



6712-01

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 54

[WC Docket Nos. 10-90, 14-58; FCC 17-12]

Connect America Fund, ETC Annual Reports and Certifications

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: In this document, the Federal Communications Commission (Commission) takes another step towards implementing the Connect America Phase II auction in which service providers will compete to receive support of up to \$1.98 billion to offer voice and broadband service in unserved high-cost areas.

DATES: Effective **[INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

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SUPPLEMENTARY INFORMATION: This is a summary of the Commission's Report and Order and Order on Reconsideration in WC Docket Nos. 10-90, 14-58; FCC 17-12, adopted on February 23, 2017 and released on March 2, 2017. The full text of this document is available for public inspection during regular business hours in the FCC Reference Center, Room CY-A257, 445 12th Street, SW, Washington, DC 20554, or at the following Internet address:

https://apps.fcc.gov/edocs_public/attachmatch/FCC-17-12A1.pdf

I. INTRODUCTION

1. With this Report and Order and Order on Reconsideration (Order), the Commission takes another step towards implementing the Connect America Phase II (Phase II) auction in which service providers will compete to receive support of up to \$1.98 billion to offer voice and broadband service in unserved high-cost areas. The decisions the Commission makes in this Order aim to maximize the value

the American people will receive for the universal service dollars the Commission spends, balancing higher-quality services with cost efficiencies.

2. First, the Commission resolves issues raised in the Phase II Auction Order FNPRM, 81 FR 44414, July 7, 2016 and 81 FR 40235, June 21, 2016. The Commission adopts weights to compare bids among the service performance and latency tiers adopted in the Phase II Auction Order, 81 FR 44414, July 7, 2016. Additionally, the Commission declines to adopt specific preferences for certain states and Tribal lands in the Phase II auction and decline to adopt alternative interim deployment obligations for a subset of Phase II auction recipients. However, the Commission does adopt preferences that will be implemented in the Remote Areas Fund auction for states where the Phase II offer of model-based support was declined, subject to certain conditions.

3. Second, the Commission also considers several petitions for reconsideration of decisions made in the Phase II Auction Order. The Commission denies a petition for reconsideration of the Commission's decision to score bids relative to the reserve price, grants a petition for reconsideration of the Commission's decision to retain the option to re-auction certain areas served by high latency bidders if a set subscription rate is not met, and grants a petition for reconsideration of the Commission's decision to require bidders in the Above-Baseline and Gigabit performance tiers to offer an unlimited monthly usage allowance.

II. REPORT AND ORDER

4. Discussion. The Commission now adopts weights for the Phase II auction performance and latency tiers that will account for the value of higher speeds, higher usage allowances, and low latency, but that will also balance these preferences against the Commission's objective of maximizing the effectiveness of its funds to serve consumers across unserved areas with the Commission's finite budget.

5. The Commission first clarifies that weights are positive values that will be added to a particular bid-price-to-reserve price ratio to arrive at a score. Mathematically, $\underline{S} = 100 \times \underline{B}/\underline{R} + \underline{T} + \underline{L}$, where \underline{S} is the bid's score, \underline{B} is the current bid price, \underline{R} is the reserve price, \underline{T} is the weight assigned to the

bid's associated tier of service, and L is the weight assigned to the bid's associated latency. Because the Phase II auction will be a reverse auction, higher service tiers will accordingly have lower weights.

6. Specifically, the Commission will weigh bids so that Minimum performance tier bids will have a 65 weight; Baseline performance tier bids will have a 45 weight; Above Baseline performance tier bids will have a 15 weight; and Gigabit performance tier bids will have zero weight. Moreover, high latency bids will have a 25 weight and low latency bids will have zero weight added to their respective performance tier weight.

