC to do something (other than ignore) a recommendation from a Joint Board. Without a provision like it, the FCC is free to sit on a recommendation – perhaps for the entire five years until the time for the next recommendation comes due. Inclusion of some analogous provision in the final bill will assure not only that the definition of supported services is actually reviewed at least once every five years, but also that the FCC will have some time pressure to act on the recommendations.

Partnership – not Preemption: Keeping State Consumer Cops on the Beat

The work of a 2004 NARUC legislative taskforce resulted in the release and adoption of a white paper that focused on the evolving nature of federalism. That paper ultimately concludes that good public policy should be based on the core competencies of agencies at each level of government – state, local and federal.

For example, effective consumer protection depends largely on where the consumer is domiciled, regardless of whether calls are placed to in-State or out-of-State destinations. Requests to interconnect, and presumably any needed service quality standards for government subsidized services obviously depend on where the relevant facilities are located. States

commissions excel at, among other things, delivering responsive consumer protection and resolving interconnection disputes.

We are particularly pleased that the draft bill's sponsors, in specifically requiring *subsidized* carriers to "comply with applicable State and federal consumer protection and service quality standards," *explicitly recognize the immutable logic of keeping State consumer cops on the beat.* As President Obama recognized in a recent Executive Order: "Throughout our history, State and local governments have frequently protected health, safety, and the environment more aggressively than has the national Government."[3]

This amendment to Section 214 recognizes the key role States play to ensure consumers receive high service quality and are treated fairly. The federal government will *always* lack the manpower to help *all* consumers in *every* State. In many cases, whatever assistance they may provide will be complicated by distance and time zones. Moreover, this section also assures that companies that seek federal (and State) subsidies actually deliver the promised quality services.

Intercarrier Compensation

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[3] May 20, 2009 *Memorandum for the Heads of Executive Departments and Agencies.* "["From our Nation's founding, the American constitutional order has been a Federal system, ensuring a strong role for both the national Government and the States. The Federal Government's role in promoting the general welfare and guarding individual liberties is critical, but State law and national law often operate concurrently to provide independent safeguards for the public. Throughout our history, State and local governments have frequently protected health, safety, and the environment more aggressively than has the national Government . . . [t]he general policy of my Administration that preemption of State law by executive departments and agencies should be undertaken only with full consideration of the legitimate prerogatives of the States... Executive departments and agencies should be mindful that in our Federal system, the citizens of the several States have distinctive circumstances and values, and that in many instances it is appropriate for them to apply to themselves rules and principles that reflect these circumstances and values. As Justice Brandeis explained more than 70 years ago, "[i]t is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.". President Barack Obama, available at: http://www.whitehouse.gov/the_press_office/Presidential-Memorandum-Regarding-Preemption/

The section of the bill that raises the most concern is the provision giving the FCC *carte blanche* to reform intercarrier compensation for both interstate and intrastate traffic. The costs and benefits of intercarrier compensation reform will vary from State to State, as will the advice of your individual State commissions, but at the end of the day, we must all find some common ground. NARUC, over the past 10 years, has created a series of recommendations for reform of these charges. Indeed, I was part of a multi-year task force that brokered a dialogue among every segment of industry seeking a consensus solution to problems raised by the current regime.

For States that already mirror the interstate regime, the preemption is not necessary. For others the preemption is problematic. The differential impact on each State makes a one-size-fits-all approach potentially punitive. NARUC has specifically endorsed several key prerequisites to intercarrier compensation reform, including:

[1] The compensation system should ensure that revenues, cost assignment, and the risk of confiscation are jurisdictionally consistent for all classes of traffic.

[2] State commissions should continue to have a significant role in establishing rates and protecting and communicating with consumers. The role should reflect their unique insights, as well as assure substantial discretion in developing retail rates for services provided by providers of last resort, even if a unified compensation solution is adopted. A proposal preserving a significant State role that fits within the confines of existing law is preferable.

[3] The estimated cost impact on a carrier-by-carrier basis, by State, must be computed before a decision is made whether to adopt a new intercarrier compensation plan.

[4] The FCC should be required to regularly revisit its cost allocation rules for regulated/ nonregulated services. Costs that should not be recovered through regulated rates ought to be excluded from the computation of intercarrier compensation rates.

[5] Before any new intercarrier compensation plan is implemented, the effect of the plan on local exchange rates, including both interstate and intrastate subscriber line charges (SLCs), should be computed.

[6] Even when a referral to a Joint Board is not mandated by law, in order to ensure State input the FCC should make a referral, and the Joint Board should act on that referral, in an expedited manner.

NARUC stands willing to work with you to modify this provision to meet our mutual goals of reducing access charges in a competitively neutral manner while not over burdening consumers or the universal service fund.

Other Issues and Some Personal Observations

NARUC has long been a proponent of efficiency in operation of the universal service programs. While NARUC has not taken a specific position on the capping mechanism, the audits provisions, the performance setting and review measures, the wireless auction mechanism, and the traffic pumping and phantom traffic provisions in the draft, combined they show an interest in and movement towards a more efficient federal mechanism that does place – at least some - limits on fund growth.

Since NARUC has NOT taken a specific position on these mechanisms – I wanted to take a moment and express my *personal* recommendations on how Congress or the FCC under its direction should proceed.

First, *in my opinion*, as provided in the discussion draft and also as endorsed by the Joint Board in its 2007 Recommendation Decision, high-speed broadband should be declared a supported service. This should be done as soon as possible. As we speak the digital divide between rural and urban America is growing exponentially and it is now two years since the Joint Board made its initial recommendation to the FCC to declare it so.

Second, *in my view*, deployment of high-speed broadband should be a condition for receiving federal funding. Receipt of high-cost support should be contingent on having a 3-5 year plan to deploy high-speed broadband to high-cost rural areas. Over that time the current high-cost fund based on the costs of a public switch telephone network could be converted to a high speed broadband deployment fund. Carriers would recover their broadband network costs from affordable end user rates and support, where appropriate, from the new fund. The target speeds should be 20-50 mbs for anchor institutions and 3-5 mbs for residential customers.

Third, *I personally believe* intercarrier compensation rates for all forms of INTERstate traffic should be transitioned to zero over five years. NARUC has not specifically addressed the length of any transition and the Association strongly believes preemption of INTRAstate authority is unnecessary and inappropriate. I believe one way to avoid preemption is to condition receipt of federal high-cost support on the State reducing in stages intrastate access

charges to mirror Federal rates. States that adopt Federal target rates could transfer foregone intrastate revenue to the Federal USF. These funds would form the basis of broadband build out fund that would be focused on high-speed broadband build out in unserved areas.

Fourth, Rural LECs support from the new broadband fund would be based on actual costs incurred in provisioning high-speed broadband subject to rate-of-return regulation with all revenues and expenses accounted for. Mid-size and RBOC funding would be frozen at current levels with additional support limited to infrastructure build out targeted to unserved areas based on a cost modeling and/or in combination with RFPs or competitive bidding. This support for infrastructure deployment to unserved areas could be subject to a 20% company match. After infrastructure build out RBOC funding for high cost rural areas would be phased out. Funding for the Mid-size companies for broadband deployment in unserved areas would be also be phased out. Continued support for mid-size carriers as frozen under the high-cost fund would be reviewed at the end of the five year period to determine the level of support required to maintain the appropriate broad services for their high-cost rural areas on a going forward basis.

Fifth, it is my opinion that the current funding of wireless service in high-cost rural areas is largely dysfunctional with a few exceptions. The draft bill's discussion of a wireless auction is a very positive step in the right direction. At some point in the very near future Congress and the FCC may find that the consuming public has chosen mobile high-speed broadband as its communication technology of choice with the expectation that it be available almost everywhere.

Finally, the draft bill's provisions on traffic pumping, phantom traffic, auditing, capping the fund(subject to ICC adjustments and repeal of the parent trap) and repeal of the identical support rule are all excellent and should be timely implemented.

I personally believe expedited implementation of the above concepts will help insure a smooth transition to a broadband world where voice is just an application, where minutes and access charges don't matter. Such an effort will greatly mitigate the digital divide that is otherwise inevitable. This will help ensure that all Americans, regardless of where they live, will enjoy the economic productivity and enhanced quality of life available through the broadband world.

Conclusion

Universal service has long been in need of reform. We appreciate Chairman Boucher and Representative Terry's leadership on this issue. This bill is a major step forward in the long journey to meaningful reform. NARUC looks forward to working with this Subcommittee and the full committee on this draft as it advances through the committee process. Thank you again for your invitation to testify before you today and I look forward to any questions you may have.

Mr. BOUCHER. Mr. McSlarrow.

STATEMENT OF KYLE MCSLARROW

Mr. MCSLARROW. Mr. Chairman, Mr. Stearns, distinguished members of the subcommittee, thank you for having me here.

Mr. Chairman, I fully appreciate the difficulty in assembling this jigsaw puzzle known as Universal Service Fund reform, and I congratulate you and Mr. Terry on producing a discussion draft which, I think, is a valuable step toward addressing issues like cost containment, injecting notions of competitive neutrality, both on the distribution side and on the contribution side.

I want to just in the time I have focus on one area where I think the draft might be improved with a proposal that I think complements the direction that you and Mr. Terry are taking, these reforms, and it is to note, I know that members of the subcommittee are aware that the cable industry offers broadband service to 92 percent of American households.

Less well-known, perhaps, is that we offer phone service, competitive phone service, to 80 percent of American households, and I am told it is going to actually reach 90 percent by the end of this year. In less than a decade, we have gone from less than 1 million phone customers to over 20 million, and, with very few exceptions, cable-digital phone service is unsubsidized by the Universal Service Fund reform.

So our view is that that change in the competitive landscape as you think about the future of universal service ought to mean something.

Our proposal is this: That in the rural study areas, for example, that receive high cost support today, we already know that 40 percent of those rural study areas have a wire line unsubsidized competitor, usually a cable company, but not necessarily. We don't actually know the answer in those other areas. Because of statewide averaging, it is harder to know for the non-rural local exchange carriers.

But in those markets, in those areas where we would say there is a competitive unsubsidized wire line phone service to more than 75 percent of the households, we would say Universal Service Fund, high cost Universal Service Fund support, should cease in that marketplace.

The alternative is in those regions or States where the State legislature has itself determined that the level of competition means that the retail rates of an incumbent carrier should be priced to regulated, we also say that would be evidence there is extant competition such that Universal Service Fund support should cease.

So a proposal that we would submit respectfully for your consideration is that we set up a process at the FCC where people can make a showing with one of those two triggers, either evidence of significant competition, evidence of deregulation by the States, and set up a process where people can figure out how to focus on those noncompetitive areas where there indeed might still be requirements for high cost support.

Every member of this subcommittee today I think has in one way or another suggested that they want to put more dollars on target

in the most efficient way possible. I think injecting notions of the changed competitive landscape will help you toward that goal.

I look forward to answering your questions on that or other parts of the discussion draft.

Mr. BOUCHER. Thank you very much, Mr. McSlarrow.

[The prepared statement of Mr. McSlarrow follows:]

TESTIMONY OF KYLE McSLARROW
PRESIDENT AND CEO
NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION

on the

Discussion Draft of the Universal Service Reform Act of 2009

before the

Committee on Energy and Commerce
Subcommittee on Communications, Technology, and the Internet

UNITED STATES HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.

November 17, 2009

TESTIMONY OF KYLE MCSLARROW

PRESIDENT & CEO, NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION

Good morning, Chairman Boucher, Ranking Member Stearns, and Members of the Subcommittee. My name is Kyle McSlarrow and I am the President and Chief Executive Officer of the National Cable & Telecommunications Association. Thank you for inviting me today to testify on the discussion draft of the Universal Service Reform Act of 2009. We welcome the discussion draft as a valuable and important first step toward bringing the universal service fund (USF) into the 21st Century.

NCTA represents cable operators serving more than 90 percent of the nation's cable television households and more than 200 cable program networks. The cable industry is the nation's largest provider of residential high-speed Internet service, having invested more than $145 billion since 1996 to build two-way, interactive networks with fiber optic technology. Cable companies also provide state-of-the-art digital telephone service to more than 20 million American consumers. Cable operators are committed to expanding access to quality voice and Internet services, and the dramatic growth in cable broadband subscribers is evidence of their success in doing so.

As a major contributor to the federal universal service fund, the cable industry has a significant interest in USF issues. We share and applaud your goal to cap the size of the high cost fund and transition away from a monopoly-era support program and toward a more modern, neutral, and forward-looking mechanism. With the same goal in mind, we recently asked the FCC to open a rulemaking to reduce high cost support in areas where there is durable unsubsidized competition. We believe the growth of local competition gives Congress the

opportunity to curb the growth of the high cost fund and turn its attention to how best to support the deployment and adoption of broadband services. Based on our research, we have concluded that there is up to $2 billion dollars in high cost subsidies currently being provided in these competitive areas.

Other elements of the discussion draft would improve the implementation and administration of the USF programs. For instance, the draft adds the principles that universal service mechanisms should be competitively neutral and that such mechanisms should be "explicit" as well as "specific, predictable and sufficient." These are valuable additions to the framework on which the FCC and the Federal-State Joint Board base policies for the preservation and advancement of universal service. It is also past time to recognize, as the discussion draft does, that providers other than traditional common carriers should be eligible to receive USF support. We are pleased that the bill would confirm the FCC's statutory authority to adopt a numbers-based contribution mechanism. Finally, we support the provisions in the discussion draft that would outlaw "traffic pumping" and the use of "phantom numbers" that seek to exploit or avoid the current access charge rules – and direct the FCC to reform those rules through comprehensive intercarrier compensation reform.

We also agree that it is appropriate to consider tailored broadening of the universal service program to include carefully targeted subsidies for broadband service. As the discussion draft recognizes, however, the transition from a voice-centric USF system to one that supports broadband will entail significant changes. We recommend the Committee consider changes that not only include measures to control costs through a meaningful cap on the size of the high cost fund, as the discussion draft acknowledges, but also include a reduction in high cost program support where it is no longer needed, and the tailoring of support for broadband services to areas

and consumers that currently lack access to such services. A renewed USF program must also include reform of contribution mechanisms and provide a new method of calculating high cost program support. I will discuss each of these issues in turn.

The Local Exchange Marketplace Has Changed Substantially Since Congress Created the USF Program in 1996

When Congress directed the FCC to create the Universal Service Fund program in 1996, incumbent local exchange carriers (ILECs) had a monopoly in the local exchange market, interexchange carriers were the only companies providing long distance service, wireless was a nascent service generally considered to be a luxury, and broadband Internet access was virtually nonexistent. Thirteen years later, the marketplace has changed completely. Cable operators today provide voice service to over 20 million voice customers, often offering it in rural areas throughout the country. Already, cable's entry into the voice market has produced billions of dollars in consumer benefits and promises even greater benefits in the future.

Notwithstanding these fundamental marketplace changes, however, the high cost program operates as if nothing has changed since 1996. Even as millions of Americans take service from facilities-based wireline competitors, and millions more decide they no longer need wireline voice services at all, the high cost fund continues to provide billions of dollars of support for wireline voice services provided by local telephone companies. And because of structural flaws in the high cost program, new entry by facilities-based competitors often has the perverse effect of *increasing* the subsidy a geographic area receives. As a result, the total size of the federal USF program, and the resulting burden on consumers, continues to escalate at a staggering rate. The current USF program is on an unsustainable path, with the contribution factor expected to rise above 14% next year – its highest level *ever* (as compared to under 6% ten years ago).

USF Reform Requires a Cap on the Size of the High cost Fund

A critical first step in USF reform is placing a cap on the size of the high cost fund. Unless high cost support is brought within reasonable bounds, it would be imprudent to expand the high cost fund to cover broadband services. The discussion draft caps contributions for high cost support at its current level, but we are concerned that the growth factor and various exceptions to the cap may not effectively limit the size of the fund. For instance, the discussion draft changes the calculation of high cost support for non-rural carriers and repeals certain existing limits on high cost support – and then permits an upward adjustment to total contributions to account for any increased demand for universal service funding caused by these changes. The unlimited upward adjustment to reflect changes in intercarrier compensation could also substantially increase the overall size of the high cost fund. Finally, the discussion draft permits an upward adjustment in the size of the fund to account for increases in the total number of ILEC access lines, but no reduction in contributions if the total number of ILEC access lines declines.

By increasing the overall level of contributions, all of these upward adjustments will increase the burden on consumers without any real change in the services they receive. Increasing the scope of state USF programs, as proposed in the draft, could add to this burden. On the other hand, any cap on contributions must be implemented in a manner that ensures sufficient USF support for tribal lands, which have been persistently underserved.

High Cost Support Can be Reduced or Eliminated in Areas Where Basic Service Can Be Provided Without Such Support

One of the fundamental problems with the current high cost scheme is that it does not include any mechanism for reassessing which providers and areas should receive support. With competition now firmly entrenched in much of the United States, we believe a mechanism that

directs high cost support away from areas with unsubsidized competition can and should be added to the USF framework to ensure that support is targeted to areas that require it. In our view, this mechanism would advance the objectives of the discussion draft.

An effective cap in the size of the high cost fund is absolutely necessary to protect consumers and promote greater efficiency. Particularly if Congress decides to bring broadband within the scope of USF, consumers should not be expected to pay any more than they do today. We believe that the growth of competition in the provision of voice service offers an opportunity to bring the high cost fund under control. Specifically, USF support can be reduced or even eliminated in areas where there is unsubsidized wireline competition. Cable voice service is available to approximately 80 percent of U.S. households. In rural LEC study areas, more than 6.6 million households, or 43 percent, have access to cable voice services. The presence of an unsubsidized competitor in a market is, in our view, clear evidence that universal service support is no longer necessary. The Universal Service Reform, Accountability, and Efficiency Act Of 2008, introduced by Reps. Barton and Stearns, likewise recognized that USF support is not needed where consumers have access to affordable voice communications offered by one or more unsubsidized providers. In markets where both wireline providers are currently receiving support, by contrast, continued support may be necessary to ensure that consumers continue to enjoy a competitive choice.

Briefly, NCTA's proposal envisions a two-step process by which the Commission would reassess the level of USF support for providers in areas experiencing unsubsidized wireline competition. In *Step 1*, a petitioner could challenge the necessity for high cost support by demonstrating that one of two triggers is satisfied:

> Trigger 1 – More than 75% of households in the relevant telco study area can purchase service from an unsubsidized facilities-based wireline competitor (or more than 50% of

households can purchase such service and there is evidence that competitors are not avoiding higher cost areas).

Trigger 2 – The state has deregulated the rates for local exchange service in the relevant study area, thus permitting provider costs to be recovered through competitive pricing of voice and other services.

Both triggers constitute strong evidence that government support is no longer needed to ensure that consumers can receive service at reasonable rates.

In *Step 2*, the ILEC would have the opportunity to demonstrate the minimum level of support needed to ensure that consumers can receive service in areas *not* served by the unsubsidized wireline competitor. The goal is to determine the costs that are attributable to customers in the noncompetitive portion of a study area and that cannot be recovered through the revenues from regulated *and unregulated* services provided to those customers.

NCTA's proposal is a modest, but critical, first step toward meaningful and needed USF reform. It targets areas where continued government support is least likely to be needed because there is durable competition. In this regard, the proposed competition trigger is satisfied only where there is extensive facilities-based wireline competition; neither wireless nor over-the-top VoIP satisfies that trigger. Indeed, the majority of rural LEC study areas do not currently qualify under this trigger. Even in areas where one of the triggers is satisfied, there are no automatic reductions in support – *LECs will have a full opportunity to identify costs that cannot be recovered from customers, including provider of last resort costs.*

We encourage you to consider NCTA's proposal as part of your USF reform effort. We have provided more detail on this approach – including an economic analysis – in a petition for rulemaking we filed with the FCC the week before last. We believe our proposal should enable the Commission to reassess the continuing need for almost $2 billion in funding. It offers a mechanism for reducing unnecessary high cost support, which will help bring the contribution

factor, and the resulting burden on consumers, under control. Of equal importance, once the existing USF program is on a better trajectory, Congress or the Commission can begin to consider whether, and how, to use USF funding to provide targeted support to programs that promote broadband deployment. It would be premature to use the USF as a vehicle for subsidizing broadband deployment, however, until the high cost program is placed on more solid footing.

We appreciate that the discussion draft also seeks to target high cost support, by calculating support based on wire center costs rather than statewide averages and providing support only to the extent that the ILEC's forward looking costs per line exceed 2.75 times the national average. This proposal assumes, however, that USF support is needed whenever costs are high – without first considering whether unsubsidized investment is taking place that makes such support unnecessary. Combining the wire center approach with NCTA's proposal could help meet the objective of targeting support where it is truly needed.

Even in non-competitive areas, targeting support to wire centers may be difficult to implement because the FCC no longer requires many of these carriers to keep or report the necessary cost data. A regime in which support is calculated based on the cost of providing telephone service to a particular wire center, but where the FCC has no ability to verify those costs, poses a risk of waste, fraud, and abuse. We believe that part and parcel of the wire center approach would be the adoption of appropriate accounting requirements, including a requirement that ILECs allocate common costs to non-supported services provided over their networks (e.g., multichannel video service), before providing USF support based on wire center costs. In this regard, it's also likely that the FCC's USF cost model is out of date and therefore may not be

useful in modeling the cost of modern broadband networks to determine the level of subsidy required in a particular wire center.

