

**Testimony of
Walter B. McCormick, Jr.
President and CEO, United States Telecom Association
before the
House Committee on Energy and Commerce
Subcommittee on Communications, Technology and the Internet
“The Universal Service Reform Act of 2010” (H.R. 5828)
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Chairman Boucher, Ranking Member Stearns, and Members of the Subcommittee:

Thank you for the opportunity to appear before you today to discuss updating the laws, and in turn securing the financial fundamentals, underlying the provision of universal service to rural Americans. I am Walter McCormick, President and CEO of the USTelecom Association. USTelecom represents innovative broadband companies ranging from some of the smallest rural telecoms in the nation to some of the largest companies in the U.S. economy. Our members offer a wide range of advanced broadband services, including voice, internet access, video, and data, on both a fixed and mobile basis. What unites our diverse membership is our shared determination to deliver broadband services to all Americans – regardless of their location – a goal to which we know this Subcommittee is equally committed.

The universal service program is an American success story. Today phone service is as ubiquitous as electricity and clean water throughout our nation. However, new technologies arise and evolve, and so it is time for universal service and the related regulatory framework governing payments among carriers to be updated to reflect the seismic changes in communications that have occurred over the nearly 15 years since passage of the 1996 Telecom Act. Paramount among these changes is the way in which broadband connections to the Internet have joined voice service as an integral part of our lives.

Over the last decade, broadband providers have invested well over \$700 billion in building and upgrading broadband networks. Reflecting the challenges of serving our Nation’s vast geography and varied terrain, investment on a per capita basis by broadband providers in the U.S. far exceeds that of other countries to which we are often compared, such as Japan, South Korea, and the United Kingdom. Ensuring that all Americans can enjoy the benefits of robust broadband is a goal USTelecom strongly supports. And because of the massive private sector investment in building broadband networks, we are close to this goal. According to the FCC’s National Broadband Plan, robust broadband is available to 95% of the country. Getting to 100% will require an efficient and effective universal service program and sensible reform to the Federal Communications Commission’s (FCC) regulatory framework for payments between and among carriers.

Chairman Boucher and Representative Terry have thoughtfully crafted a bill that carefully balances many competing interests to modernize universal service and to bring

robust broadband to areas of rural America where today's business case would not support such deployment. In particular, H.R. 5828 provides for explicit support of broadband, better targets that support, and strives to match explicit support for the construction and operation of broadband networks with incentives to provide broadband service where it is not available. And by addressing intercarrier compensation as well as universal service, the bill takes a comprehensive approach to addressing the financial fundamentals that will help spur private investment in broadband facilities. We strongly support and share Chairman Boucher's and Representative Terry's commitment to providing all Americans an opportunity to have access to broadband, and at the same time we deeply appreciate their efforts to ensure that the legislation does not impose unfunded mandates on broadband providers as we work to attain that objective. For that reason, and because H.R. 5828 as introduced would bring essential reforms not only to the Universal Service Fund (USF) program but also to the current intercarrier compensation regime, USTelecom is proud to endorse this legislation.

While the intercarrier compensation provisions comprise a smaller portion of the legislation, the dollars involved are at least twice as much as currently available high-cost universal service support. Thus, the two systems must both be addressed because they are, by and large, opposite sides of the same coin. Universal service funds provide *explicit* subsidies to support reasonably priced services. By contrast, the fundamental problem with the existing intercarrier compensation system is that it is riddled with *implicit* subsidies that can no longer be maintained in today's era of new and competitive communications technologies. The transition from implicit to explicit support must be synchronized in a logical way that recognizes the investments telecommunications companies have made in reliance on existing mechanisms.

I will return to the subject of intercarrier compensation shortly, but please permit me first to note the important improvements the Boucher-Terry bill would make in the universal service program. Most importantly, the bill clarifies the FCC's authority to collect funds in a variety of ways to then distribute as universal service support. It authorizes methodologies including use of intrastate as well as interstate revenues, working telephone numbers used by communications providers, or any other current or new connections to the network. It properly broadens the base of contributors and provides the FCC with flexibility to use any or a combination of several methods to more fairly and equitably collect universal service funds.

We also appreciate the inclusion in the bill of provisions that address particular issues with the current system – the potential for disruption in the universal service program by application of the Anti-Deficiency Act and the inequities of restricting support to primary lines. Congress has addressed both over the years in annual appropriations legislation, but this bill would include those fixes in permanent law.

The bill strikes the proper balance between the need for universal service support for broadband while not unreasonably increasing the burden that falls on consumers to fund universal service. It obligates providers to build out broadband facilities to unserved areas, but also makes necessary changes to ensure financial support for meeting those obligations by, among other things, better targeting available funds. And it includes

essential relief to providers in situations in which the mandate and the available support cannot be appropriately matched.