7. The following charts summarize the Commission's adopted approach:

Performance Tier	Speed	Usage Allowance	Weight
Minimum	$\geq 10/1$ Mbps	≥ 150 GB	65
Baseline	$\geq 25/3$ Mbps	≥ 150 GB or U.S. median, whichever is higher	45
Above Baseline	$\geq 100/20$ Mbps	2 TB	15
Gigabit	≥ 1 Gbps/500 Mbps	2 TB	0

Latency	Requirement	Weight
Low Latency	≤ 100 ms	0
High Latency	≤ 750 ms & MOS of ≥ 4	25

8. A number of commenters proposed different ways to apply weights. Some parties also suggested using positive weights, while others suggested negative weights, and some suggested a mix of both. By adding increasing weight as speed and usage allowances decrease and latency increases, the

Commission concludes that its approach is a straight-forward representation of the fact that the Commission values higher speeds and usage allowances and lower latency, and should be easier for bidders to understand and simpler for us to implement. Moreover, a number of parties suggested that the Commission uses percentage weights but suggested various ways to apply the percentage. The Commission concludes that their overall approach of adding the weight to the bid-to-reserve price ratio appropriately applies the weights uniformly across all areas, thereby increasing competition and giving providers in all eligible areas opportunities to win. The Commission also declines to adopt the approach it suggested in the Phase II Auction FNPRM, 81 FR 40235, June 21, 2016, whereby the weight would be subtracted directly from the dollar amount placed by the bidder. The Commission is persuaded by commenters who suggest such an approach would have a disproportionate impact on bidders that place bids for smaller dollar amounts.

9. The Commission's weighting scheme for the performance tiers is designed to balance its finite budget with the reality that, in some areas, speeds of 10/1 Mbps may be the limit of what is achievable in the near term but will still offer significant benefits to currently unserved areas, including the potential that service providers may choose to increase speeds to meet consumer demand once they have made the initial investment of deploying to certain areas. At the same time, the weights the Commission implements also attempt to leverage its finite budget to achieve speeds that are scalable to meet the evolving needs of consumers over the 10-year term and the broader community in areas where it is cost-effective to do so.

10. The record regarding the weights that the Commission should adopt for the different performance tiers varies, with parties arguing for weights as low as 5 and as high as 100 between tiers, and relying on several different methodologies for establishing the weights. To sift through these proposals and establish a reasonable range of weights to choose from, the Commission relies on the following propositions.

11. First, the Commission starts with the principle that the Connect America Phase II auction must indeed be an auction, not simply a procurement process. The Commission wants this to be a

competitive auction where every bidder has the opportunity to exert competitive pressure on all other bidders, and weighting increments of 100 or more would effectively result in each tier always winning over bids placed in lower tiers, which may provide an incentive for bidders in higher tiers to inflate their bids. The Commission already decided that all bids would be considered simultaneously, and it would not realize the benefits of competition if one type of bid effectively always wins over another regardless of the bids' support amounts. Or, as the Commission puts it in the New York Auction Order, an “absolute preference” for “one type of technology or speed” would be fiscally irresponsible “when more cost-effective, reasonably comparable options may be available.”

12. Second, the Commission takes that principle one step further and conclude that every bidder — no matter the service tier or latency — must have the opportunity to exert competitive pricing pressure on every other bidder. In other words, the total band of weights must be less than 100. This principle should maximize the competitive pressure all bidders bring to bear, ensuring that even the highest-tier services take into account the bang-for-the-buck they are delivering to consumers nationwide. It also ensures that the Commission examines its weights holistically, so that the accumulation of weights does not lead to untoward and unexpected consequences.

13. Third, the Commission concludes that the weights it assign should strive to reflect the value of higher-speed and lower-latency services to consumers. The purpose of the Connect America Phase II auction is to maximize the value the Commission can bring for consumers through the use of scarce universal service funds—in effect, the weights recognize that consumers can and do spend more to receive higher quality services. Accordingly, the Commission rejects claims to set weights that normalize the deployment costs for the performance tiers based on technology. The Commission sees no reason to spend scarce universal service funds to pay for more-expensive services just because they are more expensive. Indeed, the value to a consumer of a fiber-based service is not its cost but the faster speeds and lower latencies it offers—and the goal of the Commission is and must be to minimize (not maximize) the cost of such services. Moreover, adding a separate weight to account for technology costs would be contrary to the Commission's objective to maximize its cost-effective budget because it could result in

paying more for higher cost technologies when it might be more cost-effective to support lower cost technologies. And given the challenges of determining representative costs for each type of technology, such an approach is likely to add complexity to auction process and could lead to delay. In a similar vein, the Commission rejects claims to weight bids in correlation to the respective download speeds. Such an approach would have the effect of heavily weighting the Gigabit performance tier, without any evidence that consumers do indeed value that service in proportion to its speed or would be willing to spend 100 times more for such service than for service at the Minimum performance tier.

