The Public Service Commission of the State of Missouri (“MoPSC”) is submitting comments in response to the Federal Communications Commission’s (FCC’s) high-cost universal service fund reform efforts and efforts to shift savings toward supporting the provision of broadband in unserved areas. In response to the FCC’s inquiry on the type of cost model that should be used to determine funding support, the MoPSC recommends a forward-looking, incremental cost model that includes consideration of a company’s revenues. In response to issues related to using a competitive bid process for accelerating the provision of broadband service to unserved areas, states should have the opportunity to provide input into the bid evaluation process. The MoPSC supports the FCC’s specific proposals to reform the legacy high-cost program. These recommendations are more fully explained in the remainder of these comments.
Cost Model

The FCC’s Notice of Inquiry seeks comment on cost model issues related to quantifying the minimum amount of funding support necessary to provide broadband in unserved areas. Ultimately a cost model may have limited relevancy if the FCC selects an auction or competitive bid process to determine funding support. Nevertheless the FCC seeks feedback on cost models for the potential purpose of establishing a reserve price or determining appropriate support amounts in areas unable to use a competitive bidding mechanism. Although the MoPSC has reservations about the viability of using a competitive bidding mechanism, the MoPSC offers feedback concerning cost models.¹

The MoPSC recommends a cost model used for funding purposes should estimate forward-looking, incremental cost.² In general, the MoPSC has long advocated using forward-looking costs for determining support. For example the MoPSC has previously stated,³

“High-cost support should be based on a carrier’s forward looking costs. Carriers should not expect to receive high cost support based on already incurred embedded costs. A forward looking cost method will promote efficient use of scarce and valuable universal service monies.”

¹ Prior MoPSC comments have repeatedly attempted to express reservations about using a competitive bid process to determine USF support. For example see Comments of the Missouri Public Service Commission of the State of Missouri, Case No. WC Docket No. 05-337 In the Matter of High-Cost Universal Support, Case No. CC Docket No. 96-45, In the Matter of Federal-State Joint Board on Universal Service; May 2007, April 2008 and November 2008. Most notably the MoPSC’s concern is an auction process may only work well if multiple bidders are participating; an unlikely prospect in high-cost areas.

² This recommendation is responding to the FCC’s Notice of Inquiry Paragraph No. 23 where the FCC states, “We seek comment on whether the Commission should base any new CAF support on forward-looking economic costs of an efficient provider, rather than on historic, embedded costs….”

³ Page 5, Comments of the Missouri Public Service Commission of the State of Missouri, Case No. WC Docket No. 05-337 In the Matter of High-Cost Universal Support, Case No. CC Docket No. 96-45, In the Matter of Federal-State Joint Board on Universal Service; April 23, 2008.
A forward-looking cost model is preferred for a couple of reasons. A forward-looking cost model more closely approximates a competitive market.\footnote{This position is also shared by the United States Court of Appeals who supported the FCC’s use of a forward looking cost method. See Iowa Utilities Board, et al, v. FCC, 219 F.3d 744 (8th Cir. 2000).} For example, a company’s business decision to enter a market will depend on the company’s forward-looking costs. Conversely, historical costs can be considered irrelevant in that such costs are unaffected by a company’s business decision. In this regard, forward-looking costs, rather than historical embedded costs, help ensure more efficient investment decisions. For instance, it makes little sense to identify costs associated with expanding an inefficient network or using outdated technology.

The model should also identify incremental costs rather than total costs.\footnote{This recommendation is responding to Paragraph No. 33-34 of the FCC’s Notice of Inquiry whereby the FCC seeks comment on whether total costs or incremental costs should be estimated by the model.} For example, if a carrier currently provides broadband service to eighty-five percent of its customers then the model should identify the additional cost of deploying broadband service to the remaining fifteen percent of customers. An incremental cost approach makes sense because it attempts to identify the additional costs needed to provide broadband service to the unserved area. Conversely the embedded costs currently used to provide broadband service to existing customers are irrelevant because these costs remain unchanged regardless of whether broadband service is extended to the unserved area. The MoPSC has used an incremental costing approach for many years in an effort to promote an efficient pricing mechanism.\footnote{The MoPSC first adopted the use of an incremental cost approach in Case No. 18,309, In the matter of the cost of service study of Southwestern Bell Telephone Company, May 27, 1977. In this decision the Commission adopted the concept of long-run incremental costs (LRIC) as a basis for pricing decisions. LRIC is defined as “…the change in all costs, including the effect on common costs as a result of adding units of a single service or adopting an alternative schedule of rates….} The use of an incremental cost model for
support determination can be justified by the same rationale used for supporting forward-looking costs.

In addition to calculating incremental costs, the model should consider incremental revenues in determining a need for funding support. A company can generate revenue from a variety of services (i.e., voice, Internet, video, and so forth) using the broadband network. If a company expands broadband service to an unserved area then incremental revenues for all services using the network should be included within the model. Such revenues will help offset incremental costs and consequently should be a factor in any model intended to determine funding support. For modeling purposes, the calculation of such revenues should include an assumption for minimum benchmark rates.

Regardless of the model ultimately selected by the FCC, the cost model should comply with certain concepts. The FCC should strive to ensure the model is technology and provider neutral. In other words, the model should identify costs of an efficient network without favoring a particular technology or provider. In addition, any cost model should be open to public inspection whereby assumptions and algorithms can easily be viewed and critiqued.