Universal Service Support for High-Speed Broadband

The proposed legislation would allow USF support to be used for broadband facilities. Given the importance of broadband to our economy and society and its increasingly central role as a communications medium, we agree that it is appropriate to consider changes in the high cost program to help achieve the national goal of universal access to broadband. But the history of staggering growth in the high cost program suggests that the USF should have a narrowly defined role with respect to broadband, especially in light of additional government support coming from appropriations to programs managed by RUS and NTIA under the Recovery Act. The need for USF support for broadband will be better understood in the coming months, as NTIA and RUS award broadband infrastructure grants under the Recovery Act – and as the state mapping agencies complete their work on a comprehensive inventory of broadband availability.

At a minimum, we encourage you to limit any USF support for broadband deployment to those areas that currently do not have broadband facilities in place. Cable broadband service – which was created from billions of dollars of private investment and without any significant government subsidy – is already available today to 92 percent of U.S. households and subscribed to by more than 40 million of those households. It would be a poor use of scarce government resources to subsidize a broadband competitor in communities – including many small rural communities – where cable operators have invested risk capital to deploy broadband services. Government subsidies for one competitor in markets already served by broadband also might discourage the existing provider from making continued investments in its network facilities.

Given widespread broadband deployment, we believe that Congress should focus on promoting broadband *adoption*. Even in areas with one or more broadband providers, there are often barriers to broadband adoption – such as affordability, lack of a computer or other equipment to connect to the Internet, and low levels of basic "digital literacy." As Congress intended, a portion of the broadband grant and loan programs created by the American Recovery and Reinvestment Act should be targeted at programs to increase broadband affordability and adoption. The existing Lifeline and Link Up Programs are specifically designed to subsidize connectivity for users who need such assistance. Expanding these programs to include access to broadband could help bring the benefits of broadband to low-income consumers. The discussion draft recognizes that broadband support should be available on a technology-neutral basis. In light of the important social objectives served by expanding USF programs to include broadband, however, we believe that funding for broadband adoption programs should come directly from the government rather than by imposing new contribution obligations on service providers or their subscribers.

Reform of the USF Contribution Mechanism

The FCC currently assesses the USF contribution requirement on a provider's retail interstate telecommunications revenue, as required under the 1996 Telecommunications Act. While this approach may have been appropriate in 1996, however, the current monthly surcharge is approaching an unsustainable 13% on monthly telephone bills and, as I noted earlier, is expected to rise to 14% next year. NCTA has long supported basing USF contributions on assignment of telephone numbers and we appreciate that the draft discussion bill would permit the FCC to adopt a numbers-based contribution mechanism. A numbers-based contribution scheme, if properly structured and implemented, holds out the prospect of providing a more

stable, predictable and nondiscriminatory funding mechanism that would affect all providers and end-users of voice services equitably, irrespective of the particular technology used to provide that service. Because the vast majority of American consumers use at least one service with an attached telephone number, a numbers-based contribution requirement reaches an extremely broad base of providers and consumers.

Recognizing the difficulties in identifying and assessing only interstate telecommunications services, the proposed legislation would authorize the FCC to "employ any methodology to assess such contributions" including methodologies based on all communications service revenues or on working telephone numbers. We welcome this statutory reform. However, the bill also would permit the FCC to impose contribution requirements on all "communications service providers," which would authorize contributions based on broadband revenues.

NCTA believes that expanding the USF contribution requirement to include broadband revenues is unnecessary and counterproductive. There is no evidence that an untapped pool of non-contributors would be brought into the system through a broadband assessment. Rather, an assessment on broadband service likely would be paid almost exclusively by people that already contribute on their voice services. Moreover, assessing USF contributions on broadband providers would raise the cost of broadband service for consumers of those services – impeding rather than facilitating the goal of improving broadband penetration. Taking such a step seems particularly ill-advised in the current economic climate, where customers may be particularly sensitive to increased costs.

Competitively Neutral Eligibility for Funding

If the high cost program is to achieve the goal of competitive neutrality, any entity that can provide services of sufficient quality should be eligible to receive such support. The discussion draft makes two important changes to support competitive participation in high cost programs: first, by opening the program to all communications service providers able to provide required services, rather than limiting participation to only telecommunications carriers, as in the current program; and second, by defining the service area of an eligible provider to be the area where the provider is licensed or authorized to provide services, rather than requiring all providers to serve the area defined by an underlying incumbent local exchange carrier or seek a waiver. We welcome these important proposed changes to the USF program.

On the other hand, other provisions in the bill detract from the goal of competitive neutrality. For instance, the requirement in the discussion draft to provide broadband service as a condition of eligibility applies only to entities that currently do not receive USF funds. By contrast, existing recipients, *i.e.*, RLECs and ILECs, are excused from this requirement for 5 years – which could enable them to forgo broadband deployment in unserved areas and use USF support to compete against cable companies that have relied on risk capital rather than government support to build out their networks. More broadly, as noted above, the bill would also allow LECs to continue to obtain high cost support to compete against unsubsidized wireline providers. We would ask you to reconsider these disparities.

Conclusion

NCTA shares the Subcommittee's belief that USF reform is imperative if the program is to be able to continue to meet its goals and adapt to the significant changes in technology since the program's inception. We remain committed to working cooperatively and constructively with Members of this Subcommittee and other stakeholders to address these issues. We appreciate the opportunity to share our views with you and thank you again for the opportunity to appear today.

Mr. BOUCHER. Mr. Graham.

STATEMENT OF ERIC GRAHAM

Mr. GRAHAM. Mr. Chairman, good morning, and thank you for the opportunity to be here today to present testimony on behalf of Cellular South and as a carrier member of the Rural Cellular Association. RCA's nearly 100 carrier members provide commercial wireless services covering approximately 83 percent of the Nation's geography. As you would expect, much of this territory is in rural areas, and therefore many RCA members, including Cellular South, are eligible to participate in the Federal Universal Service Program. These carriers are using support to build high quality networks in some of the most rural areas of the country.

I cannot emphasize enough that for many rural areas, universal service support is the difference between high quality wireless service and no coverage at all. Today, citizens in thousands of places across the country, such as Floyd, Virginia, Spray, Oregon, Garnavillo, Maine, Bunker Hill, Illinois, and many others are receiving wireless service as a result of the Universal Service Fund program.

For its part, Cellular South has a long history of serving rural areas and has used universal service support to provide service in places like Ellisville, Mississippi, that simply would not have coverage otherwise. This program has allowed Cellular South to build a network that covers over 90 percent of the state of Mississippi, and upon which cities, counties and state agencies depend for reliable wireless services.

RCA believes in rural America and its members value the people who live there. In Cellular South's 20 years of serving rural areas, we have come to understand what rural consumers want in their wireless service. It is very simple. They want the same things that people in Washington, D.C., Boston, Massachusetts, Los Angeles California and New York City want: quality coverage, modern technology, the latest devices and the ability to access compatible networks wherever they go.

While Congress works to modernize and otherwise reform the Universal Service Fund, it is critical to keep in mind that device exclusivity and data roaming issues must also be resolved if Congress still believes that rural Americans should have services that are reasonably comparable to those in urban areas.

Today, consumers demand broadband and mobility. Policymakers and those of us in the telecom industry have seen this coming for years, and everyone in this room has acknowledged the need for more broadband services. Yet, since 2001, the FCC has not released an order that would promote rural consumers access to these services.

Between 2000 and 2008, the FCC subsidized wire line voice service to the tune of approximately $26.3 billion while funding wireless voice services at approximately $4.6 billion. Broadband services received zero.

The universal service mechanism cannot continue to support fixed voice service, 19th century technology, at a rate of over $3 billion per year. As the world evolves toward broadband and mobile services, so too should the funds to distribution mechanisms.

Accordingly, RCA supports Chairman Boucher's proposal to include broadband as a supported service within the Universal Service Fund. However, it is absolutely critical that the distribution of universal service support is competitively neutral. In other words, the distribution mechanism must not favor or disfavor any technology or class of carrier. More than that, it should not protect any technology or class of carrier. Support should be portable, and new entrants and incumbents alike should be allowed to compete for customers. This puts consumers in charge by increasing choices and consumer choice increases service quality and lowers prices.

RCA is not convinced that reverse options for just one class of carrier are consistent with the principles of competitive neutrality. To be clear, RCA fully accepts the need to sustain the fund. However, we do not believe that reverse auctions are the solution, because they sacrifice the goals of universal service in the name of sustainability.

There are a number of structural issues that must be overcome before competitive bidding can be a realistic option. First and foremost, we have not seen an auction mechanism proposed that eliminates the opportunity for USF opponents to game the system by submitting artificially low bids in order to drive out competition.

Assuming you could avoid that problem, the proposed auction system would limit support in an area to a maximum of two providers for a period of up to 10 years. This ensures that no new providers will enter that area and it forces policymakers into the position of regulating an artificial marketplace, a monopoly or duopoly.

Furthermore, if the goal of reverse auctions is to lessen support in a given area and thereby reduce the size of the fund, there is no certainty that it will happen under reverse auctions.

Finally, as proposed, reverse auctions exempt the largest category of recipients from the high cost portion of the Universal Service Fund.

In conclusion, RCA believes that support in high cost areas should be fixed at the amount needed to deliver reasonably comparable, high quality services to consumers, with support only being awarded when a carrier gets a customer and with that support being taken away when the carrier loses a customer. We believe that no one should be insulated from competition, and we believe that new entrants should be allowed into markets to maximize competition and improve choices and service for consumers.

Thank you again for the opportunity to participate today, and I look forward to your questions.

Mr. BOUCHER. Thank you very much, Mr. Graham.

[The prepared statement of Mr. Graham follows:]

Testimony of Eric Graham

Vice President, Government Relations,
Cellular South, Inc.

before the

U.S. House Subcommittee on
Communications, Technology and the Internet

November 17, 2009

INTRODUCTION

Mr. Chairman, thank you for the opportunity to be here today to present testimony to the Subcommittee as a member company of the Rural Cellular Association ("RCA"), and on behalf of Cellular South, Inc. ("Cellular South").

RCA's nearly 100 carrier members provide commercial wireless services primarily in rural areas that cover roughly 83% of the nation's geography. Many RCA members are eligible to draw from the federal universal service program and are using support to build high-quality networks in some of the most remote areas of the country.

Cellular South is the nation's second largest privately-held wireless carrier by number of subscribers, serving all of Mississippi as well as portions of Florida, Alabama, Tennessee and Arkansas. We are typical of RCA's membership in that the area we serve is overwhelmingly

rural and we face enormous challenges in competing with the "Big Four" carriers who currently dominate the commercial mobile wireless industry in this country.

Today, citizens in thousands of places across the country such as Spray, Oregon; Groseclose and Floyd, Virginia; Caldwell, West Virginia; Garnavillo and Whittemore, Iowa; Tillery, North Carolina; Trempealeau, Wisconsin; Bunker Hill, Illinois; Bloomington Springs, Tennessee; Brush, Colorado; Highlandville, Missouri; Eustis, Nebraska; Grand Isle, Maine; and Ellisville, Mississippi, are receiving high-quality wireless service as a result of the universal service program. In Mississippi, we have used support to reach out to countless small towns and rural areas, providing high-quality service in places where other carriers have not chosen to.

Universal service reform is one of three critical reforms that Congress and the FCC must enact to ensure that rural consumers have access to high-quality wireless services. In addition to universal service reform, Congress and the FCC should make clear that a person has a right to expect that a modern telecommunications device will work on any compatible network throughout the United States. It is absolutely unacceptable for a citizen of the Commonwealth of Virginia to take a Blackberry to New York, only to find that the device cannot access the carrier's fast 3G network, but is forced to "step down" to a slower one. It is even worse when a citizen travels to a distant city, only to find that email and Internet access have been completely disabled, even though the phone shows "four bars" of available signal on a compatible network.

The other consumer issue is handset exclusivity. Rural citizens must be able to buy the latest devices to enable access to the rapidly expanding universe of applications that are

increasingly becoming a staple of economic development in urban areas. Congress and FCC must do away with handset exclusivity, which large carriers are using to limit consumer choice and literally drive smaller competitors out of the marketplace.

There are simple solutions to the latter two problems: require all carriers to enter into automatic data roaming agreements, just as automatic roaming for voice and SMS text services is required today, and ban handset exclusivity arrangements. The FCC has the power to fix these two problems and RCA urges Congress to help the agency to do it.

With respect to universal service, I must be clear about the importance of high-cost support to rural wireless carriers. The key to high-quality coverage is cell density. Without support, cell sites will be constructed only in places that afford a return on investment. In cities, there are enough customers to justify dense cell site construction that provides high-quality coverage. In many rural areas, dead zones remain because places that justify dense construction are spread out – leaving small towns and rural areas with poor service.

Accordingly, one of the most important things I want you to understand is that for many rural areas, ***universal service support is the difference between spotty coverage and high-quality service throughout a rural area.***

For anyone who would say that the work of building wireless facilities in rural areas is largely done, RCA members across the country can demonstrate to you the difference between a rural area that receives little or no support, and one that receives universal service support. What

many of our members have accomplished in a relatively short period of time is truly remarkable. RCA members who are using support will be pleased to host you in your districts to demonstrate how their networks have developed and the benefits that they are delivering to your constituents.

RCA supports the Chairman's initiative, as shown in the discussion draft, to provide rural citizens with access to high-quality mobile wireless broadband services, and to enable the delivery of thousands of data applications that drive economic development. Mobile wireless networks play an increasingly important role in the health and safety of rural citizens. For example, police and first responders depend on secure mobile wireless networks in disaster recovery, and law enforcement operations. In sum, rural citizens, who pay into the federal universal service fund, deserve access to high-quality mobile voice and broadband services that Congress intended for them to have.

1. The Contribution Methodology Must Be Reformed To Reflect The Accelerating Shift From Voice To Broadband Services.

Today the FCC collects support contributions from carriers through a mechanism based entirely on a percentage of revenues. Ten years ago, when voice minutes made up the vast majority of carrier revenues, this mechanism was fine. Today it is apparent that the days of per-minute voice dominating carrier revenues are behind us.

Wireline voice minutes have been declining with the introduction of wireless and cable competition, as well as from consumers choosing Voice Over Internet Protocol ("VoIP") service on their broadband connections. Now, wireless consumers are increasingly using VoIP services

that will reduce carrier revenues for voice services dramatically in the coming years.[1] As consumer preferences shift toward data functions, including VoIP, text messaging, email, and other means of communicating, the bulk of carrier revenues are going to come from IP services, with voice bits traversing networks in the same manner as any other data bits. Less efficient circuit switched voice revenues will continue to fall for many years, and will eventually be phased out. Following the transition, consumers may spend more overall than they do today on telecommunications services, but their dollars will be spent on data platforms, applications, and vertical services, with voice being one of many data applications.

The networks that deliver all of these new services, along with IP voice, are no less challenging to construct, operate and maintain in rural America. Thus, the contribution mechanism must adapt, so that a sufficient level of support can be generated to advance the core universal service goal that rural consumers must have access to affordable and high-quality advanced services that are reasonably comparable to those available in urban areas.

The FCC's assessment of interstate telecommunications services draws from a shrinking pool of consumer revenues. That has resulted in a contribution factor that has now risen to over 14% of a customer's interstate bill. Some carriers use the FCC's "safe harbor" which pegs interstate revenues at 37.1% of a consumer's bill. The safe harbor results in wireless consumers contributing about 5.27% of their total phone bill. Other carriers are measuring traffic and discovering that interstate usage is much lower than the safe harbor, which dramatically reduces contributions. For example, if a carrier measures only 20% of its traffic as interstate, the contribution factor applies to that amount, while the remaining 80% of the bill is deemed

[1] See, e.g., the cover story of *Forbes* Magazine, November 16, 2009, "The $10 Phone Bill."

intrastate and exempt from federal universal service support assessment. This results in a lower universal service charge for the consumer, and correspondingly, less support available in the system.

There are numerous reasons why the contribution factor has recently increased, including carriers' use of traffic studies to more accurately reflect interstate traffic. Two others are worth noting. In the short run, the drop in wireless expenditures over the past year is a byproduct of our difficult economy. Consumers are cutting the cord and shifting to lower priced wireless plans. The second, as noted above, the shift to VoIP and other platforms, will be dramatic in the coming years, as new broadband platforms and increasing throughput speeds provide consumers with less expensive options for voice communications.

The near-term solution is to do exactly what the discussion draft proposes – give the FCC broad flexibility to reform the contribution mechanism. Whether support is assessed on numbers or their equivalent, on revenues, or a combination thereof, as long as everyone who uses our nation's telecommunications network contributes fairly, the result will be satisfactory. What cannot be allowed to happen is for the FCC to be limited to assessing interstate revenues that are melting away, as the distinction between voice and data traffic vanishes in an all IP world. The current course is unsustainable in the long term.

We therefore commend the Chairman for providing the FCC with much needed flexibility, and believe this legislation will remove all uncertainty about the FCC's authority to

craft a fair and forward-looking contribution methodology that ensures that the fund is sustainable long into the future.

2. The FCC Must Be Given Clear Direction To Transition The High-Cost Fund Distribution Methodology To Support Broadband and Mobile Wireless Communications Networks.

It has been said that there are only two killer applications in the telecommunications world: broadband and mobility. I agree. It is now widely accepted that access to these two killer apps must be the central focus of our government's effort to see that modern, high-quality telecommunications infrastructure is available to all of our citizens, not just those living in urban areas.

These statements are anything but new. Yet, since 2001, the FCC has not released an order advancing rural consumer access to broadband and mobility. Between 2000 and 2008, the FCC has subsidized wireline voice service in the amount of approximately $26.3 billion, while funding mobile wireless voice services at approximately $4.6 billion, and broadband at zero.[2] Although universal service support is often invested in dual-purpose networks that can deliver broadband (such as wireless towers or buried fiber), explicit support for broadband is long overdue. Society is transitioning to broadband and mobile voice platforms at an accelerating pace and will soon leave the current mechanism behind. The universal service mechanism cannot continue to support fixed voice service at a rate of over $3 billion per year, indefinitely.

[2] Source: 2008 Federal-State Joint Board Monitoring Report, Table 3.2. http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-287688A5.pdf

We therefore commend the Chairman for explicitly designating broadband as a supported service and requiring all carriers to deliver broadband within a reasonable period of time, or forfeit access to federal universal service funding. We have had discussions concerning whether the FCC currently has sufficient legal authority to fund broadband. Although we believe that current law permits it, this legislation will prevent any substantial delays that could result from court challenges.

We also believe that the draft should specifically task the FCC with determining the correct amount of support that ***high-cost areas*** need in order for consumers to have access to reasonably comparable and affordable broadband and mobile services. As drafted, the bill would allow certain ***high-cost carriers*** to receive embedded high-cost support indefinitely, which in the long run insulates specific market participants from market forces, and is therefore not competitively neutral. Support is for consumers, not for carriers, and this shortcoming in the current mechanism, supporting high-cost carriers, should not be perpetuated.

RCA favors a broadband fund that would confer upon the agency the discretion to adjust these throughput requirements periodically to account for technological developments. We think a ten year period would be sufficient to fully transition the mechanism away from supporting fixed voice and toward support for fixed and mobile broadband.

We arrive at this recommendation by looking at the past six years, during which residential access lines have dropped by over 30%.[3] The trend toward mobile voice is accelerating. By 2020, roughly ten years after this bill is passed, the percentage of Americans

[3] Source: Bernstein estimates and analysis.

using a wire for their primary access to voice service will be much lower than it is today, yet many consumers will likely continue to have a wire in their homes, to deliver IP services including Internet access and entertainment. These revenue streams will be substantial, and wireline carriers will also continue to provide backhaul for the wireless voice and broadband services that consumers need. Accordingly, subsidies must flow toward enabling wireline carriers to deliver IP services, and away from narrowband voice.

RCA believes that Congress got it right when it declared in 1996 that rural consumers should have access to "advanced telecommunications and information services."[4] As the world evolves toward broadband and mobile services, so too should the fund's distribution mechanism. For our part, Cellular South is fully prepared to make the jump to a competitively neutral system that provides efficient levels of support to rural areas, accessible by all carriers willing to take the risk of investing in broadband and mobile platforms. And make no mistake – there must be business risk in order for carriers to have appropriate incentives to deliver high-quality service. A carrier that invests and gets a customer should get support and those that lose customers should lose support. The discussion draft moves us further in the proper direction.

3. All Contribution and Distribution Mechanisms Must Be Competitively Neutral.

It is absolutely critical that all universal service mechanisms be competitively neutral, that is, they must not favor or disfavor any technology or class of carrier. This principle allows entrepreneurs and incumbents alike to compete for both consumer revenues and universal service

[4] 47 U.S.C. §254(b)(3).

support. It puts consumers more in charge by increasing choices. Consumer choice increases service quality and lowers prices.