14. Fourth, the Commission concludes that adopting minimal weights between each tier would be inappropriate. Consumers clearly value higher speed and lower latency services, and minimal weighting could deprive rural consumers of the higher-speed, lower latency services that are common in urban areas. Indeed, such an approach would likely result in bids in lower tiers prevailing, leaving all consumers with minimum service even though some service providers might be able to offer increased speeds for marginally more support. Additionally, the upcoming Remote Areas Fund auction will provide an opportunity to ensure that all Americans at least have the opportunity to receive some broadband service. For purposes of the Phase II auction, the Commission's aim is to maximize consumer welfare given the limited budget they have. The Commission disagrees with commenters that suggest that giving bids placed in the Gigabit tier anything other than a minimal preference violates its statutory duty to support reasonably comparable services because Gigabit services are not widely available in urban areas. The Commission is not persuaded that it must only support services that have "through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers" First, this is only one of several factors the Commission must consider when establishing the definition of supported services. Second, the Communications Act of 1934, as amended (the Act) makes clear that universal service is an "evolving level" of services, and thus the Commission must consider the fact that through the auction it will be providing support to voice and broadband services over a 10-year term. At the same time, the Commission disagrees with arguments suggesting that it is a violation of the Commission's statutory duty to promote access to services that are reasonably

comparable to those services offered in urban areas if the Commission awarded support to bids committing to provide a minimum of 10/1 Mbps speeds given the 10-year support term and the fact that most urban areas have access to higher speeds. Instead, the Commission finds that it is reasonably and responsibly leveraging the Phase II auction to make significant steps towards achieving its overarching statutory responsibility to support reasonably comparable services for all consumers. The Commission has adopted a range of performance tiers with increasing weights, starting with speeds and usage allowances the Commission has deemed reasonably comparable in the near term and with maximum speeds and usage allowances that are scalable to meet the needs of consumers at the end of the 10-year term.

15. With those principles in mind, the Commission reviews the weight of the record. Most parties proposing within these parameters suggest increment values somewhere between 5 and 60. Parties arguing for smaller weight increments between speed tiers with a focus on the lower speed tiers suggest that the Commission's focus should be on maximizing the number of locations that have access to services that are reasonably comparable to those offered in urban areas, and that giving a heavy preference to higher speed and usage allowance tiers would be an inefficient use of the finite budget, favoring high speeds and usage allowances at the expense of leaving many without service. They argue that heavily weighting bids or assigning any weight to bids committing to a Gigabit performance tier would violate the Commission's statutory duty to support reasonably comparable services, and they claim that consumers are more concerned with having access to service at reasonable prices than subscribing to expensive high speed packages. They suggest that if consumers' needs evolve and they begin to demand higher speeds, carriers will have an incentive to increase the speeds they offer as deployment costs go down. Supporters of narrow weights also claim that such weights would promote efficiency by challenging bidders seeking to offer services in the higher tiers to place more cost-effective bids.

16. By contrast, other parties argue that higher speeds and usage allowances should have heavier weights so these bids are more likely to prevail. Some of these parties suggest that the speeds in the Minimum and Baseline performance tiers would not be sufficient to constitute reasonably comparable

services. They argue that the Commission should focus on supporting “future proof” networks given that speeds that are reasonably comparable today may not be reasonably comparable throughout the 10-year support term. They also suggest that certain technologies that may be more cost-effective today are likely to be more expensive in the long term because such networks will need to be upgraded to meet consumers’ needs, and that it would be more efficient to support speeds that can be leveraged by entire communities. They claim that if higher tier bids are not given sufficient weight, bidders able to offer such services will be less likely to participate, and bidders in lower tiers could win without having to place cost-effective bids. Some of these commenters argue that higher speeds should be given a near absolute preference, while others argue for more moderate increments between the tiers.

