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WITH RURAL CARRIERS "ON DECK" FOR USF REFORM: FCC'S A-CAM SUPPORT POLICIES DEMAND MORE ATTENTION

The teams still playing in Major League Baseball's 2015 Post Season all have one thing in common—they practiced all aspects of the game every day in order to keep playing in October. The great American pastime provides a key life lesson—preparation. Planning and preparation are keys for a successful baseball season, especially when managing a bullpen or preparing an infield shift for an adroit left-handed batter. It seems that preparation is an important component of most, if not all, worthwhile endeavors.

Consider our rural telecom industry. The Federal Communications Commission (FCC) has been "preparing" the rural carriers for its reform of the federal Universal Service Fund (USF) for several years, ever since the 2010 National Broadband Plan and its 2011 Transformation Order. Yet despite the seemingly ample time preparing for reform, the FCC appears to be running up against a self-imposed deadline to finish many important preparations for federal USF reform. Since we are on the receiving end of the FCC's federal USF reforms, we also need to prepare and respond to proposals intended to reform vital federal support for rural carriers. In this *JSI News and Commentary*, we focus on one issue in the FCC's proposed Alternative Connect America Model (A-CAM) that may not be getting enough attention—namely, the use of <u>two</u> policies designed to limit the number of households or business locations that are eligible for A-CAM support. Early attention to these two policies will help you prepare for what lies ahead if your company transitions to the A-CAM, and may even impact your operations if you don't voluntarily elect the A-CAM.

The A-CAM's beginnings were in the price cap carrier reforms. The price cap carriers proposed a model to the FCC for use in updating and improving its hybrid cost proxy model, which has been used since 2000 to provide support for certain price cap carriers. The FCC modified this proposed model for all price cap carriers and subsequently created the A-CAM for rural carrier purposes.

For our discussion about the eligibility of locations in a study area, it isn't necessary to revisit the historical development of the A-CAM except for understanding that the A-CAM contains two modules. These two modules define the overall structure of the A-CAM. The first, the "Cost to Serve" module, determines the cost of providing universal service to specific locations using a multitude of inputs and rules. Although critical review of these inputs and engineering rules is vitally important, we'll set this review aside for discussion in a future newsletter.

Our focus today is on the "Support Module." It is in this second module where the FCC determines the number of locations in a study area that will be eligible for federal USF. The FCC uses two policies to make this determination: the competitive overlap policy and the benchmark policy. The competitive overlap policy is a significant threat to RLECs with a cable broadband or fixed wireless competitor in its service area, as locations determined to be in a competitive census block will be eliminated from support eligibility. The benchmark policy, which is explained more thoroughly below, essentially says that locations below a certain cost benchmark will not be eligible for A-CAM support. These two policies, depending on what the FCC eventually adopts, will determine the locations eligible for support, and ultimately the amount of money a rural carrier may receive if it volunteers to accept the A-CAM support (and the attendant obligations) for its study area.

There also is overlap between the two policies. Since competition typically enters the rural market in higher-density, lower-cost areas, it stands to reason that many of the locations experiencing competition are lower-cost locations that also would be subject to the benchmark policy. By examining the interaction of these two policies, it becomes apparent that the FCC has two means to achieve the same end. The FCC is able to use either one to disqualify locations from federal A-CAM support. Combined, the two policies become a 4-5-3 end-the-inning double-play.

Let's look first at the competitive overlap policy. Concern about the application of the FCC's competitive policy emerges when reviewing the FCC's current study area 100% elimination policy, its reasonable request safe harbor for broadband service, and its proposed reform for future High Cost Loop Support (HCLS) and Interstate Common Line Support (ILCS). In all these instances, the FCC's overarching objective is to limit or eliminate support in areas where there is a competitive alternative for broadband service and, by extension, VoIP service. Rightfully, rural carriers must pay attention to the competitive overlap policy and the data the FCC currently uses to make its determination. Many JSI clients have reported instances where they know there isn't a competitive provider in a study area, but the FCC claims there is. The misunderstanding arises due to how the FCC is using the Form 477 data reported by all broadband providers. The appearance of a cable wireline provider or a fixed wireless provider is largely determined by the type of technology selected on Form 477. In one example, the rural incumbent uses fixed wireless to provide voice service to end-user customers and the appearance of its own fixed wireless service on its Form 477 is being interpreted as an indication of a competitor in the area. JSI is hopeful the FCC will iron-out cases where affiliates or the incumbent's own operations are seen, incorrectly, as "competitive."