The 1996 Act intended to break down barriers to entry throughout the country, not just in urban areas, and opening universal service to competitors was a critical tool. Allowing competitors to access universal service support in high-cost areas in a competitively neutral fashion has driven enormous consumer benefits. Accordingly, we commend the Chairman for codifying the FCC's "core principle" set forth in its rules, that all universal service mechanisms must be competitively neutral.

4. The FCC Should Be Afforded Flexibility To Revamp Distribution Mechanisms, And A Given A Deadline For Action.

RCA is committed to supporting a transition of the federal universal service mechanism to broadband services, provided that consumers are empowered to choose the services that best suit their needs, and carriers are required to compete for customers. Today, the biggest carriers, AT&T, Verizon and Qwest, receive support based on a forward-looking cost model, which is over a decade old, an antiquity. Computing power and mapping software are light years ahead of where they were in 1997. We know of private companies who have used these new tools to develop much more accurate models of what it costs to build an efficient broadband or mobile wireless network.

While we know models for costs and support can be developed, we do not know whether using models is the best policy choice. We also note that the discussion draft would permit some

carriers to elect to receive support through the use of a forward-looking model. Since the discussion draft contemplates the use of models for some carriers, we support giving the FCC flexibility to consider the use of models as a means of distributing support on a competitively neutral basis to all carriers.

RCA does not support the indefinite use of the embedded cost methodology, and accordingly we believe the discussion draft should specifically require the FCC to examine alternatives that provide carriers with incentives to operate efficiently. The current embedded cost system provides an incentive to spend more in order to increase support levels, and it is not transparent with respect to whether expenditures are necessary.

In addition, over 400 wireline companies remain on what is known as an "average schedule" which means they receive support irrespective whether they make any investments. These mechanisms are contrary to the current administration's principle that scarce resources must be deployed efficiently. The FCC must develop policies that increase investment in new, efficient technologies that will reduce the need for subsidies in the long run.

Accordingly, RCA supports a provision requiring the FCC to revamp the distribution methodology within a time certain, that it be done on a competitively neutral basis, and that efficient mechanisms shall be favored over those that encourage inefficiencies.

5. Auctions For One Class Of Carrier Are Inconsistent With The Principle Of Competitive Neutrality And Would Artificially Limit Competition.

A. Competitive Neutrality.

The discussion draft would require the FCC to distribute support to wireless carriers through the use of an auction methodology. To be clear, contrary to the principle of competitive neutrality, only wireless carriers would be required to engage in the competitive bidding process. The discussion draft allows for the selection of up to two competitors and a term of up to ten years before an area is rebid. RCA opposes auctions for universal service support because they will greatly disserve rural citizens.

Requiring auctions for one class of carrier and artificially limiting competition appears to be inconsistent with the discussion draft's mandate that support mechanisms be competitively neutral. Auctions for one class of carrier, while another class remains on the embedded cost mechanism, appears to fail a reasonable competitive neutrality analysis. This is especially so when today the universal service funding provided on embedded costs to wireline carriers is overwhelmingly funded by wireless consumers, most of whom would prefer to see funding increased for the service they rely on and use most.

Accordingly, we question the policy of substantially increasing support to AT&T, Verizon and Qwest, continuing an embedded cost methodology for other wireline carriers, while funding to rural wireless carriers would be permanently capped, even if a higher level of support is needed to accelerate investment in much needed wireless broadband infrastructure. To be clear, RCA fully accepts the need to sustain the fund. We believe that funding in an area should

be fixed at the amount needed to deliver reasonably comparable high-quality services to consumers, with support only being awarded for getting a customer.

Under the current rules, when a wireless carrier takes a customer away from another wireless carrier, the winning carrier also captures the support for that customer, and the losing carrier relinquishes the support, but the fund does not grow. This is as it should be. But under the current rules, when a wireless carrier captures a customer from a ***wireline*** carrier, the wireline carrier does not lose any support, and the fund grows. In order to promote investment, increase service quality, and consumer choice, while sustaining the fund, we recommend the following:

1. Use the broadband map being developed through the stimulus bill to identify areas where investment is needed;

2. Identify the efficient cost of providing broadband and mobile wireless services in each area shown in the broadband map, using a forward-looking methodology, such as the use of cost models;

3. Once an efficient amount of support is fixed for each area, provide support to the carrier that wins the customer, with eligible ETCs being required to meet the obligations set forth in the discussion draft, including offering service throughout its service area, complying with carrier-of-last-resort obligations, and all service quality rules. Carriers that lose customers must also lose support; and

4. Encourage newcomers to enter if they can meet the required obligations and if they have a more efficient network or desirable service that consumers would choose. This would allow the market, rather than regulators, to determine the success or failure of new technological advancements and business models.

B. Specific Issues Inherent in Reverse Auctions.

There are a number of auction issues that must be overcome before competitive bidding can be a realistic option for policymakers. Chief among them is the likelihood that an auction will recreate the very problem the 1996 Act intended to solve – the problem of dominant carriers in rural areas erecting insurmountable barriers to entry by virtue of their having all the customers and all the support. In areas where a single winner emerges, the Commission will have to regulate rates, service quality, interconnection, and other terms in order to effectively create an "artificial marketplace." Even where two winners are selected, an artificial duopoly will present most of these same challenges. By dictating a specific number of providers in an area, regulators merely succeed in precluding new entry and reducing, if not eliminating, the benefits of competition for rural citizens.

Providing auction winners with an exclusive term is problematic because installed telephone plant is comprised of long-term assets that are generally fixed into the ground (e.g., concrete, tower, equipment building) and that have lengthy depreciation schedules. Dismantling a network at the end of a term is not practicable. If carriers are expected to bid at levels which would allow recovery of the cost of plant within the exclusive term, then the problem of "stranded investment" issue would be far worse than the existing wireline problem, as much wireline plant in service today is decades old and fully depreciated.

RCA is also wary of deep pockets wielded by the largest carriers, who have shown little desire to provide high-quality wireless service in many RCA member served areas. Some of

these carriers are walking away from high-cost support and actively seek to minimize their contributions to the fund. In an auction, these carriers will have an enormous incentive to drive support levels down to minimal levels, so that carriers who want to serve rural America are either driven out, or forced to bid lower than the appropriate level needed to provide high-quality service, while large carriers reduce their contributions.

We envision the largest carriers winning reverse auctions for next to nothing, and then providing service at absolute bare-minimum levels with the smallest area of coverage possible to satisfy regulators, but to the detriment of consumers. The lack of support to competitors will also reestablish the barrier to entry that the 1996 Act tore down. RCA members, who have invested in their networks over the years, would not receive the support needed to maintain and upgrade networks in remote areas, causing cell sites to be decommissioned, and harming consumers who would lose service coverage.

It is easy to see these harmful effects today, as a result of the "interim" CETC cap, which has significantly reduced universal service funding to many rural wireless carriers who are still in the process of constructing networks. For example, Carolina West Wireless ("Carolina West"), an RCA member operating in North Carolina, has canceled plans to build eight new cell sites in its licensed service area as a result of the significant USF High Cost support reductions. Due to the interim CETC cap, Carolina West has seen a 67% reduction in universal service support. As a result, twenty communities in western North Carolina served by Carolina West will continue to have limited or no cellular service. The harm that the CETC "interim" cap is causing to rural America is real and is getting worse as long as it remains in place.

In sum, targeting an efficient level of support to an area, and requiring all eligible carriers to offer service throughout the area, is a better means of ensuring that citizens have a fair opportunity to select newcomers capable of offering better or less expensive services. Support to a high-cost area should be limited to the amount of support needed to efficiently provide consumers with high-quality broadband and mobile wireless services. Finally, Congress should set these principles before the agency and require a proceeding to be concluded within a reasonable period of time.

6. Universal Service Provisions In The 1996 Act Have Delivered Lower Prices And Tremendous Benefits To Both Urban And Rural Citizens.

Often overlooked are the substantial benefits that the FCC's early work on implementing the 1996 Act has delivered to the American public. For example, in 1995, the cost of a wireless minute of service was approximately 43 cents, largely because of the high cost of transporting and terminating calls on other networks. Following the 1996 Act, the FCC adopted an explicit high-cost fund and also transferred significant levels of access subsidies out of carrier rates and into the Interstate Access Support (IAS) and Interstate Common Line Support (ICLS) funds, which were made available to all carriers on a competitively neutral basis.

As a result, access charges were reduced, enabling corresponding reductions in the price of all telecommunications services. By 2006, the cost of a wireless minute was only 6.7 cents, which enabled carriers to offer more minutes at lower prices and wider local calling areas. As shown in the chart below, even taking into account the increasing contribution factor, the amount

that consumers are paying in per minute is dramatically lower than it was when the 1996 Act was enacted, in large measure due to universal service reform. I believe the benefits of increased competition and lower retail pricing have more than offset universal service contributions needed to fund the high-cost mechanism.

Per-Minute Cost of Wireless Service
(Including USF Contributions)

(1995-2007)

Sources: FCC, *Trends in Telephone Service*, Table 19.17 (Feb. 2007); *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993 – Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, WT Docket No. 06-17, *Twelfth Report*, FCC 08-28 (rel. Feb. 4, 2008), at para. 201 (Table 14)

YEAR	(A) AVERAGE REVENUE PER VOICE MINUTE ($) 1/	(B) CONTRIBUTION FACTOR (%) 2/	(C) PER MINUTE COST OF CONTRIBUTION FACTOR ($) 3/	TOTAL COST PER MINUTE ($) (A) + (C)
1995	0.4300			
1996	0.3800			
1997	0.3700			
1998	0.2900	3.1625	0.0092	0.2992
1999	0.2200	3.0143	0.0066	0.2266
2000	0.1800	5.6980	0.0103	0.1903
2001	0.1200	6.8445	0.0082	0.1282
2002	0.1100	7.1625	0.0079	0.1179
2003	0.1000	8.7701	0.0088	0.1088
2004	0.0800	8.8000	0.0079	0.0879
2005	0.0600	10.5500	0.0074	0.0674
2006	0.0600	10.1750	0.0071	0.0671
2007	NA	10.9250		

1/ Data covers the last six months of each year.
2/ The listed number for years 1998-2007 is an average of the four quarterly contribution factors.
3/ Calculated by multiplying the average revenue per minute (A) by the contribution factor (B)

Our point here is simple. In the midst of valid concerns about the size of the contribution factor, if you add universal service contributions to the cost of a minute of service, all citizens, urban and rural, are enjoying significantly lower prices than they would have if the Commission had allowed access charges to remain artificially high.

CONCLUSION

Reforming universal service requires well-crafted legislation and a determined agency, willing to faithfully implement Congressional directives. RCA welcomes the discussion draft as it represents a substantial and persistent effort by the Chairman to move forward. RCA and our members hope for the opportunity to work with the Chairman and Subcommittee members to develop final legislation that continues to drive infrastructure investment in rural America, promote entry by newcomers who offer new technologies and efficient delivery mechanisms, and focuses universal service support on consumers.

Thank you again for the opportunity to participate in this proceeding.

Mr. BOUCHER. We have several provisions in the draft that address the Rural Health Care Fund, and Dr. Rheuban and her comments will address those provision. Dr. Rheuban.

STATEMENT OF KAREN RHEUBAN, M.D.

Dr. RHEUBAN. Good morning, and thank you, Chairman Boucher, Ranking Member Stearns and other distinguished subcommittee members. My name is Dr. Karen Rheuban, and I am a practicing pediatric cardiologist and Medical Director of the Office of Telemedicine and the University of Virginia. I am also honored to serve as president of the American Telemedicine Association. Thank you for this opportunity to testify and support the draft universal service reform bill.

The health reform debate has galvanized our Nation. The powerful tools of telemedicine and health information technologies are key to a transition from care delivered episodically in a balkanized model to an integrated systems approach. Sound policies must facilitate ubiquitous and affordable access to the broadband infrastructure to support access to health care using advanced technologies, especially for our rural Americans.

The need for access to care is greater than ever before. Our Nation faces a critical shortage of physicians, with a projected deficit of 200,000 doctors by 2020. The aging of our population has created increasing demands for health care services. Access to speciality care is inadequate for many Americans.

Telemedicine programs can be found in every State offering clinical services that span the entire spectrum of health care. At UVA, we have been privileged to work with Chairman Boucher to deploy an extensive telemedicine network connecting more than 30 federally-qualified health centers, clinics, hospitals, school and correctional facilities in his district, in addition to other regions of the Commonwealth.

Medical specialty societies have endorsed tele-health as an effective tool for the delivery of care. As an example, during an acute stroke, life-saving, clot-busting therapies administered by stroke neurologists through telemedicine have been proven to reduce the morbidity, mortality, burden and cost of stroke.

Telemedicine programs improve access to prenatal care. The University of Arkansas now reports a 26 percent reduction in neonatal mortality attributable to their high risk obstetrics telemedicine program.

Telemedicine plays an important role in chronic disease management. The VA's care coordination and home tele-health program has resulted in a 19 percent reduction in readmission to the hospital and 25 percent reduction in hospital days.

Each tele-health application relies on broadband communication services that meet the need of the specific clinical service required. Surgical mentoring requires high definition and higher bandwidth, as do the transfer of large medical imagine files and video teleconferencing. Remote monitoring and home tele-health require less bandwidth.

Regardless of the clinical application, affordable, reliable, secure quality of service is imperative. The rural health care program has been critical to tele-health networks nationwide. However, statu-

tory and regulatory barriers have severely undermined the programs' effectiveness.

As of June 30, 2009, USAC reports a total disbursement over 12 years, total, of only $249 million, which is only 5 percent of the originally authorized amount.

For the rural health care program to succeed as intended, a number of areas need to be corrected that have been addressed in your draft bill. Statutory barriers limit the eligible consult origination sites, excluding such important entities as nursing homes, EMS providers, and even for-profit rural hospitals. For purposes of emergency preparedness or for access to emergency care there is no question that rural for-profit hospitals serve the public interest.

The program is bound by definitions of "rural" that fail to take into account our serious maldistribution of specialty health care providers. An expansion of the "rural" definition would align universal service support with these specialty workforce shortages.

Other administrative barriers, including allowing only 25 percent support for Internet services, are counter-intuitive in an era where most tele-health programs deploy IT-based technologies. All communications providers should be eligible to participate in the program.

In 2007, the FCC launched the rural health care pilot program, recognizing 69 entities, including UVA, as eligible to receive more than $400 million in funds to expand the communications infrastructure for health care. As of June 30th, beginning the third year of the program, less than $1 million had been disbursed.

This program, albeit well intended, is equally fraught with significant barriers. Eligible providers are restricted, no funds are available for project management, and yet we have applicants who are asked to provide letters of agency from each remote site, secure 15 percent in cash as matching funds, provide detailed quarterly reporting, even in the absence of funding, and sign 5-year contracts for service for purposes of sustainability. These obstacles have hindered the program.

Tele-health services both drive demand for broadband adoption and increase access to acute care and chronic disease management through networks that include hospitals, clinics, physician offices, nursing homes, ambulances, the workplace and the home. Broadband provided over wire line, wireless, cable, satellite, power lines and other emerging technologies provide the communications infrastructure that supports the transformation of health care delivery.

As you have addressed in this bill, our universal service programs must be modernized with a closer alignment with our health care needs so that one major value proposition of our investment in universal service can be achieved—that is an improvement in the health of all Americans.

Thank you.

Mr. BOUCHER. Thank you very much, Dr. Rheuban.

[The prepared statement of Dr. Rheuban follows:]

Testimony of Karen S. Rheuban M.D.
Professor of Pediatrics
Medical Director, Office of Telemedicine
University of Virginia Health System
President, American Telemedicine Association
Before the
Subcommittee on Communications, Technology and the Internet
November 17, 2009

Chairman Boucher, Ranking Member Stearns, and other distinguished members of the Subcommittee on Communications, Technology and the Internet, my name is Dr. Karen Rheuban. I am a pediatric cardiologist, Senior Associate Dean for Continuing Medical Education and Medical Director of the Office of Telemedicine at the University of Virginia Health System. I am also honored to serve as President of the American Telemedicine Association and as board chair of the Virginia Telehealth Network. I am also a board member of the Center for Telehealth and E-Health Law. As a physician serving many rural patients, I have come to appreciate how broadband and information technology can greatly enhance the delivery of quality healthcare, and substantially reduce the cost of providing healthcare for tens of millions of Americans. Thank you for this opportunity to provide testimony regarding the Universal Service Reform Act of 2009 and related barriers to the adoption of telehealth.

The health reform debate has galvanized our nation. The powerful tools of health information technologies are key to the transition from healthcare delivered episodically in a balkanized model to an integrated systems approach focused on disease prevention, enhanced wellness, chronic disease management, quality care and patient safety. Sound policies that facilitate the integration of advanced broadband and information technologies with healthcare

delivery must be a priority in the digital era. **Such policies must include and facilitate ubiquitous and affordable access to the requisite broadband infrastructure that supports the delivery of healthcare using telemedicine, teleradiology, home telehealth and remote monitoring tools, health information exchange and distance learning for patients, students and health professionals.**

USING TELEMEDICINE TO REFORM THE DELIVERY OF HEALTHCARE

The need for access to care is greater than ever before. Our nation faces a critical shortage of physicians, with a projected deficit of 200,000 doctors by 2020.[1,2] The aging of our population has created increased demand for healthcare services that address both acute and chronic disease. Access to specialty care remains inadequate for many Americans, attributable to a host of factors including geographic, economic and societally imposed barriers. Although rural communities face the same basic challenges in access, quality and cost as their urban counterparts, they do so at far greater rates. "Core health care services" as defined by the Institute of Medicine as primary care, emergency medical services, long term care, mental health and substance abuse services, oral health and other services are considerably less accessible in rural communities.[3]

The incorporation of telehealth technologies into integrated systems of care can address the challenges of access, specialty shortages, and changing patient needs in all

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[1] Cooper, RA, Weighing the evidence for expanding physician supply, Ann Intern Med 2004: 141:705-714.
[2] Blumenthal D. New steam from an old cauldron: the physician supply debate, N Engl J Med: 2004:350:1780-1787
[3] Quality Through Collaboration, The Future of Rural Health, Institute of Medicine, National Academies Press, 2004

settings. Telemedicine does not create a new field of healthcare, but rather allows appropriately credentialed clinicians to provide care at a distance using technology and broadband communications services. Live interactive videoconferencing linking patients and specialists, asynchronous transfer of medical data (store and forward) and home telehealth and remote monitoring all improve access, lower costs, improve patient triage, reduce travel, and improve outcomes.

Telemedicine programs can be found in every state. Clinical services delivered via telehealth technologies span the entire spectrum of healthcare, and across the continuum from prenatal care to geriatric care, with applicability to more than 50 clinical specialties and subspecialties.[4] The University of Virginia's Telemedicine program that I oversee provides services in more than 35 subspecialties to patients located at more than 60 sites in the Commonwealth of Virginia. In particular, we have been privileged to work with Chairman Boucher and his staff to deploy a robust and extensive telemedicine network in southwest Virginia.

Medical specialty societies have endorsed telehealth as an effective tool for the delivery of care, and many have published practice guidelines and standards, based on a careful analysis of the evidence. As an example, during an acute stroke, when "time is brain", life saving

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[4] Hersh WR, Hickam DH, Severance SM, Dana TL, Krages KP, Helfand M. (2006). Telemedicine for the Medicare Population: Update. Evidence Report/Technology Assessment No. 131. (Prepared by the Oregon Evidence-based Practice Center under Contract No. 290-02-0024.) AHRQ Publication No. 06-E007. Rockville, MD, Agency for Healthcare Research and Quality. February 2006.

thrombolytic (clot-busting) therapies administered by stroke neurologists through telemedicine networks reduce the morbidity, mortality and burden and cost of ischemic stroke.[5]

Telemedicine programs improve access to prenatal care supported by maternal fetal medicine specialists. The "Arkansas Angels" telemedicine program, designed to improve access to high risk obstetric services has reduced premature deliveries and neonatal mortality in Arkansas by 26%.[6, 7] Virginia Medicaid reports expenditures of more than $50 million dollars annually on neonatal intensive care. Our own pilot high risk obstetrics program in Virginia has demonstrated reduced newborn ICU admissions through appropriate management of high risk pregnancies.

Telemedicine plays an important role in chronic disease management. Jencks et al published an analysis of the readmission rates in the Medicare population. In 2004, 19.6% of nearly 12 million hospitalized Medicare beneficiaries were readmitted with the same diagnosis within 30 days, 34% in 90 days and 56% in one year.[8] Of those, it was estimated that only 10% were planned re-hospitalizations. The Medicare Payment Advisory Commission reported that in

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[5] Schwamm LH, Holloway RG, Amarenco P, Audebert HJ, Bakas T, Chumbler NR, Handschu R, Jauch EC, Knight WA 4th, Levine SR, Mayberg M, Meyer BC, Meyers PM, Skalabrin E, Wechsler LR; American Heart Association Stroke Council; Interdisciplinary Council on Peripheral Vascular Disease. A review of the evidence for the use of telemedicine within stroke systems of care: a scientific statement from the American Heart Association/American Stroke Association.Stroke. 2009 Jul;40(7):2616-34.