The MoPSC has reservations about the National Broadband Plan model’s approach to existing funding support. Specifically, the National Broadband Plan model ignores existing funding support currently provided to the area. Stated differently the National Broadband Plan model assumes existing networks will be available on an

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7 This MoPSC recommendation is responding to the FCC’s Notice of Inquiry Paragraph No. 35 where the FCC asks, “We seek comment on whether the Commission should consider revenues, as well as costs, in determining CAF support….”
ongoing basis. This modeling approach raises concerns if the model’s purpose is to determine the amount of additional funding support needed to provide broadband service to the unserved area. For example, existing funding support may be inappropriate since no analysis has ever been performed to evaluate whether current funding support is adequately promoting the universal service principles of the Act. Conversely, future changes to the existing high-cost program may reduce existing funding levels and impact a company’s ability to maintain broadband service where it currently is available. If the FCC ultimately intends to use the National Broadband Plan model to determine additional funding support then the FCC should reexamine the appropriateness of the model’s approach and assumptions concerning existing funding support for the area. The National Broadband Plan model’s approach and assumptions concerning existing funding support only make sense if: (1) existing support levels are determined to be appropriate, and (2) future changes to the amount of existing funding support will not impact the ability to maintain broadband service where it is currently available.

**Expedited Process for Providing Funding to Extend Networks in Unserved Areas**

The FCC appears to be primarily considering variations of a competitive bid process as the means to accelerate and target funding for extending broadband service to unserved areas. If the FCC uses a competitive bid process, the FCC should strive to develop a bid evaluation process that selects the best bid versus the lowest bid. The procurement auction process outlined in Appendix B of the FCC’s Notice of Inquiry

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8  This assumption is acknowledged in the FCC’s NOI, Paragraph 33.

9  This concern was previously raised by the MoPSC. See page 8, Comments of the Missouri Public Service Commission of the State of Missouri, Case No. WC Docket No. 05-337 In the Matter of High-Cost Universal Support, Case No. CC Docket No. 96-45, In the Matter of Federal-State Joint Board on Universal Service; April 23, 2008.
appears to try and identify the “best” projects by careful auction design whereby bid scoring or ranking criteria is very clear and simple.

In the quest to select the best bid, a state should have some input to the evaluation of bids pertaining to unserved areas within the state. For example, a state should have the opportunity to review bids relevant to the state and submit input in a timely manner. Local input should improve the evaluation process without an unnecessary delay. State involvement could be performed after an initial prescreening process whereby frivolous bids failing to meet all the auction rules and requirements are eliminated from further consideration. Time constraints could be placed on states to review bids and provide input.

**Reforming the Legacy High-Cost Program**

The FCC’s proposal to cap legacy high-cost support to incumbent local telephone companies at 2010 levels appears reasonable as a temporary measure until the FCC determines how to distribute funds in a more efficient manner. As previously expressed by the MoPSC, the appropriateness of existing high-cost support levels needs to be examined. The MoPSC has repeatedly urged comprehensive reform of the high-cost universal service support program, including an examination of whether existing support is needed to maintain the universal service principles identified in federal law. High cost support should cease if the principles of universal service can still be achieved without such funding. USF reform should not attempt to preserve existing revenue levels.
At this time, the MoPSC cannot specifically comment on the other specific legacy high-cost support reform proposals identified by the FCC. In this proceeding the FCC has sought specific feedback from parties if they believe any of these high-cost reform proposals will negatively affect affordable voice service. While the MoPSC reserves judgment until such feedback can be reviewed, the proposals are conceptually reasonable approaches to reforming and controlling the size of the universal service fund. Despite the proposal ultimately selected, to the extent possible, the MoPSC recommends gradual implementation. A gradual approach may help minimize any negative impacts to companies and ultimately consumers.

The MoPSC’s rationale for generally supporting the FCC’s various reform proposals of the legacy high-cost program are as follows: The proposal to shift rate-of-return carriers to incentive regulation has merit simply on the basis of the archaic nature of maintaining rate-of-return regulation. The proposal to eliminate interstate access support has merit because a support fund should not be used as a long-term revenue replacement mechanism for lowering interstate access charges. At the time the FCC created this support in 2000, the FCC indicated it would revisit this support after five years; however to date no review has been conducted. In this regard, reform should be on providing or maintaining universal service to those customers needing access to service consistent with the principles of the Telecommunications Act of 1996, not on preserving revenue streams.

10 These proposals include shifting rate-of-return carriers to incentive regulation, eliminate interstate access support, implement the Sprint and Verizon Wireless merger commitments, and eliminate competitive ETC high-cost support.
The proposal to eliminate high-cost support for competitive eligible telecommunications carriers has merit because supporting multiple providers to provide service within the same area is conceptually inefficient. The MoPSC maintains high-cost support should be provided to the least number of carriers and areas necessary to achieve universal service. The MoPSC has also previously supported the concept for providing support to only one recipient as a way to minimize the size of the fund and still maintain the Act’s universal service principles.\textsuperscript{11}

Respectfully submitted,

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Dated: July 12, 2010

\textsuperscript{11} Comments of the Public Service Commission of the State of Missouri regarding reverse auctions in WC Docket No. 05-337 In the Matter of High-Cost Universal Support and CC Docket No. 96-45 In the Matter of Federal-State Joint Board on Universal Service, pages 3-7, April 23, 2008.