17. Taking into account these principles and the record, the Commission finds that increments of 15–30 between performance tiers appropriately balance the concerns of these potential bidders, and their representatives, by adopting increments that are within a reasonable range of the increments proposed by both sets of commenters. Based on the Commission’s predictive judgment, the Commission concludes that this approach is likely to promote competition both within and across areas by giving all service providers the opportunity to place competitive bids, regardless of the technology they intend to use to meet their obligations. The Commission weights appropriately recognize the value to rural consumers of higher speeds and higher usage allowances, but bids placed in the higher tiers will not necessarily win because of the generally greater costs of deploying a higher capacity network at higher speeds. Bids placed for lower speeds and usage allowances will still have the opportunity to compete for support, but will have to be particularly cost-effective to compete with higher tier bids.

18. The Commission is not convinced by suggestions that it should adopt weights that are based on metrics derived from consumer preference data. Commenters proposed several competing data sources and methodologies in an attempt to substantiate their proposed weights as “objective,” but the Commission declines to adopt any of these proposals. The Commission concludes that establishing weights based on specific data is likely to be a drawn out and complicated process that may further delay the Phase II auction and may not produce an improved outcome in the auction. Moreover, a consumer’s

decision to subscribe to a particular service may be based on numerous variables and does not necessarily suggest that one level of service should be valued by a particular percentage over another level of service in areas where consumers currently have no options for service. The Commission is not persuaded that its decision to adopt weights that are not derived from specific data is “arbitrary.” Instead, the Commission adopts weights between each tier that recognize the value of increased speeds and usage allowances and select weights that fall within the range of weights proposed by parties in the record that do not seek to give any one tier an absolute preference.

19. The Commission is not persuaded that some of the other proposals parties made in the record regarding how to approach weighting the different tiers would be consistent with its objectives and statutory duties. First, the Commission disagrees with the suggestion that it should only weight bids in higher tiers if sufficient funding is available to fund all bids at the Baseline performance tier. While this approach might permit us to serve more consumers, the Commission would lose out on the opportunity to balance its other objective of funding service that will achieve reasonable comparability for the long term. Section 254 of the Act makes clear that universal service requires an evolving level of service.

20. Second, the Commission is not convinced that it should fund extremely high-cost locations only after the Commission has funded all bids for high-cost locations. When it decided to include the extremely high-cost census blocks in the Phase II auction, the Commission explicitly recognized that in some areas a service provider might be able to make a business case to serve extremely high-cost areas efficiently even though the Connect America Cost Model has determined an area to be extremely high-cost. The Commission has explained that, because extremely high-cost areas are interspersed among high-cost areas, including extremely high-cost census blocks in the Phase II auction enables parties to build integrated networks that span both types of areas as appropriate. The approach gives bidders the flexibility to decide how to most efficiently upgrade or extend their networks. It would contradict this rationale to refuse to fund bids in extremely high-cost areas until high-cost area bids have been awarded because such an approach would assume that bids in high-cost areas would be more cost-effective.

21. The Commission also concludes that its decision to adopt a weight of 25 for high latency bids appropriately balances its objective of using its finite budget in a cost-effective manner, but also supporting services that will meet consumers' needs. The Commission decided in the Phase II Auction Order to open the Phase II auction to participation from satellite providers "in the interest of making this auction as competitive as possible." It adopted objectively measured latency performance standards to ensure that consumers received an appropriate level of service.

22. Commenters propose a wide range of weights in the record for the latency tiers, from weights as high as 100 to weights as low as 10, with commenters proposing weights lower than 100 suggesting a weight within the range of 10 to 75. Because they propose latency tier weights relative to their proposed performance tier weights, the Commission similarly considers weights for the latency tiers relative to the weights it adopted for the performance tiers above. The Commission is not persuaded by commenters that argue that low latency services should be heavily weighted or by comments suggesting that low latency services should always win over high latency services. Thus, the Commission concludes a weight of 100 or 75 would be too high. While many commenters raise concerns about high latency services, the Commission already took such concerns into account when deciding to adopt objective performance requirements so that high latency providers can participate. The Commission is not persuaded that high latency providers should have to partner with terrestrial providers in order to participate competitively in the Phase II auction. Indeed, by choosing to adopt alternative latency requirements for high latency providers, the Commission has already rejected the concept that this is the only way high latency providers can be competitive. While the Commission welcomes such partnerships, it concludes that it serves the public interest to permit service providers to determine how they are best able to place a competitive bid, either by leveraging their own network or partnering with other providers.