[6] Hall-Barrows, J. Evaluation of ANGELS - Report of Findings from First Thirty-Three Months April 2003 to December 2005 Arkansas Department of Human Services March 16, 2009

[7] Lowery C, Bronstein J, McGhee J, Ott R, Reece EA, Mays GP. ANGELS and University of Arkansas for Medical Sciences paradigm for distant obstetrical care delivery, Am J Obstet Gynecol. 2007 Jun;196(6):534.e1-9.

[8] Jencks SF, Williams MV, Coleman EA.; Rehospitalizations among Patients in the Medicare Fee-for-Service Program; N Engl J Med. 2009 Apr 2;360(14):1418-28.

2004, Medicare expended $17.4 billion dollars on unplanned hospital admissions. Home telehealth and remote monitoring tools have been shown to reduce hospitalizations, readmission for the same diagnosis, and improve outcomes. In Congressional testimony, the Department of Veterans Affairs reported that its Care Coordination and Home Telehealth program resulted in a 19% reduction in readmission and a 25% decrease in hospital days.[9, 10] To provide a real-life demonstration of this, next month, the University of Virginia and Habitat for Humanity in partnership with Comcast and the Intel Digital Health Group will be breaking ground on Habitat's first "Health House," with remote monitoring embedded into affordable housing in Charlottesville.

Each telehealth application relies on scaleable broadband communications services that meet the need of the specific clinical service required. Surgical mentoring requires high definition and higher bandwidth as does the transfer of large medical image files and video-teleconferencing. Remote monitoring and home telehealth require lesser bandwidth. Either wired or wireless, broadband facilitated connectivity is far superior than POTS (plain old telephone service) when connecting patient and provider. Regardless of the clinical application, reliable, secure quality of service is imperative.

IMPROVING UNIVERSAL SERVICE PROGRAMS

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[9] Darkins, A., Congressional Testimony, http://veterans.senate.gov/hearings.cfm?action=release.display&release_id=9fb33d22-3b6c-483d-b43c-2637e6e4c6f3

[10] Darkins A, Ryan P, Kobb R, Foster L, Edmonson E, Wakefield B, Lancaster AE. (2008). Care Coordination/Home Telehealth: The Stystematic Implementation of Health Informatics, Home Telehealth, and Disease Management to Support the Care of Veteran Patients with Chronic Conditions. Telemedicine and e-Health, 14(10): 1118-1126.

The Rural Healthcare Program, established in the Telecommunications Act of 1996, administered by the Universal Services Administrative Company (USAC), has been critical to the deployment and sustainability of telehealth networks nationwide. Prior to the passage of the Act, in 1995 we priced a 1.54 Mbps connection to a rural hospital in southwest Virginia at an unaffordable $5800 per month. In 2009, with enhanced competition and Universal Service subsidies, that connection to a small rural hospital cost $170 per month over Network Virginia, managed by Verizon Business Solutions and Sprint.

Although initially authorized to support funding requests up to $400 million per year, statutory and regulatory barriers have severely undermined the effectiveness of the Rural Healthcare Program. Many on your Committee strongly supported the establishment of this program. You therefore may be taken aback to learn that as of the last fiscal year, ending June 30, 2009, USAC reports a **total disbursement over 12 years of only $249 million, about 5% of the originally authorized amount. Of those funds, over half supported communications services in Alaska.** In the past year, USAC reports funding commitments of $61 million, still far short of the $400 million authorized for the program.

In its first 12 years, the Rural Healthcare Program has clearly failed to meet the worthy goals set by Congress. For the program to succeed as intended, a number of areas need to be corrected:

1. Eligible Sites - Statutory barriers limit eligible consult origination sites, excluding such important entities as nursing homes, EMS providers, and for-profit rural hospitals.

2. Definition of Rural - The program is bound by definitions of rural that fail to take into account our serious national mal-distribution of specialty healthcare providers. In its December 2004 Order, the Federal Communications Commission (FCC) changed the rural definition[11], and approved funding of telecommunications support for for-profit rural hospitals with an emergency department. The FCC recognized that for emergency preparedness, and bound by federal EMTALA[12] (the Emergency Medical Treatment and Active Labor Act), rural for-profit hospitals serve the public interest. Unfortunately, however, the 2004 FCC Order excluded from the Rural Healthcare Program many otherwise eligible telemedicine consult origination sites with limited access to specialty medical services. Specialists tend to locate in regions with denser populations and we believe expansion of the rural definition will further align universal service support with specialty workforce shortage areas. In comments to the FCC, the American Telemedicine Association requested permanent grandfathering of previously eligible sites prior to the 2004 Order. Other administrative barriers in the Rural Healthcare Program include only 25% support for internet services, counterintuitive in an era in which most telehealth programs deploy technologies that are IP based.
3. Determination of discounted services - The rural-urban disparity in line rates envisioned in the original legislative language for the rural health care program for such broadband services as ISDN is disappearing with the use of alternative technologies. However, the need for broadband-based health telecommunications remains. The FCC should consider replacing current discounts in rural rates with an across-the-board discount.

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[11] FCC Second Report and Order, Order on Reconsideration, and Further Notice of Proposed Rulemaking Federal Register: February 7, 2005 Volume 70, Number 24

[12] EMTALA 42 USC 1395 dd 42

4. Eligible services - Health provider access to services including new "on demand" broadband services from alternative carriers should be included. All communications providers should be eligible to participate in the health program.
5. Rural Healthcare Pilot Program –As discussed above, in 2007, to improve utilization of the rural healthcare program, the FCC launched the Rural Healthcare Pilot program, recognizing 69 entities as eligible to receive more than $400 million in funds to expand the communications infrastructure for healthcare. As of June 30, 2009, however, entering the third year of the program, only $902,000 had been disbursed and only 12 of 69 programs received their funding commitment letters. The Pilot Program, although well intended, is fraught with significant administrative barriers. As examples, no funds were made available for project management. The applicant must obtain letters of agency from each of the remote sites, be fiscally responsible for each site's activities, secure 15% in cash as matching funds, provide detailed quarterly reporting even in the absence of funding and sign five year contracts for service. Applicants may include within their network a de-minimus number of urban locations, however, the eligible entities remain the same as those previously articulated in the Act. For-profit hospitals were specifically excluded, as were EMS providers and nursing homes. Despite these problems, the intent of the pilot program is important and should be preserved. The development of regional network grids, extending through firewalls and different network architectures to link neighboring telemedicine networks will facilitate a "best practice" model for health care delivery. This is the core of the current rural health pilot program and is a critical component in the national objective of building a healthcare information infrastructure as well as a central component in many proposed approaches to the use of

telecommunications for disaster response. The support of such regional network grids using any available broadband network or technology should be permanently incorporated into the rural health program.

Telehealth services can help drive demand for broadband adoption by increasing access to acute care and chronic disease management through networks that include hospitals, clinics, physician offices, nursing homes, ambulances, the workplace, and the home. Broadband provided over wireline, wireless, cable, satellite networks, power lines and other emerging technologies provide the communications footprint that supports the transformation of healthcare delivery. Universal service should take into account all such technologies that provide broadband services for purposes of healthcare.

In establishing universal service policies there are several other important issues related to telemedicine that need to be addressed:

1. Minimum broadband speeds – unlike entertainment applications, remote health care services rely on information coming **upstream** from the patient to the provider or monitoring center. Establishing only downstream broadband goals will ignore the rates and quality of service requirements that are essential in order to make many telemedicine applications viable.
2. Universal service support for wireless – Home telehealth is no longer tied to the home. Thousands of new remote monitoring and related health applications for wireless phones allows for the provision of care at the point and time of need. The cell phone has become a critical part of everyday life for millions of Americans and the use of wireless continues

to accelerate. Congressional reform of lifeline programs and universal service access should take into account this new development and incorporate wireless access into national goals for universal service.

OTHER FEDERAL PROGRAM CHANGES

It is not enough to simply ensure deployment of the communications infrastructure, -- we must also address other serious barriers to adoption and sustainability. The most critical barriers are limited coverage and reimbursement for telehealth services. The prime example is that the nation's largest payer, Medicare, spends only about a nickel per year per fee-for-service beneficiary for telehealth. More than 34 million disabled and elderly beneficiaries are not covered for the most common form of telemedicine, clinical services provided via interactive video, solely because they live in a metropolitan county.

The Centers for Medicare and Medicaid Services (CMS) recently published its final rule under the Physician Fee Schedule and other Revisions to Part B for CY 2010. Per CMS, "The total annual Medicare payment amount for telehealth services (including the originating site facility fee) is approximately $2 million. Previous additions to the list of telehealth services have not resulted in a significant increase in Medicare program expenditures. While we believe that these proposals will provide more beneficiaries with access to these services, we do not anticipate that these changes will have a significant budgetary impact on the Medicare program."[13]

[13] CMS Rule:Medicare Program; Payment Policies Under the Physician Fee Schedule and Other Revisions to Part B for CY 2010, p1179 http://www.federalregister.gov/inspection.aspx#special

To bill Medicare for professional services rendered via telemedicine, the beneficiary must reside in or receive care through a telemedicine system located in:

1. a federally designated rural Health Professional Shortage Area (HPSA); or
2. a county that is not included in a Metropolitan Statistical Area (MSA); or
3. via a Federal telemedicine demonstration project that was approved or funded by the Secretary of Health and Human Services as of December 31, 2000.

The Federal government and even Medicare have several definitions of "rural." The rural definition used for telehealth coverage is the most restrictive - it even classifies Grand Canyon National Park as metropolitan. Many metropolitan counties seem rural (there are about 400 of them with less than 50,000 population) and many parts of metropolitan counties almost everyone would call rural. For example, some of Medicare's critical access hospitals do not utilize telehealth because they are "metropolitan," such as Carilion Giles Memorial Hospital in the Chairman's District because it is in a metropolitan county (Giles), despite a county population in 2000 of only 16,657 and a population density of 47 persons per square mile. Store and forward telemedicine is covered under Medicare for patients in Alaska and Hawaii, but not in the other 48 states. Yet, store and forward services offer timely access to diagnosis and care, and improves the efficiency of the workforce. As an example, screening for diabetic retinopathy can be accomplished via store and forward retinal photography, resulting in early interventions that spare patients and the healthcare system the burden and cost of blindness.

In addition, Medicare Conditions of Hospital Participation Standards require that every consulting physician who provides services via telehealth be credentialed and privileged at every

consult origination site. This is an overly burdensome Medicare regulation that proves to be costly, time consuming and counter to the 2004 Joint Commission standards which allowed for credentialing and privileging by proxy with appropriate hospital and medical staff agreements. Our program at the University of Virginia makes available any of our on-call physicians for emergency or elective telemedicine consultations. If we are required to credential and privilege all 790 physicians on our medical staff at each of our 60 telemedicine sites in Virginia, it would cost the University millions of dollars in remote hospital fees and many hundreds of hours of administrative time. Each of our physicians is appropriately credentialed and privileged at the University of Virginia, and we detail the scope of services and ensure the credentials of our participating physicians in letters of agreement with each telemedicine partner.

Medicaid coverage determinations fall within the purview of the states, despite federal law which governs the Medicaid programs. More than 30 states include telemedicine as a covered service under Medicaid. Virtually all Medicaid programs fund the cost of transportation to care. To spend millions of dollars on transportation to care, but not reimburse consultations provided more cost effectively over telemedicine networks is incomprehensible..

Third party private pay reimbursement for telehealth has been mandated by statute in ten states, and three more state legislatures, including the Virginia General Assembly, have before them similar bills. The American Telemedicine Association proposes that any federally supported health insurance plan require coverage for telehealth services.

To ensure expansion of telehealth, the continued development of technology standards and clinical practice guidelines beyond what has been accomplished to date should be funded.

Federal agency alignment, engagement and incentivization of the states and the private sector remain a critical priority. **We strongly urge Congress to require greater interagency collaboration for telehealth services, with a goal of advancing telemedicine within all the agencies.** More than a dozen federal agencies recognize or fund telemedicine related grant programs and services and yet there is no office for or champion of telehealth within the Centers for Medicare and Medicaid Services. This is why the CMS Telehealth Advisory Committee called for in the House health care reform bill is so important. Equally important, is the need for collaboration between Federal Communications Commission and relevant agencies of multiple departments, notably Health and Human Services, Defense, Veterans Affairs, Commerce and Agriculture.

The recently House approved health reform bill, H.R. 3962, expands the eligible consult origination sites, and allows for credentialing by proxy but not privileging which remains a costly and time consuming process. The Senate bill, and in particular the recently introduced Rural Telemedicine Enhancing Community Health Act, S. 2741, addresses both credentialing and privileging barriers, and expands coverage, importantly to priority safety net sites: HHS-funded community health centers and Indian Health Service facilities.

In conclusion, as our nation moves forward in restructuring its healthcare delivery system, innovative uses of telehealth tools will likely be an important driver of that change. With the adoption of favorable policies, innovation applied to the care of patients using integrated telehealth tools that include interactive video teleconferencing, home telehealth, remote monitoring, and mobile health technologies hold promise to enhance access to timely, appropriate and expert care that will improve the health of our citizens. Universal Service

Reform and accelerated broadband deployment and adoption are critical pillars of this transformation of healthcare for all Americans. Thank you.

FF Principal Investigator/Program Director *(Last, first, middle):* Rheuban, Karen, S.

BIOGRAPHICAL SKETCH

Provide the following information for the key personnel in the order listed for Form Page 2.
Photocopy this page or follow this format for each person.

NAME	POSITION TITLE
Karen S. Rheuban	Professor

EDUCATION/TRAINING *(Begin with baccalaureate or other initial professional education, such as nursing, and include postdoctoral training.)*

INSTITUTION AND LOCATION	DEGREE *(if applicable)*	YEAR(s)	FIELD OF STUDY
University of Rochester	BS, cum laude	1971	Biology
Ohio State University	MD, summa cum laude	1974	Medicine
University of Virginia		1974-1977	Pediatric Resident
University of Virginia		1977-1978	Chief Resident
University of Virginia		1978-1980	Fellow, Pediatric Cardiology

Employment History

1980-present, Professor, Pediatrics, School of Medicine, University of Virginia
1990-present, Associate Dean, Continuing Medical Education, School of Medicine, University of Virginia
1994-present, Medical Director, Office of Telemedicine, School of Medicine, University of Virginia
2004-present Senior Associate Dean for External Affairs and Continuing Medical Education

Memberships

Fellow, American Academy of Pediatrics
Fellow, American College of Cardiology
American Telemedicine Association, President
Member, Scientific review committee, American Telemedicine Association
Board Chair, Virginia Telehealth Network
Center for Telemedicine Law, Board member
American Heart Association, Telestroke Subcommittee

Research Projects Ongoing or Completed

- "Southwest Virginia Alliance for Telemedicine". Karen S. Rheuban, PI. Sponsor: United States Department of Commerce (DOC). Oct 1, 1997-December 31, 2002. #51-60-97044-NTIA
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Mr. BOUCHER. Mr. Rosston.

STATEMENT OF GREGORY ROSSTON

Mr. ROSSTON. Good morning. Thank you. My boss has always told me in order to do a good job, you should pick your predecessor. Unfortunately, I have failed in that today, but I am going to go ahead with my testimony anyway.

I would like to thank Chairman Boucher, Ranking Member Stearns and members of the subcommittee, with special recognition for my representative, Congressman Eshoo, for the opportunity to appear before you here on this very important matter.

Before I start, I want to recognize my colleagues, Brad Wimmer of the University of Nevada Las Vegas for his work on this testimony and our research over the past decade on universal service.

I serve now as Deputy Director of the Stanford Institute for Economic Policy Research and have studied universal service for more than 10 years.

We are pleased that you have put forth legislation to reform the current universal service program. As with any program, it is important to implement universal service in as efficient a manner as possible.

The current discussion draft includes some provisions that likely increase the efficiency of the universal service program, but changes are possible that could decrease the costs substantially without sacrificing coverage or quality. The committee should implement legislation that makes revenue raising as efficient as possible and harnesses the power of the market to drive down subsidies and increase competition for consumers.

First I will address the revenue side. The charges to raise money for universal service distort customer behavior and can be very costly. The best way to minimize these distortions are to have a low tax rate which can be achieved by keeping the size of the program relatively small and then deriving the revenues from a broad base.

It is good that the proposed legislation broadens the funding base. That should reduce distortion, if the lower tax rates do not induce increased spending. Using general tax revenues would be a better way to funduniversal service. While such an approach may not be politically feasible at this point in time, it should be considered.

The discussion draft has several provisions; declaring broadband to be universal service, using wire center averaging, the primary line rule, and eliminating the so-called parent trap, that have to the potential to increase the size of the Universal Service Fund; and some draft provisions have the potential to compound harm by decreasing efficiency without any offsetting benefits.

So now I want to move on to service provision. The primary reason that a household does not connect to the communication network is because the household is not willing or able to pay as much for telecommunication services as the price charged. The Lifeline and Linkup programs provide subsidies to low income households in an attempt to increase subscriptions rates among poorer households.

Representative Matsui has introduced a bill that would extend the Lifeline and Linkup programs to cover broadband service. We think such a program has the potential to increase broadband subscriptions rates among low-income populations, although more study is needed before any firm conclusions can be drawn.

The results of our recent research indicate that moving money from the Lifeline program to the Linkup side has the potential to increase the penetration rate without increasing the program size, because Linkup is targeted to households not connected and because low-income households face high barriers in upfront costs to getting connected.

The high cost fund subsidizes the companies that provide services in the high cost areas. The majority of these subsidies are given to the incumbent local exchange carriers, or ILECS, and the discussion draft includes several proposals that appear to insulate the ILECS from competition for subsidies, which, in turn, insulates them from competition.

It would be best to distribute subsidies to rural customers themselves, not to the companies that serve them. Extending a program like Lifeline with costs in income based vouchers to rural customers and urban customers could accomplish this goal, as Mr. Doyle discussed.

Every dollar in the USF program comes from someone else's pocket, so it is important to be careful on how this is spent. The rural high cost fund has increased substantially over the past several years, but one cause of this, competition, provides an indication that the current system is broken and that there is room to reduce instead of increase subsidies. Competition should drive down subsidies not increase them.

The discussion draft is a plan to use subsidy auctions, but only in very limited circumstances and not for all providers. Instead, subsidy auctions should be used pervasively. There should be subsidy auctions when there are two or more providers of any type, and all providers should participate in a subsidy auction. Such expansion of the subsidy auction plan could help drive down subsidy payments substantially while at the same time protecting consumers.

The most important feature of the subsidy auctions is that the incumbent local exchange providers would be subject to competitive discipline in the amount of subsidy that they receive for providing service.

If it truly costs a lot of money to serve households in rural areas, companies serving the consumers in those high cost areas will end up with relatively high subsidy payments through the auction system. But if there are ways to serve the customers more efficiently, as Mr. McSlarrow has stated, the auction system will reveal it.

The current system and the system in the current draft do not have these critical features. There is little incentive to reduce costs or the overall size of the Universal Service Fund. Obviously, the design of subsidy auctions needs to be considered carefully. But the experience with subsidy auctions in other countries and the success with spectrum auctions in its United States shows that we can implement such a system in a pro-competitive manner.

Major concern that we have overall is that there not only be mechanisms to reduce the growth of the fund, but that there also be mechanisms to make the fund as small as possible while still satisfying the goal will of connectivity.

We think that the current bill makes a very good move towards broadening the base of support to minimize distortion and arbitrage incentives. We also think that it could be improved substantially if it were to set up a framework to allow competition to reduce the size of the subsidize, because that would be in the interests of all consumers. More detail is in our written testimony.

Thank you for having me here today. I am happy to answer any questions.

Mr. BOUCHER. Thank you, Mr. Rosston.

[The prepared statement of Mr. Rosston follows:]

Testimony of

Gregory L. Rosston
Stanford Institute for Economic Policy Research

and

Bradley S. Wimmer
University of Nevada, Las Vegas

on

Universal Service Reform

Before the

Committee on Energy and Commerce

Subcommittee on Communications Technology and the Internet

United States House of Representatives

Washington, D.C.

November 17, 2009

Testimony of

Gregory L. Rosston and

Bradley S. Wimmer

Good Morning. I would like to thank Chairman Boucher, Ranking member Stearns and members of the subcommittee for the opportunity to appear before you on this very important matter. We are economists at Stanford University and the University of Nevada, Las Vegas who teach and conduct research in the areas of microeconomics, regulation and competition policy. Neither of us is representing any entity regarding universal service – the views expressed here today result solely from our academic research and government service. Both of us have studied universal service issues since we served as economists at the Federal Communications Commission in the mid-1990s. Since that time, one strand of our research has focused on the effects of universal service on consumers and competition. To that end, we are very pleased that you have put forth legislation to reform the current system.