However, it would be folly to focus on only the competitive overlap policy when the FCC actually may eliminate more locations with its second support module policy—the benchmark policy. This policy establishes a benchmark for the average cost of providing service to an area. If the incumbent's cost is lower than the benchmark, then it doesn't need federal support for these locations. Simply put, the FCC assumes the carrier will receive enough end-user customer revenue to support the cost of providing service to locations in the area, absent any additional support from the future Connect America Fund (CAF) for rate-of-return carriers.

Remember how A-CAM grew out of the price cap carriers' USF reform efforts? As part of that process, the FCC created a benchmark for price cap carriers and, absent further discussion, uses this benchmark for rural carriers too. The current benchmark is $52.50 per month per location. The FCC calculated that number by assuming that end-user customer revenue for basic voice and basic broadband is $75 per month. Although, the FCC recognizes that carriers don't provide service to every potential location, they do assume that the rural area subscribership penetration rate is 70%. Seventy percent of $75.00 equals $52.50. JSI has concerns about both the $75.00 per month revenue assumption in rural areas and the 70% take rate assumption. In its 2015 Report to Congress (Section 706 Report), the FCC identified the national non-urban area take rate for 10Mbps/768Kbps at just 47%. Accepting *carte blanch* 70% as the correct take rate when the data show a lower percentage for non-urban areas warrants an explanation.

The appropriateness of these two assumptions has not been fully vetted. JSI brings the FCC's benchmark policy to your attention because of its analysis of the FCC's newly released A-CAM version 2.0. It is apparent that the benchmark policy is as important, or perhaps even more important, than the competitive overlap policy, in the determination of locations eligible for A-CAM support. To support this claim, consider the national numbers coming from the FCC's Form 477 as reported by the FCC when it released A-CAM version 2.0.

The A-CAM 2.0 scenarios released by the FCC report 6,532,549 total locations in rural carrier areas. Of these, the FCC determines that only 1,997,508 locations are currently eligible for A-CAM support, thus eliminating 4,535,041 locations due to either the competitive overlap policy or the benchmark policy, or both. JSI can break down these two individual effects for those who have signed the FCC's non-disclosure agreement, but we cannot divulge the details in this newsletter. Notwithstanding, looking at the individual effects, it becomes clear that the benchmark policy is a powerful player in the FCC's lineup of policy reforms to reduce reliance on USF and instead focus support only for locations that are truly unserved and high cost. Even without applying its competition policy, the FCC eliminates the vast majority of the total "eliminated" locations using its benchmark policy.

A preliminary analysis of the A-CAM version 2.0 suggests that rural carriers need to focus on the <u>two</u> support module policies equally in order to prepare for the anticipated federal USF reforms. Companies that are already planning to voluntarily elect A-CAM support as soon as it is available (tentatively early next year), as well as those that plan to stick with reformed legacy support, are strongly encouraged to consider how the two policies would impact support levels, and to ask hard questions about the policies in preparation for the decision. Both policies also need to be fully vetted before the FCC adopts them for rural carrier use. Input from the industry about the actual broadband adoption rate and competitive market in your service areas is vital for the FCC to prepare its final rules about how both policies impact A-CAM support.

If you have any questions or comments on this article or about any aspect of the A-CAM, please contact John Kuykendall or Brian Sullivan in JSI's Maryland office at 301-459-7590 or Douglas Meredith in our Utah office at 801-294-4576.

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