23. Commenters suggesting weights below 75 argue for a range of weights between 10 and 45 relative to their own various performance tier proposals. Similarly, based on the weights the Commission has adopted for the performance tiers above, it concludes that a weight of 25 would reasonably maximize competition. A weight of 25 is appropriate because a bidder placing a low latency

bid in the Gigabit performance tier will not necessarily win, which will add pressure on such bidders to make more cost-effective bids. A Minimum performance high latency bidder will have cumulative weight of 90 (65 for the Minimum performance tier; 25 for the high latency bid), which will provide a reasonable opportunity for high latency bidders to make competitive bids in the lower performance tiers.

24. Relative to the performance tiers the Commission has adopted, it also concludes that a weight of 25 is more appropriate than a narrower weight like 10 or 15, given the arguments in the record about the benefits of low latency services, especially in areas where the Phase II auction recipient is the only voice provider. The Commission concludes that like the weighting approach it has adopted for the performance tiers, adopting a moderate weight will take a significant step towards ensuring consumers throughout the country have access to reasonably comparable services pursuant to the Commission's statutory duty, while also balancing the realities of its finite budget and the high costs of providing voice and broadband to these unserved areas. The Commission rejects arguments that it should adopt a narrower weight for latency than it has adopted for speed tiers to account for claims that consumers value higher speeds over lower latency. First, the performance tier weighting the Commission has adopted already accounts for the value of higher speeds given that, as speeds increase, the weights will decrease. Second, while high latency providers suggest that consumers' satisfaction with high latency services has improved so that it is comparable to some cable services, some consumers have chosen high latency services over low latency services, and that terrestrial providers emphasize speed and price over latency in their marketing materials, these claims do not address the concerns raised by commenters about the inherent limitations of high latency services—particularly for interactive, real-time applications and voice services given that high latency providers may be the only voice providers in the area. The Commission is not persuaded that it should use consumer data to establish the bidding weight between low and high latency bids. As explained above, such an approach has the potential to be highly subjective, and the process would likely be complex and time-consuming. Moreover, the fact that parties subscribe to more low latency services in urban areas could be due to a number of factors and does not necessarily suggest

that a high latency service would not meet the needs of consumers living in otherwise unserved high-cost areas.

25. Finally, the Commission is not persuaded that it should adopt other types of weights that have been proposed in the record. Generally, the Commission finds that the more weights it adopts to effectuate various perceived policy preferences, the more the Commission moves away from the objective of maximizing the reach of its budget by awarding bids based on cost-effectiveness. Moreover, additional weights add more complexity to the auction design and, in turn, this increased complexity could drive down interest and participation in the Phase II auction. In addition, the Commission explains above why the weights it has adopted serves the public interest because they help us balance other important objectives, like ensuring that consumers have access to reasonably comparable services. Parties proposing that the Commission adopts other types of weights to advance other objectives have not demonstrated similarly compelling public interest benefits.

26. For example, the Commission declines to adopt weights that would improve a bid's ranking if it covers small areas. The Commission notes that in some cases, service providers may be able to take advantage of economies of scale by bidding on larger areas, and in those instances bids for larger areas may be more cost-effective. But the Commission also declines to adopt weights that would give a preference to bids that included 75 percent or more funded locations within a state. The Commission notes that there could be instances when it is more cost-effective for a number of carriers to offer service within a state. Similarly, the Commission declines to adopt weights to give a preference to small bidders. The Commission's focus is on maximizing the effectiveness of its funds to serve consumers nationwide. While the Commission encourages small bidders to participate in the Phase II auction and have adopted eligibility requirements to facilitate their participation, it is not persuaded that giving a preference to smaller bidders will necessarily achieve its objectives when it is possible that a larger bidder may be able to make a more cost-effective bid in a higher performance or lower latency tier. Rather than artificially give a preference to smaller or larger bids or to small bidders, the Commission prefers to rely on the cost-

effectiveness scores of bids to determine how its budget can best be maximized to serve the most consumers with service that is reasonably comparable to service offered in urban areas.