Our view is that universal service can be a very important societal goal; connecting people to the voice and data information networks can have profound impacts on people's lives in terms of safety, productivity, and participation in society. As economists we are interested in providing such connectivity in as efficient a manner as possible. It is important that policy makers consider carefully all of the costs and benefits associated with a universal service program when determining the extent of the program, how and to whom subsidies are dispersed, and the manner in which revenues used to fund the program are raised.

We are encouraged that the current discussion draft includes provisions that likely increase the efficiency of the universal service program. We believe however that further improvements are available; and that such improvements could substantially decrease the cost of the program without sacrificing coverage or quality. With these changes either more consumers can be served without increasing the cost of the program or consumers can benefit from lower prices.

Our comments today will address the components necessary for a well-designed universal service program. Such a program raises revenues in a way that minimizes distortions, minimizes the cost of obtaining the desired outcomes, and determines program size based on a careful examination of the costs and benefits of the program. Our comments will touch upon these components and how the proposed legislation addresses them. Then we offer suggestions on how the universal service program and proposed legislation could be improved to achieve the same or greater levels of connectivity at a much lower cost to society.

Our main points are as follows:

- Universal service can serve an important societal goal.
- Reducing the tax rate by increasing the revenue base so it includes more services, holding the fund size constant, is good policy.
- The fund size should be controlled to minimize distortions caused by the taxes, or contributions, used to fund the programs.
- Lifeline and linkup may help increase low-income penetration
- Subsidies should go to consumers, not companies, to increase competition and choice
- Companies should not be insulated from competition and should not receive subsidies if they are not the most efficient service provider
- Subsidy auctions should be used pervasively to increase competition, consumer choice, and to drive down the cost of the program.

REVENUE RAISING

The charges used to raise money for universal service may not be "taxes" in the legal sense of the word, but to an economist, they are a form of taxation and the large public finance literature on taxation provides important lessons for understanding the impact of fees or surcharges or whatever else they might be named. Taxes distort consumer behavior because they change the relative prices of goods and services. This distortion has been shown to be very costly – on the order of 1/3 more than the revenue raised (Ballard, Shoven and Whalley, 1985). Economics tells us that the best ways to minimize these distortions are to have a low tax rate, which can be achieved by keeping the size of the program relatively small, and the deriving revenues from a base that is broad.

While some may object to taxing phone and/or broadband to fund phone and/or broadband, it is important to note that the payers of the tax and the recipients of the subsidy are likely to be different people or different groups. However, because some of the people receiving subsidies will also pay taxes, they see the price of some services increase. This counteracting effect reduces program effectiveness. Hausman et al. (1993) found that taxes on long-distance, that were used to cross subsidize basic subscriptions to the network caused a substantial number of households to discontinue telephone services altogether. These concerns lead us to conclude that using general tax revenues would be the best way to fund universal service – the base is broad and it would not add significantly to the percentage tax burden. While such an approach may not be politically feasible at this point it time, we feel that it should be considered.

We are encouraged that that proposed legislation broadens the base from which revenues are raised from interstate revenues, to a system that assesses contributions based on revenues derived from the provision of intrastate, interstate and foreign communications services; a system based on telephone numbers and network connection; or a combination of these two approaches. Broadening the base from which contributions are derived reduces the costs associated with raising revenues, and, holding program size constant, is good policy. The changes in the tax base proposed in the discussion draft also eliminate arbitrage problems that arise from arbitrary interstate/intrastate distinctions (Rosston and Wimmer, 2000).

There will, however, remain incentives to categorize services so that they do not qualify to pay universal service fees. However, with a lower fee, such incentives are reduced. Decreasing the amount of revenues required to fund the program also reduces the distortions associated with collecting revenues. Decisions that affect the size of the program not only affect the amount of money that needs to be raised, but also affect the distortions associated with the tax – the rate of loss caused by tax distortions increases more than the increase in the size of the tax. It is therefore important to design a program that minimizes the cost of achieving its goals, and that policy makers carefully consider the benefits and costs associated with different aspects of the program.

The discussion draft addresses several issues that could have a major impact on the size of the universal service fund. For example, the discussion draft declares broadband to be a universal service, uses wire center averaging rather than study-area averaging to determine high-cost subsidy amounts, and eliminates the "parent trap," which requires that when a carrier acquires telephone exchanges from an unaffiliated carrier its universal service support does not change. Each of these proposed changes has the potential to increase the size of the universal fund. We encourage policy makers to evaluate the effects each of these changes has on the fund size and how they affect the efficiency of service delivery. Some of these proposed changes have the potential to compound harm by increasing costs and decreasing efficiency.

The discussion draft proposes to institute a cap on the size of the funds, although the above-mentioned items are not included in this cap and there may be other mechanisms that increase the size of the fund. Finally, the discussion draft proposes to begin using auctions to determine high-cost subsidies. This last proposal, if properly implemented, has the potential to improve dramatically the efficiency of the high-cost universal service program.

EFFICIENT SERVICE PROVISION

Universal service, in theory, means ensuring that people who would not otherwise connect to the network do so because of a government program. For this testimony, we focus on how well the current, and proposed, low-income and high-cost programs contribute connecting people who would not otherwise connect.

Low-Income Support

The primary reason that a household does not connect to the communications network is because the household is not willing or able to pay as much for telecommunications services as the price charged. A subsidy reduces the household's cost of subscribing, and hence increases the likelihood that a household connects to the network. The FCC's Lifeline and Linkup programs provide subsidies to low-income households in an attempt to increase subscription rates among poor households. These programs may be considered effective when the subsidies are given to households who, in the absence of the subsidy, would not be connected to the network. Conversely, the program does less to contribute to universal service when subsidies are provided to households who would connect to the network even if the subsidies were eliminated. In such a case, the low-income subsidy does not increase universal service – it simply results in a transfer payment.

Empirical research has shown that local telephone service is extremely inelastically demanded. This means that subscription decisions are not very sensitive to price. It would take a large increase in price to cause people who were subscribing to the network to drop telephone service, or a large decrease in price to get people to subscribe. As a result, subsidy programs are not expected to have a large effect on subscription decisions – people generally place a high value on telephone service and would subscribe in the absence of a subsidy (at least in the relevant range of prices).

Our recent research (Ackerberg, Riordan, Rosston and Wimmer, 2009) examines the effectiveness of the Lifeline and Linkup programs. We find that while they are relatively more sensitive to price changes than the general public, low-income households' demand for telephone service responds very little to a reduction in price. This finding indicates that Lifeline and Linkup programs have a small effect on the penetration rate of low-income households. Connecting an additional low-income household using the Lifeline program, which reduces a household's monthly rates, is expensive. Conversely, we find that Linkup program, which provides a subsidy that reduces the initial charge for connecting to the network, is more cost effective than the Lifeline program. We suspect that is the case because the Linkup program, by definition, targets households who are not currently connected to the network. In addition, it helps households avoid the high up-front costs associated with connecting to the network. This is particularly important for households that face severe credit constraints and relocate frequently. While the discussion draft mentions Lifeline and Linkup, it does not propose any

changes. The results of our research indicate that moving money from the Lifeline program to the Linkup side has the potential to increase the penetration rate of low-income households without increasing the program size.

Representative Matsui has introduced a bill that would extend the Lifeline and Linkup programs to cover broadband service. We think that such a program has the potential to increase subscription rates among low-income populations, although more study is needed before any firm conclusions can be drawn. We expect that the FCC's Broadband Report will provide more information about this when it is released early next year. As in the case of basic telephone service, the effectiveness of a broadband program depends on low-income households' elasticity of demand for broadband service and the subsidy's size. We are not aware of any recent studies that provide estimates of these elasticities. Research that focused on low-income adoption rates under current rates, and possibly surveys of willingness to pay for broadband service, would provide guidance on how to design a broadband Lifeline program. The Matsui Bill has the potential to provide an important venue for acquiring more information on the ability of a Lifeline program to increase broadband penetration rates. It would be extremely useful to design program evaluation into the proposal for any broadband Lifeline and Linkup program to ensure effective use of subsidy money.

High Cost Support

The goal of the high cost fund is to ensure that customers living in rural areas pay prices for telecommunications services that are reasonably comparable to prices paid by customers in urban areas. To accomplish this goal, the high-cost fund subsidizes telecommunications companies that provide services in these areas. The majority of these subsidies are given to the incumbent local exchange carriers (ILEC). The discussion draft includes several proposals that appear to insulate the ILECs from competition for subsidies, which, in turns, insulates them from competition in general. For example, the discussion draft places a cap on the size of the total amount of universal service support that is based on the total number of ILEC working loops. While the cap is allowed to increase if the number of loops grows, it is not allowed to fall if the number of ILEC loops fall. In addition, the discussion draft proposes that subsidies be determined through a competitive bidding process. This process, however, is only to determine the amount of subsidy provided to wireless carriers. ILEC subsidies will be determined using alternative measures that are generally not affected by competition.

The Telecommunications Act of 1996 opened telecommunications markets to competition, with the goal of providing customers options when choosing telecommunication services. In urban areas, customers can choose among several technologies, such as landline, wireless and IP, for their telecommunication needs. Rules that favor a particular carrier or technology run counter to the goals of the Telecommunications Act. In general, high cost support programs should be competitively neutral, allowing the rural customers to determine the services that meet their telecommunications needs. We believe that this could best be achieved by distributing subsidies

to rural customers themselves, not the companies that serve them. Extending a program like Lifeline to rural customers could accomplish this goal. Such an extension has the additional benefit of allowing that subsidies be based on the customer's ability to pay as well as the cost of providing service. In the event that such a proposal is too radical, and is not politically feasible, we believe that a high-cost program that continues to subsidize companies must be competitively neutral and have built-in mechanisms that allow the size of subsidies to fall if costs fall. Our comments below explain how the proposals contained in the discussion draft can be altered to achieve this important goal.

It costs more to provide terrestrial telecommunications service in rural areas because of longer loop lengths and lower household densities. Governments have instituted a number of different programs to reduce the prices paid by rural consumers, and to ensure that telephone companies serving rural areas remain profitable. Rural high-cost subsidies come in many forms in the current system – directly from the federal universal service fund (USF), directly from states, indirectly through access charges and indirectly through implicit cross subsidies internal to the providers. Because of the complexity of the system and the entrenched interests in maintaining the current systems, it may be politically difficult to modify it to improve efficiency. We believe that some small changes in the proposals in the discussion draft will result in rural customers receiving improved services for less money; possibly substantially less money.

One goal of regulation should be to have service provided at the lowest cost possible to minimize the need to raise revenue. It would be wonderful to know the true cost of the most efficient provider to deliver service to each household across the country, and to have a time path of the costs for the next ten or twenty years. That is unrealistic, so we need to rely on other mechanisms to reveal the best information about those issues.

The rural high cost fund has increased substantially over the past several years. One explanation is that new CETC's have begun to provide service and to receive subsidy payments. These companies have begun to provide service and to make money doing so because they are able to provide the service at a cost below the value of the subsidy plus the customer charges. As a result, some have argued that they do not merit such a high subsidy. This indicates that there may be room to lower the subsidy payments.

The other side of the increase in subsidy payments is that the new CETCs have taken customers away from the traditional incumbent wireline carriers, yet the subsidy payments to incumbent wireline carriers has not diminished. While some may view that there is an implicit contract or need for a traditional Carrier of Last Resort, the competition indicates that there may be room to provide service more efficiently.

The discussion draft has a plan to use auctions for subsidy payments in limited circumstances. Subsidy auctions have been under consideration for nearly 15 years at the Commission, but have never been undertaken. However, subsidy auctions can be an effective tool for inducing

providers to compete to provide service at a low cost to taxpayers. In essence, the government can use auctions to harness the power of market incentives to ensure that rural customers get service and that the service is not expensive for them or for urban customers who provide the funds for rural subsidies.

While the current discussion draft makes good progress by mandating subsidy auctions in certain circumstances, there is much more potential gain from more extensive use of auctions. In particular, the discussion draft limits subsidy auctions to situations where there are three or more wireless providers willing to compete for a subsidy to provide service. In those situations, there are likely to be a total of four or even five or more competitors when one considers the telephone and cable companies that could be or already are serving households in those areas. Instead of having auctions limited to times when there are three or more wireless carriers, and limiting the subsidy auction to the wireless carriers, it would be much better to use subsidy auctions more broadly.

Competition from a variety of sources is important. The discussion draft makes no mention of cable or other wireline competitors. Cable and other should be able to compete for subsidy dollars, to the extent that they are necessary to induce service provision. To the extent that companies are willing to provide the required service without subsidy dollars, there is no need to provide subsidy dollars to any company. Kyle McSlarrow testified here two and a half years ago that cable broadband was then available to 94% of U.S. households (McSlarrow, 2007) Eisenach (2009) presents analysis showing that cable systems are making broadband service to a large percentage of high cost households without receiving any subsidy. Cable companies that have upgraded their networks to provide broadband and telephone service without a subsidy implies that no other company should get a subsidy for serving customers in those areas. In these cases, if there is a subsidy auction, the cable company should be able to participate in the same manner as others, and if it is a low-cost efficient provider, it will bid a low or zero subsidy. This competition will benefit consumers in all areas – those receiving competitive service and those funding universal service subsidies.

In particular, it would be more efficient to have subsidy auctions when there are two or more providers of any type and to include all providers in the subsidy auction. Such expansion of the subsidy auction plan could help drive down subsidy payments substantially while protecting consumers. The auctions with three or more wireless carriers (those contemplated in the discussion draft) would be more competitive because the wireless carriers would be forced to compete with wireline carriers as well. More importantly, auctions would be used in many more geographic areas, providing downward pressure on subsidies and the size of the universal service fund which would be good for all consumers – urban and rural.

At the same time, consumers in subsidy auction areas would continue to receive service at the mandated rates since the auctions would be designed in a way that protected rate payers. While companies expecting to receive high or excessive subsidies are likely to object to the additional

competition and potential for reductions in subsidies, competition through subsidy auctions is in the interests of rural and urban consumers. The most important feature of expanding the auctions is that incumbent local exchange providers would be subject to competitive discipline in the amount of subsidy that they receive for providing service. If it truly costs a lot of money to serve households, companies serving consumers in high cost areas will end up with relatively high subsidy payments through the auction system. But if there are ways to serve the customers more efficiently, the auction system will reveal it. Subsidy auctions are a way for regulators to induce firms to more truthfully reveal their costs of service and to reduce the cost of service. The current system and the system in the current draft does not have these critical features – it does not provide an incentive to reduce costs nor to reduce the overall size of the universal service fund. Any system that exempts the incumbent providers from competition and insulates their subsidy payments will increase costs and decrease efficiency, threatening the efficacy of the universal service program.

Obviously, the design of the subsidy auctions needs to be considered carefully, but the experience with auctions in other countries provides some guidance for how to implement these types of auctions effectively (Wallsten, 2009). It would be relatively easy to implement subsidy auctions in a short period of time and in a competitively neutral manner because of substantial advances in auction theory and applications. Many prominent auction economists have examined subsidy auctions and more general procurement auctions and agree that ubiquitous subsidy auctions would increase efficiency substantially. In fact, we were part of a group of 71 auction and telecommunications economists who submitted comments to NTIA and RUS encouraging them to use auctions to award the broadband stimulus grants (71 Concerned Economists, 2009). The same logic in those comments applies here – competition will benefit consumers by driving down costs.

The U.S. should implement extensive use of subsidy auctions. The nature of the problem allows such auctions to be rolled out over time to test and modify the auction design. The FCC could designate some areas for auction immediately. For example, the first areas designated for auction could be areas where there are two or three providers in addition to the incumbent local exchange provider. It would be important to ensure that all providers receiving subsidy be put on notice that the FCC planned to institute auctions more broadly over a short period of time. As Congress did with spectrum auctions, time limits for the implementation would be useful to insulate the FCC from political pressure to delay auctions.

The FCC implemented its simultaneous multiple round auctions for spectrum licenses with a gradual roll out over a short period of time. In the Omnibus Budget Reconciliation Act of 1993 (OBRA), congress gave the FCC a very short timeline for implementing auctions. The FCC started with a relatively straightforward auction of 10 nationwide narrowband PCS licenses less than six months from passage of OBRA '93. After conducting the nationwide narrowband PCS auction, the FCC modified its software and ran a second auction for 30 regional narrowband PCS licenses. Finally, about six months after its first auction, the FCC used the refined auction

software and design for the PCS Broadband A & B block auction and has continued to use that system (with modifications) for many subsequent auctions (Kwerel and Rosston, 1999). Other countries have also used the FCC auction system as the basis for their spectrum auctions. The idea of a short time frame for starting auctions with mandated times for broader implementation could work well for subsidy auctions as well.

Universal service money should be to connect consumers in an efficient manner, not to provide an unnecessary subsidy to companies. In those cases where the incumbent provider is the most efficient provider of service, it will bid the lowest subsidy in the auction and get the subsidy money and serve the customer. Universal service reform has the chance to reward efficient local telephone companies that are efficient and serve customers, and to save consumers money if there are other more efficient providers.

If there is any view that there is some implicit contract with the incumbent providers, we believe that should be treated separately. For example, it might be the case that the incumbent could be guaranteed a declining fixed annual payment for five more years regardless of its success in the market or auction. That way, the payment would not distort competition and there would be a set end to the implicit contract. Such a payment would depend on a detailed accounting of costs, revenues, dividends, other transactions, and an evaluation of any implicit contract.

There are other provisions of the discussion draft that have the potential to increase the size of the universal service fund, possibly without any benefit to consumers. The elimination of the "parent trap" provides an incentive for a large company that does not qualify for universal service funding to sell exchanges to small companies that do. Currently, such sales would take place if the smaller company were more efficient, and the sales price would be lower to reflect the lack of a subsidy. Under the discussion draft, there would incentives to sell to less efficient small companies and to increase the size of the universal service fund, both of which would be bad for consumers. The move to a wire center basis for funding also has the potential to increase the size of the fund. We would be less concerned with these issues if the bill adopted a comprehensive subsidy auction that put all of the subsidies up for competition.

The major concern we have overall is that there not only be mechanisms to reduce the growth of the fund, but that there also be mechanisms to make the fund as small as possible while still satisfying the goal of connectivity. We think that the current bill makes a very good move to broadening the base of support to minimize distortion and arbitrage incentives. We also think that it could be substantially improved if it were to set up a framework to allow competition to reduce the size of subsidies.

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Biographies

Gregory L. Rosston is Deputy Director of the Stanford Institute for Economic Policy Research and Deputy Director of the Public Policy program at Stanford University. He is also a Lecturer in Economics and Public Policy at Stanford University where he teaches courses on competition policy and strategy, intellectual property, and writing and rhetoric. Dr. Rosston served as Deputy Chief Economist at the Federal Communications Commission working on the implementation of the Telecommunications Act of 1996 and he helped to design and implement the first ever spectrum auctions in the United States. He co-chaired the Economy, Globalization and Trade committee for the Obama campaign and was a member of the Obama transition team focusing on economic agency review and energy policy.

Dr. Rosston received his Ph.D. in Economics from Stanford University specializing in the fields of Industrial Organization and Public Finance and his A.B. with Honors in Economics from University of California at Berkeley. Dr. Rosston has written extensively on the application of economics to telecommunications issues and is the co-editor of two books relating to telecommunications. He has served as a consultant to various organizations including the World Bank, and as a board member and advisor to high technology, financial, and startup companies in the area of auctions, business strategy, antitrust and regulation. He also serves as an advisory board member for Sustainable Conservation and the Nepal Youth Opportunity Fund.

Bradley S. Wimmer is an Associate Professor of Economics at the University of Nevada, Las Vegas. Dr. Wimmer has published numerous articles on the effects of regulation and deregulation on market outcomes in telecommunications. Dr. Wimmer served as a senior economist at the Federal Communications Commission from 1995 to 1998. During his time at the Commission, Dr. Wimmer worked extensively on issues related to the implementation of the Telecommunications Act of 1996, including universal service. While at the Commission, Dr. Wimmer served as the Acting Chief Economist of the, then named, Common Carrier Bureau, which was in charge of overseeing interstate telecommunication services. Dr. Wimmer received his Ph. D. in Economics from the University of Kentucky in 1992 specializing in the fields of Industrial Organization and Labor Economics. He received his BA in economics from Coe College, located in Cedar Rapids, IA in 1988.

Mr. BOUCHER. Our thanks to all of our witnesses for their very thoughtful comments here this morning, and particularly for the broad consensus in support of the draft legislation that you have expressed today.

I am going to direct several questions to our rural representatives, Ms. Moyer and Mr. Greer, and I am going to begin by referencing the recommendations made by Mr. McSlarrow, where he says that the principles of competitive neutrality may be violated where you have wire line voice competition with one wire line carrier receiving support and competing with a wire line carrier that does not.

On its face, I think his argument has merit, and I am wondering what your response to that is? If we were to consider a provision that would prohibit support being provided in those instances where you have actual voice competition by wire line, limiting the unavailability of support just to the precise areas where the competition actually exists, what would be your response to that?

I realize it may be a question of first impression, and if you don't have a definitive answer today, that is certainly acceptable. But I wanted to pose that to you and get your thoughts, at least for the record, this morning.