Under today's system, rural consumers may be penalized by virtue of which company provides them service. The bill would eliminate that inequity by targeting rural areas for USF regardless of which company is providing service there and by eliminating the parent trap, which penalizes a rural carrier seeking to buy an exchange based solely on the seller's identity, rather than on the inherent characteristics of the area being served. That is the right and fair way to approach universal service support.

The Boucher-Terry bill also appears to appropriately balance competing interests, in its efforts to better target support by reducing or eliminating high-cost support provided in areas where 75 percent or more of the households have voice and broadband service available from another wired provider, typically a cable company. To ensure consumers are protected, cable companies would be subject to a set of obligations similar to those for incumbent telecommunication providers – such as the basic requirement to provide service to any customer requesting it in the company's service area. Support would then be targeted to the non-competitive areas that tend to have the highest costs. This mechanism, then, seeks to target funds to the truly high-cost areas and conserves scarce universal service funds.

Mr. Chairman, as you well know, it is not uncommon in the legislative process for one stakeholder or another to seek a tweak here or a change there that will make the legislation “just a little bit better” for them. But in this instance, we would respectfully caution that changes to this delicately balanced package potentially risk undermining the compromises you and Representative Terry have worked so hard to forge. The bill as introduced strikes a very careful balance between establishing obligations to provide service in even the most financially challenging areas and the funding available to support the construction and operation of broadband networks in those areas. Mandates that exceed the amount of support provided will not achieve their intended objective. Indeed, they risk driving broadband providers out of the program entirely. As this bill moves through the legislative process, it is very important that the delicate balance you have struck here not be upset by unrealistic expectations about what can or should be accomplished within the limits of the funding being made available.

Let me return now to the other subject of H.R. 5828, intercarrier compensation – the complex regulatory mechanism by which providers pay each other for carrying voice calls on each other's networks. The actual costs of terminating a call are the same no matter where the call originated. However, as a result of the implicit regulatory subsidies mentioned earlier, the rate for terminating a call may be vastly different depending on the origin of the call. Under this system, regulatory arbitrage has become a serious financial problem in the industry, creating an unnecessary obstacle to efficient network investment and operation. The FCC has been struggling with reforming its compensation rules for a decade without success. H.R. 5828 provides much needed guidance, clarifies certain jurisdictional issues, and sets a deadline for the FCC to complete comprehensive reform. The bill also provides guidance on two important elements of reform – traffic pumping and phantom traffic – that are long overdue for FCC action.

Traffic pumping is a scheme by which communications companies artificially generate huge volumes of calls, typically through the offering of services like free conference calling, and then bill other carriers at the highest possible compensation rate. These particular compensation rates were originally established to keep consumer charges reasonable in rural areas, where providers typically have high deployment costs but low average call volumes. Today these rates are being taken advantage of by entities using new technologies with very low deployment costs and tremendously high call volumes. These charges are ultimately borne by all consumers of long distance services. As the National Broadband Plan explained, “because the arbitrage opportunity exists, investment is directed to free conference calling and similar schemes for adult entertainment that ultimately cost consumers money, rather than to other, more productive endeavors.”

Phantom traffic is an even simpler and more pernicious arbitrage scheme – communications companies send traffic over the network to and through other companies, but don’t provide information sufficient for the traffic to be identified. As the National Broadband Plan explained, “traffic is masked to avoid paying the terminating carrier intercarrier compensation entirely, and/or redirected to make it appear that the call should be subject to a lower rate.” If you can’t identify the traffic, you can’t bill for it. So the costs of terminating phantom traffic are passed on to others. The legislation addresses phantom traffic by including a simple but important provision that requires any communications provider that originates traffic to sufficiently identify it.

As much as we appreciate and support the bill’s inclusion of provisions to end both these regulatory arbitrage schemes, we hasten to emphasize that the FCC has a more than sufficient record to deal with them right now. It has received extensive public comment on both traffic pumping and phantom traffic – indeed, USTelecom has provided the Commission with detailed proposals for addressing both these issues that have received broad support. Moreover, the National Broadband Plan urges the FCC to adopt rules to reduce these arbitrage opportunities. It is critical that the Commission not use the pendency of legislation to delay further in adopting fixes to these rapidly growing problems, which it has ample jurisdictional authority to address. And so in addition to moving forward with this legislation, we hope the Subcommittee will encourage the FCC to follow the common sense guidance in the bill and adopt rules immediately.

By squarely addressing the thorny issues of intercarrier compensation reform and universal service, the Universal Service Reform Act of 2010 represents an important milestone in the effort to establish a sound, modern regulatory framework for the future deployment and operation of broadband networks in rural America and throughout the Nation. Adoption of the key elements of the bill, whether legislatively or through speedy FCC action where appropriate, would remove a great deal of regulatory uncertainty and spur investment in broadband facilities. USTelecom looks forward to continuing to work with you, Chairman Boucher, as well as with you Representative Terry, and the members of the Subcommittee, to accomplish these worthy goals.