Mr. Greer.

Mr. GREER. Yes, Chairman Boucher. On the surface, we do have some concerns with the competitive bidding between the two.

Mr. BOUCHER. It wouldn't necessarily—let me just interrupt to say—be a competitive bidding. I think his proposal doesn't actually relate to competitive bidding. It relates to simply saying that support would not be available where you have a carrier that is offering voice service without support.

In theory, where you have a carrier that is offering the service in that particular study area without support, it suggests that support is not necessary in order to sustain a service. So he is suggesting that you not have competitive bidding. You just deny the support under that circumstance.

Mr. Greer.

Mr. GREER. I would like to think on that for just a moment real quick.

Mr. BOUCHER. That is fine.

Ms. Moyer.

Ms. MOYER. I guess I would like to point out that one of the problems with our service area with 5,000 square miles is that roughly only 15 of those square miles would be what I consider town. Within those 15 square miles, there is a cable company that serves. It actually belongs to us because no one else wanted to come in and provide cable service. But the problem being within that 15 square miles, the majority, over 90 percent of our population is going to reside in those areas.

So when we get outside of those areas, we are talking about very few customers and a very large service area that would need to be served. Thus, you are talking about dollars that are going to be exponentially related to those very few customers.

Obviously, I have read NCTA's proposal here just last week, but we would be more than happy to submit something further to you on the record in writing.

Mr. BOUCHER. Well, let me encourage you to think about it and to engage with us on that subject. I think a number of members are going to have those interests.

Mr. Greer, would you like to respond further?

Mr. GREER. Yes, sir. Thank you, Chairman Boucher.

In those areas to where there is wireless and wire line competition, when we look at our USF and how we average our costs, we average it over our whole service area. So if you just eliminated a portion of that, then our costs in those other areas that are unaveraged will actually go up. That is one of the concerns we would have, is they may serve a portion of our service area, but it doesn't do a complete coverage, so it will actually drive up our costs, because we average that through our service territory.

But we also want to get back to you with further comments.

Mr. BOUCHER. That is fine. I thank both of you for that. Frankly, I would have been somewhat surprised if you had just immediately agreed with the entire recommendation.

Let me pose another question to you. Some have suggested that the high cost fund, approximately $4.5 billion per year, be repurposed in whole or in part in order to provide broadband services. My understanding is that that $4.5 billion each year is spoken for. That funding is presently fully subscribed in order for you to offer the telephone services that you are offering. That money is subscribed for equipment, for maintenance, for your normal operations.

My question to you is what response do you have to the idea that some repurposing could take place, with money devoted today to those needs being devoted tomorrow to broadband? What would happen in your exchanges if that were to occur?

Ms. Moyer.

Ms. MOYER. One of the issues is that 2-year lag, the 2 years in between when we actually put money in the ground and 2 years later we actually receive the support or the cost recovery for those dollars we have already spent. So part of that problem going forward is the issue of what happens to what I spent in 2009 if in 2010 the entire fund is repurposed.

There are ongoing maintenance costs that are always going to be there. My company is in southwest Kansas. We are several hundred miles from any major metropolitan area. That transport to any major metropolitan area is huge, not just to mention just meeting up with carriers at tandems. So those costs, those dollars have already been spent. Then to recover those, there needs to be, if in fact we are going to repurpose the fund, there seems to be some attention paid to the fact of the 2 year lag.

Mr. BOUCHER. Very quickly, Mr. Greer.

Mr. GREER. We concur with those comments as well. Currently, the costs that we spend, we are not reimbursed until 2 years down the road anyway.

Mr. BOUCHER. So you do agree that those monies are fully subscribed?

Mr. GREER. They are fully subscribed.

Mr. BOUCHER. And there is nothing available really to support broadband deployment within the size of the existing fund without

surrendering the low cost, the affordable telephone service that you presently provide?

Mr. GREER. That is correct.

Mr. BOUCHER. Thank you very much. My time has expired. The gentleman from Florida, Mr. Stearns, is recognized for 5 minutes.

Mr. STEARNS. Thank you, Mr. Chairman.

Mr. Lubin, Vice President of Public Policy, AT&T Services. You are probably a good one to answer this, and I have limited time so if you could just answer in a very small amount of time by the word "increase" or "decrease" can the key terms to use.

Could you estimate whether each of the following provisions is more likely to increase or decrease the size of the fund. Or, if it is unclear to you, could you please tell us what additional information you would need to provide a cost estimate.

The first one is moving from a geographic to wire-center averaging. Does it increase or decrease the fund? That is moving from geographic to wire center averaging. Just your humble opinion. Just move the mike close to you, if you could.

Mr. LUBIN. It sounds like a simple question, and I will give you a simple answer.

Mr. STEARNS. Just does it increase or decrease?

Mr. LUBIN. My guess it is going to increase. However, it is a function of what model you use, and the current language in the bill says 2.75.

Mr. STEARNS. Using that modeling, would it increase or decrease?

Mr. LUBIN. When you say "using that modeling," it is not clear to me what model which are using in the bill.

Mr. STEARNS. That is a good point. That goes to the idea that you need additional information before you could say increase or decrease. At this point you are saying at your first hand blush, it increases.

Mr. LUBIN. That particular piece.

Mr. STEARNS. The next one is eliminating the parent trap rule. I had that explained to me. I wasn't sure what that is, but now I do, and I think you know what the parent trap rule is. So would it increase or decrease the fund, eliminating the parent trap rule?

Mr. LUBIN. The potential is it would increase. It is a function of how many exchanges and lines get sold.

Mr. STEARNS. Creating an alternative recovery mechanism for intercarrier compensation revenues.

Let me repeat that. Creating an alternative recovery mechanism for intercarrier compensation revenues. Will that increase the size of the fund or decrease it in your opinion?

Mr. LUBIN. That has the potential for increasing. Again, it is a function of how and what the benchmarking means.

Mr. STEARNS. OK. So in this question I have given you three areas, and it looks like to me in all three areas you said it would increase.

Mr. LUBIN. I said the potential is there.

Mr. STEARNS. Potential. OK. Let me have Verizon. Do they have any disagreement on this?

Mr. GREER. No disagreement on that, Representative Stearns. I think you are probably getting to the second half of the question,

which is are there other aspects of the legislation that could potentially decrease the size of the fund as well.

Mr. STEARNS. I am happy with the decrease. I am just concentrating this morning on what areas that I think might increase, just so we have an understanding where the worst case scenario would be.

Mr. Rosston, is there anything you might want to comment on this relative to Mr. Lubin's answers?

Mr. ROSSTON. No, I agree that I think those all three provisions would increase, are likely to increase the size.

Mr. STEARNS. Likely increase. Mr. Lubin has indicated in some cases he would need additional information to provide a real cost estimate. Do you think you can emphatically say, more so than he, he sort of has some qualifying points here. Do you feel pretty much that all three of them will increase in your mind?

Mr. ROSSTON. Mr. Lubin has studied this in much, much more detail than I have. But, for example, the parent trap would have almost no chance of decreasing the fund, and any sales would probably increase the size of the fund, as one example. The same would be true of intercarrier compensation.

Mr. STEARNS. Let me go to Mr. McSlarrow. You recommended targeting support for broadband services to areas and consumers that currently lack service. I guess the first question is, do we know those areas and consumers, where they are today? Do we know where they are?

Mr. MCSLARROW. I think by and large we do, so I think we do have the ability to target support where it is most needed.

Mr. STEARNS. Shouldn't we wait on the results of the 7.2 billion broadband stimulus and the broadband mapping efforts that are currently underway before paying companies even more to provide broadband service in areas that may already have it?

Mr. MCSLARROW. I think the answer is yes, but I think it is going to happen. I mean, the timeline here, we are already in November of 2009. The mapping will get done next year, and any plausible scenario where this legislation moves, I think it will match up so we have that data.

Mr. STEARNS. So in your opinion, we shouldn't wait?

Mr. MCSLARROW. No, I am not suggesting we wait. What I am suggesting is the mapping I think will get done——

Mr. STEARNS. Before the bill passes?

Mr. MCSLARROW. Yes.

Mr. STEARNS. Dr. Rosston, isn't it true that a tax on broadband could decrease broadband subscription and inhibit adoption?

Mr. ROSSTON. Yes. Increasing taxes on broadband to pay for—as I said earlier, every dollar you spend comes from someone else's pocket. So that would increase the price for other people, and they would possibly respond by reducing their subscriptions.

Mr. STEARNS. OK.

Ms. Moyer, do you think in your heart of hearts that the bill, as drafted right now, would lower a consumer's bill? I mean, would you put your money on it?

Ms. MOYER. My own money?

Mr. STEARNS. Your own money.

Ms. MOYER. I truly believe that, by expanding the contribution base, yes, it would.

Mr. STEARNS. So in your heart of hearts, you would put your own money on this then?

Ms. MOYER. I guess that is what I am saying.

Mr. STEARNS. OK. Well, you have some skin in the game, so I respect your opinion. Thank you.

Ms. MOYER. Thank you.

Mr. BOUCHER. Thank you very much, Mr. Stearns.

The gentlelady from California, Ms. Eshoo, is recognized for 5 minutes.

Ms. ESHOO. Thank you, Mr. Chairman.

And thank you to all of the witnesses.

I have made a point in other hearings and in my communications with the NTIA, the FCC, and RUS that high-speed should be a primary goal for broadband rollout. I think that this legislation sets the floor too low. It defines broadband as 1.5 megabits downstream without any upstream requirement, and it locks in this speed for 6 very long years. And, as I said in my opening statement, you know, I mean, everything has changed and continues to change so quickly. Six years is a very long time.

People in rural America deserve, I think, high-speed access, as well. And I don't think we should lowball them as part of the overall reform efforts. I think we need to keep in mind that we have no idea what will be happening in 6 years. Telecommunications develops so quickly that this speed might be considered a relic by then. So why lock this in for 6 years?

In the broadband bill that I had put forward, we set forth a 50 megabit down and 20 up requirement, which I believed would drive investment and spur adoption. But who knows? That might even be too slow. So I think we need to use the broadband map to determine which speeds are appropriate for a given market.

So my question to you, the panelists, is, how can we use the broadband map to help guide our policy, especially on determining the appropriate speed? Do we really need one speed for the whole country?

And I am also concerned about the bill essentially maintaining the status quo for the High-Cost Fund. Recipients of the fund are not required to provide broadband services, which I think is a huge mistake. I mean, I think that we are ignoring our future. I think we are ignoring the present, much less the future. So I think that there is a big hole in the bill in this area.

And so my second question is, shouldn't the bill require the FCC to utilize the new broadband map to determine if an area is already served by a provider that may not receive any, you know, fund support?

Is there any sense how much could be saved if we first determine which areas—and I think Mr. McSlarrow spoke to this, and maybe some others did, as well. Is there any sense how much could be saved if we first determined which areas are already served by a provider offering voice, video, and data today and not receiving any government support?

And, lastly, if there is anyone that would like to comment on Ms. Matsui's bill, which will use the Lifeline Program as a base for

broadband accessibility for the unserved and the underserved populations.

So those are my three questions, and whomever would like to start the ball rolling.

Good. AT&T is first.

Mr. LUBIN. To me, those are three very important——

Ms. ESHOO. Can you get closer to the microphone so we can hear you? Thanks.

Mr. LUBIN. Three very important questions. The first question about speed, and I want to link that question——

Ms. ESHOO. Can you be as concise as possible, since I asked three and I want to get as many answers in as possible? Thanks.

Mr. LUBIN. OK. The issue of speed is all about how much are we willing to pay into the fund; meaning, how big is the fund? The higher the speed, the more the size of the fund will be. So that is a tradeoff for the policymakers if you want it to end up being——

Ms. ESHOO. But what is AT&T's position in this, though?

Mr. LUBIN. AT&T's position with regard to speed, with regard to USF, is, if you take USF, then you have to meet whatever speed requirement is in the bill, and you are going to ultimately be a form of making a commitment to provide all comers with that speed. And so our concern with going—even 1.5 megabit is potentially too high when you start looking at what the size of the fund would be. So that is our concern with regard to the first question.

With regard to the second question on unserved areas in terms of the mapping, we think that is a very important issue to be addressed. And AT&T, April 18, 2008, made a filing teeing up this point, where we should focus on unserved areas, thus possibly being able to control the size of the fund. So having focused on unserved is a very important aspect.

But I would like to highlight to you, once you do that, in particular for the RLECs, if you start looking at the very high-cost areas, the presumption is you may reduce the size of the fund. I think Ms. Moyer hit right on the head, is that once you do that, you may, in fact, start to increase the size of the fund.

With regard to Lifeline, we think as we transition from this POTS world to a broadband world, we think a lifeline is going to be absolutely critical in a broadband world. Our bottom line with regard to Lifeline is we think the whole Lifeline plan——

Ms. ESHOO. How long do you think it is going to take to get us to what you are describing, though? Do you think we should set this down, the lowest numbers for 6 years, 6 long years? Do you think that is good policy for the country?

Mr. LUBIN. Again, it is a question back to how much are you willing to fund, how big will it cause the fund—I have already heard issues about what the concern of the growth of the fund will be. I think if you make it much greater than 1.5, that question is on the table.

If you want to suggest less than 6 years, I think that is a valid thing to say. Let's look at it shorter than 6 years. But listening to this conversation, clearly, the higher it is, the bigger the size of the fund. That is the linkage and the issue.

Mr. BOUCHER. Thank you very much, Ms. Eshoo and Mr. Lubin.

The gentleman from Texas, Mr. Barton, is recognized for 5 minutes.

Mr. BARTON. Thank you, Mr. Chairman.

I was watching the hearing in my office, so I heard everyone's testimony, and I heard your questions and Mr. Stearns's question. So I haven't been present, but I have been observant while I have been multitasking.

I brought my bill. I just got my Verizon bill. And for services I pay $26.53. For taxes—actually, it says "taxes, fees, and other Verizon charges," whatever that is, $10.49. So I am paying 40 percent of my basic phone service in Virginia in taxes, fees, and other Verizon charges.

It seems like—although I did find out that the universal service portion of this is fairly minimal because I don't make any long-distance charges. Although Virginia does charge me a Virginia Federal Universal Service Fund surcharge, Mr. Boucher, of 76 cents. And I hope you can do something about that.

If I wanted to ask a trick question, I would ask Mr. Davidson what a sensible minute is. Verizon charges me $2 a month for a sensible minute. I have no clue what a sensible minute is.

Mr. DAVIDSON. We will have to get back to you on that, Mr. Barton, on the sensible minute. But I doubt it was our idea.

Mr. BARTON. Yes.

My first question is a rhetorical question. Anybody on the panel can answer. When did we first pass universal service? When did it become a mandate that there be a universal service charge? Anybody know? I would assume in the 1930s. Does anybody on the dais know? And I don't——

Mr. BOUCHER. Would the gentleman yield for just a moment?

Mr. BARTON. Yes.

Mr. BOUCHER. Universal service has been inherent in the structure of the telephone network essentially since its inception. And it wasn't until the Telecom Act of 1996 that we made the universal service subsidies explicit.

Mr. BARTON. But when did we first start charging universal service——

Mr. BOUCHER. Well, that has been inherent in the structure of the flow of revenues essentially ever since we began——

Mr. BARTON. But it wasn't a Federal mandate——

Mr. BOUCHER. It was not a mandate. It was just done within the industry, where urban residents and users of long distance wound up paying somewhat more in order to keep telephone service affordable elsewhere.

Mr. BARTON. OK.

Well, my first question, I am going to ask this to the gentleman from Stanford, Dr. Rosston. Is broadband today the equivalent of basic telephone service in the 1930s?

Mr. ROSSTON. I think that is not an economics question that I would answer as an economist. It is probably much—if you look at the data, broadband is much more pervasively adopted today than telephone service was in the 1930s. Whether you are asking that as a values question, I can't answer that. But just, sort of, the data shows that broadband has been adopted much more rapidly than

telephone service was and it is much more pervasive than it was in the 1930s.

Mr. BARTON. Well, the reason I ask that is because one of the apparent premises of the Boucher-Terry draft is that broadband should be equivalent to basic phone service, that it is almost an entitlement and should be treated as such. And I am not quite ready to go there yet.

I think broadband is an improvement, I think it is an enhancement, I think it is a good thing to have. But if I choose to live in very rural America by choice, I like that lifestyle, I don't know that—one of the witnesses from one of the smaller phone companies basically said, "People that live in rural America expect to have the same services," la di da di da, "as people that live in urban America."

And I am not sure—I mean, I think you make a value decision, if you have a choice of where you live. If you choose that rural lifestyle, I don't know that you automatically are entitled to the enhancements that require more critical mass and a greater population density.

So that is one of the things I want to work with Mr. Boucher and Mr. Terry on, is this broadband mandate.

My time has expired. I am going to ask one question to Mr. McSlarrow. Does the cable industry currently pay a universal service charge?

Mr. MCSLARROW. Yes.

Mr. BARTON. You do. Do you support the concept in the Boucher-Terry draft that expands the base of who pays the tax?

Mr. MCSLARROW. Yes.

Mr. BARTON. You do. OK.

Thank you, Mr. Chairman.

That is not the answer I wanted, but thank you.

Mr. BOUCHER. It is the answer that I am glad he gave. Thank you very much, Mr. Barton.

The gentleman from Pennsylvania, Mr. Doyle, is recognized for 5 minutes.

Mr. DOYLE. Thank you, Mr. Chairman.

Mr. Rosston, in your testimony, you said you believe that subsidies should follow consumers, not companies, to increase competition and choice. Do you think, is a reverse auction the only way to accomplish that, or could a voucher work? And are there any other ways, as well? And what are some of the pros and cons of those approaches?

Mr. ROSSTON. So, what I said in the testimony is, if you had a voucher system that, in my view, would be low-income vouchers that were cost-adjusted—so a low-income household in a dense, urban area would get a smaller voucher because the company would be charging a lower price in that area, and a higher voucher in a rural area so that they could afford it in a rural area—you could do that. And the voucher could be income-tested and cost-tested, sort of like health-care vouchers might be adjusted for people's age and health conditions, that you would have a voucher for telephone service or broadband service.

And that could be done without an auction, and it would cause the consumers to have the ability to choose their provider. And the

providers would have to compete for the service. Whether they wanted 1.5-megabit service or 5-megabit or 10-megabit or portable service so that they could use it on their wireless phone as opposed to at their home, they would have this ability to have companies compete for their business.

Mr. DOYLE. Thank you.

Mr. McSlarrow, what do you think about those ideas?

Mr. MCSLARROW. I didn't hear the question.

Mr. DOYLE. What do you think about the idea of a voucher system or——

Mr. MCSLARROW. I mean, in economic terms, I agree with that. And I think any system where we can put more money in the hands of the consumers themselves and let them make the choices is probably a better system.

Mr. DOYLE. And I also want to give you the opportunity—I know that several of the testimonies from the phone companies talked about some of the concerns they had with your proposal. And I wanted to give you an opportunity to maybe address some of those concerns that were brought up about your proposal.

Mr. MCSLARROW. Thank you.

The first thing I would say is that what we are proposing is, in essence, a framework. There is no automatic reduction of high-cost support. What we are saying is that you apply two tests. One is a regulatory test; one is a market competition test. If it shows that you have that kind of competition, it still allows the incumbent who is receiving support to come forward and say, "Here are all the reasons why, if you took out support in a competitive area, my revenues can't cover my costs." So they still have an opportunity to make a showing for some level of support.

And Ms. Eshoo actually asked a question; I didn't get a chance to answer you. Our analysis is that there is about $2 billion that we would at least, under our proposal, take a look at. We are not saying $2 billion goes away. People have the opportunity to make those showings back and forth.

Mr. DOYLE. Very good.

That is all I have, Mr. Chairman. Thank you. I will yield back.

Mr. BOUCHER. Thank you very much, Mr. Doyle.

The gentleman from Nebraska, Mr. Terry, is recognized for 5 minutes.

Mr. TERRY. Thank you, Mr. Chairman.

And, Mr. Lubin, let's continue this exercise. Assume the cap is put in place. Will the fund go up or down?

Thank you for your answer.

And Cliff did a great job of, kind of, hitting on what the main issue is here. We understand that, with some of these reforms, that the costs will have additional pressures. The pressures from those items that were brought up, other than ICC, which I think is a different issue than what this base bill addresses today, would make the fund increase.

The reason why our rural friends have had a difficult time embracing this bill is because of the cap. And I think that is an important point to make here, is with the cap, that keeps it status quo, albeit with an FCC traditional inflation rate.

So, with the cap, do you think that that is an adequate measure to hold down the explosive costs of high-cost USF?

Mr. LUBIN. With the way in which this bill structures the cap and the way in which you just removed three of the items, I would say yes.

Mr. TERRY. OK.

Mr. LUBIN. I would also highlight that how you handled the wireless issue, with the competitive bidding, there you have the opportunity that the aggregate dollars would come down.

Mr. TERRY. And that was my next question. Thank you. You just eliminated that for me. I appreciate that.

But, yes, there are actually cost-cutting measures in here. For example, limiting new entrants, especially on the wireless side. And we appreciate Verizon and the others helping participate in brokering that deal. Limiting new entrants, going to actual costs. Is that something that would relieve pressure on—the upward pressures on the fund?

Mr. LUBIN. That remains to be seen.

Mr. TERRY. OK.

The gentleman from Stanford, Doctor—what was your last name again?

Mr. ROSSTON. Rosston.

Mr. TERRY. Rosston. Economist. Based on your experience as an economist, let me throw this scenario out. University of Nebraska beats Kansas State. We go to the Holiday Bowl and play Stanford. Who wins?

Mr. ROSSTON. I will have to get back to you on that.

Mr. TERRY. OK. Good answer.

But getting to a more serious question, you brought up the distortion in the pool. And that is that, as the pool of payers grows smaller—and we have heard testimony here— since those that pay the universal service fee into the system, they just get billed every, what, 6 months or something by USAC. And now it could go as high as 14 to 15 percent. I mean, that is something that was unfathomable a year or so ago.

So, broadening the pool of payers is one of the founding principles of this bill. So at least that principle you think economically is sound?

Mr. ROSSTON. Yes, I think broadening the base of the tax will help to reduce distortions from the tax.

Mr. TERRY. And the distortions here have been, I think, well set out by the ranking member, former Chairman Barton, when he talks about the impact on his bill. Although the USF impact is hidden within the charges, and it is not explicit. But the fact of the matter is, he is one of those left standing paying, and if you broaden the base, his bill could actually go down?

Mr. ROSSTON. Well, I think that depends on how many bills he has and——

Mr. TERRY. And also assuming the cap is in place.

Mr. ROSSTON. Well, the cap is—I think it is—it could be—it is a question of how effective the cap is at reining in spending, as well, because there are provisions about whether the cap would be effective, I think, about it adjusts for working loops as well as infla-

tion. I think those things could be tightened down a little bit, as well.

Mr. TERRY. Well, we can look at that. I am going to interrupt because I only have a few seconds left.

And, Ms. Moyer, one of the items that I think will help control the costs is having professional, skilled audits done. Do you support that? And give us examples of how the audit process works today.

Ms. MOYER. Yes, we fully support that.

Today's audit procedure, especially at the FCC's OIG office, the most recent three rounds of audits have unfortunately been performed by auditors who don't know much about telecom bookkeeping and finances and, I think, led to some erroneous results, many of which USAC has refuted since then.

But to actually do something that is based on FCC methodology and with some trained auditors would be welcomed.

Mr. BOUCHER. Thank you very much, Mr. Terry.

The gentlelady from California, Ms. Matsui, is recognized for 5 minutes.

Ms. MATSUI. Thank you, Mr. Chairman.

As I mentioned before in my opening statement, there have been several recent reports that strongly suggest that adoption rates are largely associated with income. I would like to highlight one study that particularly affects my home State of California.

According to the Public Policy Institute of California, only 58 percent of Californians earning under $40,000 a year subscribe to broadband at home, but, in contrast, 97 percent of those earning over $80,000 or more a year subscribe.

I would like to ask a question of Mr. Rosston, the Californian there. It is my understanding that you have conducted extensive research on the USF Lifeline/Link-Up program. As you know, the price of broadband is not cheap these days, usually ranging from $40 to $60 a month. In your studies, is there strong evidence to suggest that the price of broadband is a determining subscribership factor of many low-income Americans in urban and rural areas?

Mr. ROSSTON. So, my research is focused on Lifeline and Link-Up for telephone service and not necessarily for broadband, but it would be sacrilegious, as an economist, not to say that price matters.

For low-income households, I think we should study this and make sure that any program we have we can figure out, what is the impact of price on low-income households? The evidence, in our research, is that—there are two programs, Lifeline and Link-Up. In our view, we found in our research—we didn't go into this thinking about it, but that Link-Up turned out to be much more effective because of the high cost for telephone service just paying the connection fee. For broadband service, you need to not only pay the connection fee, but you also need to have a computer and knowledge of how it might work and how it might benefit you.

So, Link-Up targeting those who are not already online is probably a very effective way of doing this.

Ms. MATSUI. So you believe that if you had a program similar to the Link-Up program, that if it was created for the universal broadband, that it would be an effective vehicle to expand increased broadband adoption rates?

Mr. ROSSTON. Yes, I think the Lifeline and Link-Up program would increase broadband adoption rates.

Ms. MATSUI. OK. And your analysis of the current Lifeline/Link-Up program, would be it accurate to assume that any expansion of the program for broadband adoption would be just as beneficial for rural consumers as it would be for urban consumers?

Mr. ROSSTON. Yes, I think so. I think that poor people live both in urban and rural areas, and so Lifeline and Link-Up would be beneficial in both areas.

Ms. MATSUI. OK. Thank you.

I have a question for Ms. Moyer and Mr. Rhoda.

Ms. Moyer, I would like to begin with you. It is well-noted that one of the barriers to further broadband deployment in rural areas is getting more households to subscribe to broadband.

In your view, would a program for broadband adoption similar to the current Lifeline Program help increase adoption rates in the communities in which you serve and other rural areas across the country? And would it help further the goal of broadband deployment in current unserved rural areas?

Ms. MOYER. Yes, I do agree. And I believe that your legislation would spur that adoption, as well as education.

Ms. MATSUI. OK. Thank you.

And, Mr. Rhoda, could you briefly address the same question?

Mr. RHODA. We agree, as well.

As far back as 2006, we talked to the FCC about adoption programs. We have been in recently to do the same. And I think they need to cover the cost of the device, the laptop, the computer. I think that they need to cover education. Some people just clearly don't understand the benefits that broadband will bring to them. And then they also, finally, need to cover the cost for those that can't handle the monthly service in some respect.

So we are fully supportive of your efforts.

Ms. MATSUI. OK. Thank you.

And I have a question for Mr. Baum. Deployment of broadband has reached 96 percent, but subscribership rates have lagged far behind, in both urban and rural areas.

Do you believe Lifeline for broadband would improve subscribership rates? And at what price point do you believe or do you think would be reasonably affordable?

Mr. BAUM. First of all, the NARUC board of directors passed today a resolution supporting your Lifeline bill.

Ms. MATSUI. Oh, thank you.

Mr. BAUM. And we think it is difficult to put the benchmark out there, but I would take a wild guess, would be $25, $20, something in that neighborhood.

Ms. MATSUI. $25, $20.

Mr. BAUM. But I would probably defer to my colleagues in the industry that actually run the models and do this kind of thing.

Ms. MATSUI. Does somebody else have a comment on that?

Mr. BAUM. But, yes.

Ms. MATSUI. OK. Thank you.

I was actually thinking maybe in the $30 range or so, so it is probably quite close to what you are thinking. And so that really sounds like maybe a $10 to $15 per month subsidy, which is in line

with the reimbursement under the current Lifeline Program. Would you consider that to be about right?

Mr. BAUM. If we had broadband as a supported service, the benchmark for that service would be in the $30, heading towards $40 in the future, because that simply is the basic cost out there for that 1.5-megabit service is in that range.

Ms. MATSUI. OK.

Thank you very much, and I yield back my time.

Mr. BOUCHER. Thank you very much, Ms. Matsui.

The gentlelady from Tennessee, Mrs. Blackburn, is recognized for 5 minutes.

Mrs. BLACKBURN. Thank you, Mr. Chairman.

And I thank you all for your patience and your indulgence. I know you have been here for quite a while.

I got just a couple of questions that I want to ask. And let me start, Mr. Davidson, with you. And let's just go down, if you all have something to add on this.

If you could change one part of this bill, if you think we are getting it wrong in one area, if you wanted to change one section of this, what would you change and why?

And quickly, we will start with you, sir.

Mr. DAVIDSON. Sure. I think probably the first thing that we would look at is—and this is actually a suggestion that is in the bill, but it is directed in the bill, and that would be going to the numbers contribution formulation. I think that is the most efficient way in the modern world of the various means——

Mrs. BLACKBURN. OK, so let me interrupt you right there. The contribution formulation, just to give some specifics on that, to define it.

Mr. DAVIDSON. Sure. So today, as I mentioned in my testimony——

Mrs. BLACKBURN. No, I mean, in the language. You are just saying——

Mr. DAVIDSON. Oh, well, it would just specify in the language that the FCC should follow a numbers-based approach for contributions.

Mrs. BLACKBURN. Great.

Mr. Greer.

Mr. GREER. We have concerns with the cap. But we look forward to working with the FCC on the national broadband plan when it comes out next year.

Mrs. BLACKBURN. OK, great.

Mr. RHODA. From Windstream's perspective, it would be driving efficient costs across the board. Some of the mechanisms in today's environment don't necessarily force carriers to be efficient and yet still get reimbursement. There is a number of measurements in this bill that do drive efficiency, but it is not across the board.

Mrs. BLACKBURN. Thank you.

Mr. LUBIN. I would highlight the issue of speed. I am concerned about the level of speed, not that it is too high—I am sorry, that it potentially is too high. And the issue of concern is if you can—now, I am focused on rural area, I am focused on if there is an alternative technology that can get it out there in a cost effective way. And that is a way to control the size of the aggregate fund.

Mrs. BLACKBURN. Excellent.

Ms. Moyer.

Ms. MOYER. The rural ILECs have concerns with the cap language.

Mrs. BLACKBURN. OK.

Mr. BAUM. Well, NARUC has concerns about the preemption language. But, on a personal basis, I think the speed needs to be realistic as to what we really need in the economy.

And we have to also acknowledge that there are a lot of rural constituencies that produce the food and fiber for the country that need access to this kind of broadband technology. And it is not a choice for them to live there; it is how we feed ourselves. And their hospitals and schools have to have that same access to broadband.

Mr. MCSLARROW. Since I have already talked about my proposal and Peter talked about numbers, I am going to cheat and add a third, which is ensuring that if we are going to have support for broadband, that it be restricted to truly unserved America.

Mr. GRAHAM. Thank you for your kind comments earlier. I appreciate that.

RCA would change the reverse auction provision. It is simply not a silver bullet for USF reform. Reverse auctions encourage a race to the bottom. They do not guarantee a reduction in cost. And they discourage new entrants.

However, if we move forward with reverse auctions, they absolutely should apply to everyone participating in the USF fund and not only wireless providers. If wireless providers are subject to it as part of a greenfield build, surely wireline providers who have depreciated plant in the ground over a number of years could compete as well.

Dr. RHEUBAN. For purposes of telemedicine, we are very supportive of the bill in its current status.

The one thing we might add is to ensure upstream bandwidth, as well, because for telemedicine we are trying to get feedback from the patient or from the hospital. So it should be bidirectional.

Mr. ROSSTON. So I would change the whole system to be vouchers to low-income households. But, given that that is not going to change in this bill, I would say extend auctions, set a time limit for the FCC, and put them in in the next 6 to 12 months and go ahead. They are not a silver bullet, but they are better than the current system.

Mrs. BLACKBURN. Thank you very much.

And I have 23 seconds left. Mr. McSlarrow, I will come back to you and not take the committee's time right now. But I think we need to look at how quickly we are moving to an IP world and VoIP as a primary technology. And as we looked at the reauthorization of the 1996 Telecom Act, one of the things we heard from all of you was, "Well, the bill is arcane, the bill has outlived its usefulness, technology changes so fast." And I think that one of the things that we need to look at is what we can do to ensure that the universal service mechanisms work in a changing environment, in a VoIP environment, and making certain that this bill is going to work in an IP world.

And I know I am out of time, but I would appreciate your response to that question in writing as we move forward or at a later date.

And I yield back, Mr. Chairman. Thank you.

Mr. BOUCHER. Thank you very much, Mrs. Blackburn.

The gentlelady from the Virgin Islands, Mrs. Christensen, is recognized for 5 minutes.

Mrs. CHRISTENSEN. Thank you, Mr. Chairman.

I will direct my first question, not surprisingly, to Dr. Rheuban. But I wanted to thank you for some of the recommendations that you have made, realizing how much we are relying on telemedicine and health-care reform and to improve outcomes and reduce costs. So I appreciate the recommendations that you made.

The USF Reform Act requires that universal fund recipients offer high-speed broadband services with a download rate of at least 1.5 megabytes per second. In your testimony, you spoke to different broadband needs for different services. And I wanted to know if the speed that we are recommending of at least 1.5 megabytes per second is adequate for what is required to support all of the services.

Dr. RHEUBAN. I think for HD and surgical mentoring it is not sufficient. I think it is sufficient for a clinic operation or, certainly, for the home. You know, home telehealth wouldn't require quite as much bandwidth as some of the more sophisticated applications.

And if you have multiple users providing health-care services in a hospital, you can imagine that the demand for the bandwidth would be significantly greater. So, again, 1.54 is good for some applications but not for others.

Mrs. CHRISTENSEN. Thank you.

I guess I would ask this question to Mr. Baum and Mr. Rosston, but if anyone else wanted to jump in, it would be fine.

Section 104 on eligible recipients of universal service support exempts existing recipients of the USF funds, primarily rural telecos, from the requirement to deploy and provide high-speed broadband service for 5 years. The FCC may also grant a 3-year waiver of this provision if the provider demonstrates that it is not technically feasible or would materially impair its ability to continue to provide local exchange service. That waiver is renewable for every 3 years.

Ubiquitous broadband deployment is a primary goal of the administration and this Congress, this committee. Currently, the FCC is working on a new national broadband plan. Even the discussion draft requires new providers who are eligible to receive USF support to deploy high-speed broadband service and provide it.

So why should we exempt existing recipients of USF? Do you agree with that exemption or waiver?

Mr. BAUM. What that refers to is the fact that some of these areas are so remote and so expensive to serve that we really probably need to have a satellite option there. There will be some really remote pockets of population and even single-family dwellings that simply are too far out in the rural areas of America to be receiving broadband by a fixed basis. So either their service is either some kind of wireless broadband or, in this instance, it would be satellite.

We simply can't get everywhere in the country. We might get to 98 percent, we might get to 96 percent somewhere. And, also, remember that we never got phone service beyond about 95 percent of the population. Some people just don't want to hook up, and some people are just too far out, and it would be too expensive to serve them. And they will have to do a satellite.

Mrs. CHRISTENSEN. Mr. Rosston, did you want to add anything?

Mr. ROSSTON. No. Just, the satellite option is an important safety valve, in that it covers pretty much most everywhere and especially the high-cost areas. That would be a safety valve in this.

Mrs. CHRISTENSEN. Well, let me ask you, Mr. Rosston. One of your main points is that you suggested subsidies should go to consumers, not companies, to increase competition and choice.

Could you elaborate on that? It sounds very attractive. It sounds like it may be a major upheaval, though. Could you elaborate on that recommendation?

Mr. ROSSTON. Sure. It is generally a way of giving consumers choice in what they want. If you decide that the best service for your house is a wireless service because you work outside a lot of the time and need to be accessible, that you would have the chance to use the subsidy to provide you service that gets you outside.

Or if you move around, if you are a plumber that does jobs and you need to look up stuff and you don't need 20 megabits a second to watch videos but you need to look up parts for your job, you would be able to do that and use the different kinds of services that are tailored to what you want to do.

So I think that this would then give consumers the choice to pick the service that best suits their needs.

Mrs. CHRISTENSEN. Thank you.

Mr. Davidson, you, in your testimony, said the problem is not spending too little but spending it in the wrong places. How would you redistribute the funds? And does the bill adequately address that change?

Mr. DAVIDSON. Thank you for the question.

Yes, I think that is right. I mean, the question is of finding out right now where the true needs of consumers are. And I would also go back and focus the panel on the needs of the consumer, too, which I think has been a great part of this hearing. We have spent a lot of time talking about that.

So the mechanisms that the Boucher-Terry bill use to figure out where the services are needed and where they aren't I think are very important. So, the competitive bidding portion. Again, I mentioned the numbers formulation before. And——

Mrs. CHRISTENSEN. So you think we are adequately addressing that issue in the bill?

Mr. DAVIDSON. I think they are, yes. I think the bill has many provisions in it that are trying to prioritize where the scarce resources should be directed. So there are many aspects of the bill that are directed towards doing that.

And there have been some other ideas raised on the panel here, as well. Mr. McSlarrow's idea is interesting, and others as well. So I think those should be examined to make sure that we are prioritizing the funds.

Mrs. CHRISTENSEN. Thank you.

Thank you, Mr. Chairman.

Mr. BOUCHER. Thank you very much, Mrs. Christensen.

The gentleman from Oregon, Mr. Walden, is recognized for 5 minutes.

Mr. WALDEN. Thank you very much, Mr. Chairman.

I want to thank all the witnesses for their testimony today on this very important piece of legislation.

I want to go to Mr. Baum. In Oregon, where certain nationwide service providers are shedding their remaining rural lines, can you outline for us how the parent trap may impact other carriers' decisions to step in to provide phone service to the rural constituents I have?

Mr. BAUM. Well, the reality is that the Regional Bell Operating Companies have been unable to do an adequate job of deploying broadband in their high-cost rural areas. That is because they face competition in their urban areas, and their business model just simply doesn't allow them to do that.

The RLECs, rural companies, in contrast, do receive better subsidies from the Universal Service Fund, which allows them to deploy broadband. So their broadband is out there about 92 percent, and, depending on the company, the RBOCs are anywhere from the low 70s to the high 80s.

They just don't have a business model that works. So the parent trap would allow some of the midsized and small companies to come into those areas and to refurbish them and get the subsidy that they would receive as RLECs to refurbish some of those areas and deploy broadband.

It would be important to have that dealt with in some way because, really, the failure to deploy broadband in rural high-cost areas is largely a Regional Bell Operating Company's issue and affects about 50 percent of the country. And we simply have to address that issue. And that is why it is important that we do something in that regard about the parent trap.

It is also important that we focus some of this money, if there is some, on the unserved areas in those RBOC areas. And that could be done by auction; it could be done by requests for proposal. But we need to have infrastructure built out there so that those communities can have the same benefits that the communities have that are served by the rural local exchange carriers.

Mr. WALDEN. Let me switch gears, since we are on the broadband build-out. And when the stimulus bill was debated before this committee, there was a significant amount of money put forward to engage in broadband build-out. And we had rather extensive discussions here about the money getting out there before the mapping was completed and the debate over underserved versus unserved.

Now I understand they are compressing the second and third wave of funding. And I just wonder, from your position at NARUC and as a commissioner, what you are seeing in terms of where this money is going. Because it seems to me that, with the taxpayer dollars involved or the USF dollars involved, it should go into areas that have no service to begin with if we are going to knit this country together in a broadband world.

Mr. BAUM. One of the problems of the current broadband stimulus package is some of the bigger companies have declined to apply because of some issues over Net neutrality and they are not certain about what those strings mean to the deployment of dollars. So half of the country's areas, they don't have the major ILEC in that area even applying in the high-cost areas.

Now, there are some other people that are applying, kind of, in a little bit of an over-built fashion. Some of them are in other areas. You know, we have a—for instance, in Oregon, Bend Cable is also applying to roll out broadband in an area that is served by Qwest. And they are trying to go outside of town and serve unserved areas, but unfortunately when you try to serve any area, you are going to serve the populated area as well. And so it is difficult to truly target an unserved area.

So there will be some improvements in the broadband stimulus. It will deploy some things in some unserved areas. But we still have major players out there who aren't in the game.

Mr. WALDEN. And, Mr. McSlarrow's, Kyle's comment, his suggestion about a different way to look at the whole model. And, Kyle, I believe you indicated that it be in an area that is 75 percent served? Would then be in a competitive——

Mr. MCSLARROW. Yes, we are proposing, essentially, two tests. One would be in a rural study area, say, where there is significant competition, which we are defining as 75 percent or more of the households can receive a competitive unsubsidized service, or a situation where the State has actually deregulated prices, on the theory that competition is present.

Mr. WALDEN. So I guess my question would be—and, again, I have a district that is 75,000 square miles. So you could have the urban area, to the extent we have them, in a very large geographic area and probably serve 75 percent of the population.

My concern is, what happens to that other 25 percent that is out in the area? And so, how do you define that circle, if you will, in which you score the 75 percent penetration?

Mr. MCSLARROW. It is a good question, I think. And, actually, this goes to one of the proposals in the bill. I think moving to wireline centers actually helps. I think the smaller you can make a certain area, the less you are going to run into that problem.

But, remember, under our proposal, you still have the ability, if, in fact, there is some other area that isn't being covered, to make a showing that USF high-cost port is still appropriate——

Mr. WALDEN. So if you have an area that is 100 percent and 75 percent is the area that is served and would meet your test, do you have that ability, under your proposal, to go after that remaining 25 percent in that area and be subsidized to reach it?

Mr. MCSLARROW. Yes. The incumbent can come make a showing that there is 25 percent that is not covered by competition and that there is still a need for high-cost support.

Mr. WALDEN. All right. My time has expired, but I appreciate your generosity with the time.

And, again, thank you to the panelists.

Mr. BOUCHER. Thank you very much, Mr. Walden.

The gentleman from Michigan, Mr. Stupak, is recognized for 7 minutes.

Mr. STUPAK. Thank you, Mr. Chairman.

And thank you for our witnesses for being here.

Mr. Baum, let me ask you this question, if I may. A little different twist here. Do you believe that, as we reform USF, that we should consider the telecommunication needs of public safety? And, if so, how would you go about doing that?

Mr. BAUM. Well, you are aware that public safety is one of the applications that is eligible under the broadband stimulus.

Mr. STUPAK. On the stimulus, right.

Mr. BAUM. Yes. And there is also those 700-megahertz applications that some of the local jurisdictions are applying for waivers to get from the public safety trust. So that is moving ahead on that front. So there is, kind of, some things moving ahead.

But right now, for instance, in Oregon, we have a $440 million bonded project to build out a microwave public safety network. And those are our local State efforts. So, nationally, there is some funding available through the Department of Homeland Security, there is some stimulus money there. It is, obviously, not going to do the trick.

But we judge our applications for stimulus based on how many of these proposals they serve, whether they provide public safety application in their proposal, telehealth, distance learning. All of those things are part of the application process that we are encouraging companies to make under the broadband stimulus, to make sure they satisfy those criteria.

Mr. STUPAK. Right. But what about under USF? Should we use law enforcement as one of them? Especially, when we talk about interoperability, I mean, rural areas just cannot keep up with the high cost of technology.

Mr. BAUM. In my perfect world, we would focus on those unserved areas, and anchor institutions would include law enforcement, schools, libraries, medical facilities. And from there you could build it out and spider-web it out to the residences. But you need to have that for the public safety network, as well.

Mr. STUPAK. Correct. OK.

Mr. Graham, do you want to jump in on that?

Mr. GRAHAM. Yes, thank you.

The easiest way to deploy broadband for public service, at least within the State of Mississippi, is to make broadband a supported service immediately. We are in the process of preplanning some applications with the Mississippi Highway Patrol which would allow officers to have an E-ticket program with a wireless connection. It would also allow them to input accident data into their laptop——

Mr. STUPAK. Sure, but that is basically for State employees, right? How do you get your local police chiefs, the sheriff's departments in the same system so it is interoperable so you do have a seamless flow of communication? It seems like we are going to have a dedication of funds that is somewhere between $20 billion and $40 billion, and every time we try to do a trust fund so law enforcement will have the money we never seem to get anywhere.

Mr. GRAHAM. In one of our metro counties, we have already launched this with the sheriff's department, a similar program. They have broadband connectivity from their cars. Applications are easy to envision where they will have realtime video late at night

on a county road. And you can easily extend that into paramedics and emergency responders like that.

Mr. STUPAK. Sure. The county may have it, but what about the municipalities within there? Are they part of that same system?

Mr. GRAHAM. They are not part of that same system yet. They could be part of that system.

Mr. STUPAK. Could be, would be, want to be. Lack of money, right?

Mr. GRAHAM. As long as the services—as long as the cloud is there, the broadband cloud is there, they can access it.

Mr. STUPAK. Let me ask you this, then, Mr. Graham. Based on your testimony, since 2000, USF has provided, like, $26 billion in subsidies, landline, and 4,000 for wireless. The FCC capped the wireless fund to control costs, but we still have an increased contribution rate somewhere around—it went from about 10 percent to 14 percent.

So we have increased the contribution that consumers are paying, yet we capped the wireless. It seems like we are getting less for more. So Joe Barton, when we comes in with his telephone bill, he is paying more, but yet we have less than we did 2 years later for wireless communication.

Isn't that really the way we are going?

Mr. GRAHAM. We completely agree with that. We are going in the wrong direction, capping wireless. Wireless may have seen growth, but it is because we have gone from zero funding to the funding we receive today. We continue to subsidize 1876 technology at cost level. Whatever it costs them to build the network, they get the money.

Mr. STUPAK. OK. The draft bill contemplates capping USF support for high-cost areas. And, in your testimony, you assert that the bill would allow certain high-cost carriers to receive support indefinitely. Do we run the risk of freezing investment, much like what has occurred with rural wireless?

Mr. GRAHAM. We do run that risk and, in some areas, curtail investment and, in other areas, if the cap continues to run indefinitely——

Mr. STUPAK. What would you propose for changes, then, in the current legislation?

Mr. GRAHAM. Well, we would target the support to areas where it is absolutely necessary. We think a thorough review by the expert agency must be undertaken. That has not been done. No one has ever sat down and figured out exactly where the support really and truly needs to go.

Mr. STUPAK. OK.

Mr. Lubin, let me ask you, because, in your testimony, you also urge a bit of caution about how we utilize a cap to contain costs. Does AT&T believe a cap may run the risk of freezing investment in rural areas?

Mr. LUBIN. Yes, there is that risk.

Mr. STUPAK. So, same thing, identifying, mapping?

Mr. LUBIN. For us, the bottom line is, if you have that cap, you have potentially constrained how much investment in the high-cost areas. And that is a dilemma. That links back into a lot of the different things we have discussed this morning.

Mr. STUPAK. OK.

Mr. McSlarrow, let me ask you this one. I am looking at your map here that you submitted. How did you identify these areas, excess high-cost support funding? And what was the data for your economic analysis on this to come up with this map?

Mr. MCSLARROW. The data that we use is the data that is produced by the rural study areas within the High-Cost Program itself. So what we essentially did was we took all of the rural study areas and looked at the support that was going to each of them. Then we overlaid that on top of what we knew about where unsubsidized competition was.

Mr. STUPAK. All right. So you get that 75 percent area, then you get the uncompensated competition or unregulated——

Mr. MCSLARROW. Yes. And I should just point out: In our proposal, we actually made what we believe is the most conservative case. We are not even taking into account wireless. We are just saying if there is another unsubsidized wireline competitor, that that is the case for taking a fresh look.

Mr. STUPAK. OK.

Let me ask you this. It is my understanding you are concerned with broadband network connections being assessed for contribution into the USF. How would you propose to ensure that contribution mechanisms are there long-term? Again, we capped off wireless, but yet we have spent—it has received more money. How do we do it long-term——

Mr. MCSLARROW. In terms of the contribution side?

Mr. STUPAK. Yes.

Mr. MCSLARROW. Well, like a lot of folks, we support a numbers approach. But that is just a proxy for saying a connection.

Mr. STUPAK. Correct.

Mr. MCSLARROW. Our concern about broadband revenues is simply this. All the other services are highly penetrated. They are at the 90-plus level. Broadband, as we have all been talking about, still has some adoption challenges. So we are a little leery of putting another assessment or fee on the cost of broadband when we are actually over here trying to drive more adoptions.

But a numbers approach or some kind of connectivity approach that is true for everybody across the board, we think that is the way to go. And that does broaden the base.

Mr. STUPAK. But if you use a numbers approach, aren't you still with the rural areas with small population base still never being built with broadband? I mean, if you look at your map, heck, my district is not even covered, hardly.

Mr. MCSLARROW. If you take phone numbers—and I think there are about 650 million phone numbers in existence. If you had something that is something less than a dollar month, right there you get over $7 billion for the entire Universal Service Fund.

Mr. STUPAK. Thank you.

Thank you, Mr. Chairman.

Mr. BOUCHER. Thank you very much, Mr. Stupak.

The gentleman from Indiana, Mr. Buyer, is recognized for 5 minutes.

Mr. BUYER. Thank you.

Mr. McSlarrow, I wanted to give you an opportunity to clarify. When you were answering questions of Mr. Barton relative to the expansion, I got this sense—did you really mean that we should be taxing broadband by implication here? I just want you to clarify what you meant by, yes, more people should be paying in.

Mr. MCSLARROW. Well, I may have misunderstood his question, because, as I just said to Mr. Stupak, we are against taxing broadband. I thought what he asked was whether or not we were for broadening the base. And we are, through a numbers assessment.

Mr. BUYER. OK. All right.

Mr. MCSLARROW. So thank you, if I misunderstood that.

Mr. BUYER. All right. Thank you.

Mr. Davidson, the cap on the High-Cost Fund in the Boucher-Terry bill, due to exceptions, is being referred to as a soft cap. If we don't put a firm cap on the High-Cost Fund, what would be the impact on consumers?

Mr. DAVIDSON. Well, as I said in my testimony, you know, with the contribution factor going to be reaching 14 percent next year and no end in sight unless we fix the system, I think everyone agrees that there needs to be some kind of cap on the process here or it will simply become unsustainable.

So what does "unsustainable" mean? Unsustainable means that people like Mr. Barton and other folks who are looking at the bottom of their telephone bill are going to say, "I am not going to pay 25 percent of my bill to subsidize this system anymore." So it has to be fixed.

I think what Representatives Boucher and Terry have done have introduced a cap concept. And, as you hear throughout this panel, there are a lot of different positions on how exactly to do that. I would just urge this committee and all of those that are going to be participating in the legislative process to preserve the discipline, as much discipline as possible, in keeping that cap as concrete as it can be, as it moves through the process. Because that is what is going to keep the system sustainable going into the future.

So I think there has been an honest attempt to create a cap. And talking with the various parties, they have reached the cap they have. I just urge everyone to keep it as tight as possible.

Mr. BUYER. In response to Mrs. Blackburn, Mr. Davidson, you said you are an advocate for universal service fees to be based on a numbers-based system versus revenue. That is correct?

Mr. DAVIDSON. Yes.

Mr. BUYER. All right. I would like to get a sense, and go right down the line, of whom would advocate a numbers-based system versus a revenue-based system?

So, Mr. Greer.

Mr. GREER. We would advocate a revenues-based system.

Mr. BUYER. Revenue-based.

Mr. RHODA. Connections-based.

Mr. BUYER. Connections-based?

Mr. RHODA. Connections, numbers, yes.

Mr. BUYER. Numbers. All right.

Mr. LUBIN. Telephone numbers.

Ms. MOYER. Connections.

Mr. BAUM. NARUC doesn't have a position, but I would support numbers and connections.

Mr. BUYER. Great.

Mr. MCSLARROW. Telephone numbers.

Mr. GRAHAM. RCA doesn't have a position on that yet, but some hybrid numbers-and-contributions-based.

Dr. RHEUBAN. ATA doesn't have a position on that.

Mr. BUYER. OK.

Mr. ROSSTON. I haven't studied it much, but it seems to me that numbers or connections would be a better way than revenues.

Mr. BUYER. And if we go to numbers, it is better with predictability, would you not agree?

Mr. Rosston, since the goal of the High-Cost Fund is to make service more affordable for consumers in high-cost areas, shouldn't the focus be on consumers and not necessarily the carriers? Meaning, shouldn't the subsidy follow the consumer so that, if the carrier loses a subscriber, they also lose the subsidy?

Mr. ROSSTON. Absolutely.

Mr. BUYER. Very good.

I yield back.

Mr. BOUCHER. Thank you very much. We appreciate those questions.

The gentleman from Vermont, Mr. Welch.

Mr. WELCH. Thank you very much, Mr. Chairman. I appreciate your work here.

I want to ask Commissioner Baum, if I could, the discussion draft allows eligible providers basically to avoid the requirement of offering broadband service where it is deemed too costly for them to do that. And I gather that is about three times the national average.

Do you see this as a clause, almost an escape clause, that could let providers that still receive support not make significant expansions where they are needed?

Mr. BAUM. I am not sure about the impact of that 2.75 ratio.

First of all, before I say that, I want to thank you for speaking at NARUC yesterday. We appreciate you coming out.

Now, back to your question——

Mr. WELCH. Thank you.

Mr. BAUM. At some point, we have to have some way by which we are going to determine how far we are going to penetrate into those high-cost rural areas, particularly the unserved portions. And I am not sure if the 2.75 ratio is accurate. We may be able to go further than that.

But, at some point, we are probably not going to be able to afford to provide high-speed broadband to every person or residence in America regardless of where they are located.

Mr. WELCH. But I am, kind of, wondering if we have it structured right. Because, obviously, there may be a point where the cost is beyond what is affordable. But, on the other hand, there are a lot of rural areas where we need that service, Vermont among them.

And the specific question I have is whether you are going to have, under the draft language, some possibility of companies on

the one hand receiving support but on the other hand actually not doing build-out in some of these areas.

Mr. BAUM. I just can't tell you based on—I wasn't briefed on how that actually worked or was I part of that process. But there has to be some way by which we can figure out how far we are going to go, and the percentage should be in the high 90s. And I am just not sure, between 95 and 100 percent, how far we can go on an affordability basis.

Mr. WELCH. OK. Thank you.

Mr. Rosston, how about you? I know you have studied the economics of this pretty extensively.

Mr. ROSSTON. So, my view is, if you went to a system of vouchers to consumers, you would not have to worry about this because they would be cost-based and you would get them able to pay in other areas. I think it is important to also consider the satellite alternatives in very, very high-cost areas.

Mr. WELCH. Right. And what is the cost of a satellite connection?

Mr. ROSSTON. My impression, I haven't subscribed, but I thought it was between $70 and $90 a month for broadband access.

Mr. WELCH. In contrast, if there was a buildout, what would be the average costs there?

Mr. ROSSTON. If you think that people sort of pay in the $40 to $50 in urban areas, and you are talking three times for this bill, that would be getting it well more than this $70 to $90 for a retail subscription to satellite.

Mr. WELLER. Thank you. Mr. McSlarrow, your view on this? I am interested in obviously a rural buildout, representing a rural State. And the point has been made by you as well by folks on this table that that buildout is really a lifeline for the economic activity of those rural residents and they are there for a variety of reasons.

I don't think it is quite an individual choice to be a hermit. I come from a town of 1,800 people. That is my base. We like broadband.

Go ahead, Mr. McSlarrow.

Mr. MCSLARROW. I think our view is that there clearly are areas that deserve high cost targeted support, and it is about taking scarce dollars and putting them where they are needed. I will say at least in our own industry's experience, whether it is broadband or phone, we don't actually differentiate in terms of the pricing in an urban area to a rural area.

Mr. WELLER. You do not. Right. And you support maintaining that nondiscrimination in pricing.

Mr. MCSLARROW. We tend to just roll out across our entire national footprint.

Mr. WELLER. Thank you.

Mr. DAVIDSON. Congressman, could I expand on that for a minute? I think one of the things to recognize as well is the expense in the areas you represent aren't necessarily last mile expenses as well. We have a proposal that deals with the so-called middle mile, which is terms of the amount of transport that broadband needs to go over long areas to get to remote areas and then serve those remote areas. So I would be happy to explain and come talk to you a little more about what our proposal is.

But basically we think if you provide some support to build those middle mile facilities and then that subsidy goes to the end broadband provider, it doesn't go to the middle mile facility, but it makes it possible for that middle mile provider to build the transport, that is enough of an incentive perhaps to tip the balances in terms of bringing broadband to more remote areas. So we would encourage you to look at that proposal as well.

Mr. WELLER. I look forward to seeing that. While you are here, Verizon, I know it has left or you are in the process of leaving 17 rural States with your wire land network. Vermont, of course, is one where you did recently leave. And what I understand is you are also going to discontinue providing what is relatively high cost support for the wireless network.

I am wondering whether Verizon is willing to commit to serve every customer and be the carrier of last resort throughout all of your rural areas without any universal service support?

Mr. DAVIDSON. Well, first of all, I wanted to respond to this question earlier that came up as well. Commissioner Baum had mentioned the development of this new rural LEC company. We have Windstream here, we have Century Link, we have others that do an excellent job with the business model in terms of serving rural areas. So issues like the parent trap and others are very important and kind of get to your question as well.

In terms of the Verizon territories, we currently participate in the universal service program in certain areas. We are by far a payor into the system by a large amount and we take a small amount out. And that amount is decreasing over time due to merger conditions and other reasons, so we actually participate on the payee side to a very small percent right now. But, again, we support the bill and we support moving through the process in terms of serving our existing customers.

Mr. WELCH. Let me stop you there. Thank you for that. I only have a few seconds left.

Mr. Lubin, in reviewing the draft legislation, what would you see as the three most important components of it?

Mr. LUBIN. The three most important components of this; contribution reform, fixing it; intercarrier comp, fixing it; and recognizing USF for broadband. The 21st century is all about broadband. POTS is going away. You have to figure out how to get broadband. I am sympathetic to your point of how do you get it into the rural area.

Mr. WELCH. Does Mr. Lubin spell for the rest of you? Commissioner Baum.

Mr. BAUM. Just one question. I have now figured out your first question, I am sorry. But, yes, there would be a great—that three factor that they have in there would effectively take communities in some areas of Oregon that are under like 500 population and under who are remote, wouldn't be serviced by this broadband effort.

Mr. WELCH. Thank you.

I think Mr. Graham wants to speak, but I know my time is up, Mr. Chairman, so I yield back.

Mr. BOUCHER. Mr. Graham, go ahead.

Mr. GRAHAM. Very briefly. One other piece of discussion draft would be true competitive neutrality. When wireless goes into an area, we don't get support until we get a customer. When we lose a customer, we lose that support. It seems incredibly reasonable for us for everyone to get support when they get customers, and lose support when they lose customers.

Mr. BOUCHER. Thank you very much, Mr. Welch. And the committee's thanks to all of our witnesses today. We have had a thorough ranging and informative conversation about universal service. I appreciate the broad consensus of support for the discussion draft that has been expressed by the witnesses here today and the many recommendations that we have received for possible additional changes that we could make which would expand that consensus even further. We intend to focus on those recommendations and have subsequent conversations with many of you as we do so over the coming weeks.

Our goal will be to fashion a reform that with broad bipartisan support, we can pass through this committee and the House and have enacted into law during the course of this Congress. Each of you here has contributed to that process here today. We thank you for it.

This hearing stands adjourned.

[Whereupon, at 1:41 p.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

Opening Statement of Rep. Henry A. Waxman
Chairman, Committee on Energy and Commerce
Legislative Hearing on a Discussion Draft of the
"Universal Service Reform Act of 2009"
Subcommittee on Communications, Technology, and the Internet
November 17, 2009

I would like to thank Subcommittee Chairman Boucher and Mr. Terry for bringing forward legislation designed to reform the High Cost Fund of our national Universal Service Program.

In the last century, thanks to the Universal Service Fund (USF) and other support programs, phone service was extended to virtually all Americans. For this century, with a world economy transformed by the Internet, we must ensure that all Americans have access to broadband networks and services.

To meet this challenge, the USF program must be reformed.

The reform principles I listed at our hearing in March still apply:

First, the goals of universal service are as important now – in the age of broadband – as they have ever been.

Second, any modification of the program should be forward looking, not based on past models or even the present subsidy system.

Third, we must recognize that Universal Service Fund dollars are public dollars and with public dollars come public obligations.

Finally, we must ensure full accountability and transparency in this program.

I am encouraged that the Boucher-Terry legislation takes direct aim at a number of these issues.

Specifically, the discussion draft would:

- Broaden the base of revenues on which contributions to the fund would be based;
- Explicitly allow the fund to support broadband deployment;
- Restrain growth through a competitive bidding process;
- Target support paid to non-rural carriers, like AT&T and Verizon; and
- Bring about greater accountability.

In addition, the Boucher-Terry draft addresses a number of related matters that are becoming urgent, including "traffic pumping" and the rural health care program.

These provisions are important reforms, and I commend Chairman Boucher and Mr. Terry for including them.

There are additional issues I hope the Committee will consider as the legislation moves forward.

Should the concept of competitive bidding for USF support be extended to wireline providers as well as wireless providers?

Particularly where unsubsidized competition exists, should the incumbent wireline carrier continue to receive the same subsidy as it always has, or would it make more sense to target ongoing subsidies only to areas where there are no other choices for service?

Should we explore additional carrier obligations to promote the most robust network of networks possible? For example, we might consider eliminating the ability of USF recipients to deny access to competitors that seek to purchase roaming services on networks supported by public monies.

Should we impose obligations on USF supported networks similar to those that were imposed on networks supported by Recovery Act dollars?

Our goal has to be to focus more specifically on how the USF subsidies can better benefit consumers. Over 90% of American households have access to wireline broadband, but the adoption of broadband among low-income households lags far behind the national average.

To address this digital divide, we need to consider shifting money in the current Fund to support consumer adoption of broadband. Congresswoman Matsui has introduced a bill with the goal of expanding access to low-income consumers through a Broadband Lifeline program, and I support her approach.

Finally, I think any effort to reform USF should be closely coordinated with the Federal Communications Commission's (FCC) pending broadband plan. As Chairman Genachowski testified before this Subcommittee, universal service reform will be a critical component of the broadband plan that emerges in February of next year. Just last week, the FCC issued a Public Notice seeking comment on the role of Universal Service and Intercarrier Compensation in the National Broadband Plan. The FCC raises several of the issues addressed by this legislation and asks dozens of questions on these topics. I look forward to hearing more from the FCC on these matters and learning what issues the Commission can address independently and where Congress must act.

Ultimately, this legislation and the FCC's broadband plans must be harmonized.

In closing, I would like to thank Subcommittee Chairman Boucher for being a tireless advocate for universal service reform and his ongoing efforts to engage Congress in this important matter.

I look forward to working with Chairman Boucher, Congressman Terry, and other members of the committee to repurpose this program for the age of broadband.