27. If unqualified bidders are able to participate in the auction and divert support from qualified bidders able to offer service meeting the Commission's requirements then consumers would ultimately be harmed. In the Phase II Auction Order, the Commission required bidders to submit with their short-form applications any information required to establish their eligibility for weights adopted by the Commission. Now that the Commission has adopted weights for the performance and latency tiers, it is persuaded that in some circumstances it may serve the public interest to require potential bidders to submit evidence that demonstrates that they can meet the service requirements associated with the tiers in which they intend to bid. The Commission concludes that such an approach is likely to provide further assurance that Phase II auction support will be awarded to qualified bidders. In a future Commission-level public notice after opportunity for further comment, the Commission intends to: 1) specify what evidence or other information must be submitted, 2) establish the conditions for when such information must be submitted, 3) adopt the applicable standards that bidders must demonstrate, 4) set procedures for reviewing and validating the submitted information, and 5) adopt any additional penalties if capabilities are misrepresented.

28. While the Commission already requires that potential bidders make certain showings in their short-form applications, the Commission is not persuaded by claims that this information will offer sufficient assurance that potential bidders are qualified to meet the applicable tier requirements in all circumstances. Instead, given the varying capabilities of the technologies that the Commission expects bidders will propose to use to meet their obligations, it concludes there may be circumstances where it will serve the public interest for the Commission to make an independent, objective decision regarding potential bidders' capabilities and also require bidders to demonstrate they have undergone the necessary due diligence to ensure they can meet the applicable requirements before bidding in particular tiers. The Commission also disagrees with claims that the technical showings it requires in the long-form

application will sufficiently address the Commission's concerns because it will not have access to this information until winning bidders have already been selected.

29. Finally, the Commission rejects suggestions that the Commission intended to adopt the same eligibility process it adopted for the rural broadband experiments or that the Commission would need to reconsider the eligibility requirements it has already adopted in the Phase II Auction Order to require potential bidders to submit additional evidence in their short-form applications. Instead, the Commission made clear that potential bidders would be required to submit any information or documentation required to establish their eligibility for bidding weights adopted by the Commission. Moreover, eligibility considerations are different in the Phase II auction context than they were for the rural broadband experiments. The intent of the rural broadband experiments was to award support to discrete experiments. If a bidder was found to be unqualified after being announced as a winning bidder, the relevant service area would be made eligible for Phase II if the Commission determined that the area remained unserved. By contrast, one of the main objectives of the Phase II auction is to maximize coverage. As the Commission explained above, selecting bidders that are later determined to be unqualified will thwart this objective because the areas included in the unqualified winning bid and other areas covered by bids that would have otherwise been selected will lose an opportunity to be served through the Phase II auction.

30. Although the Commission declines to adopt state-based preferences or ceiling in the Connect America Phase II auction, it is persuaded that it should reserve funding in the Remote Areas Fund for any state that did not receive support equal to the funding declined in the statewide election process, subject to the conditions described below. The Commission continues to recognize the importance of connecting consumers in areas that would have been reached had the Phase II offer been accepted and to provide sufficient universal service funds to do so. Accordingly, the Commission intends to observe the outcome of the Phase II auction, and will adopt a process for the Remote Areas Fund to ensure that states receive an equitable distribution of funds. In order to ensure service is extended expeditiously to areas not supported in the Phase II auction, the Commission also reaffirms that the

Commission will seek to commence the Remote Areas Fund auction no later than one year after the commencement of the Phase II auction.

31. Specifically, once the Commission has had the opportunity to observe the results of the Phase II auction it will prioritize bids in the Remote Areas Fund auction that are placed in such declined states until it has awarded enough support to make up the difference between the total Phase II declined support and the total support that was awarded in the state by the Phase II auction, to the extent possible based on bids placed, remaining eligible areas, and budget available. To ensure that support is targeted to commercially reasonable bids, the Commission anticipates that only bids that are at or below the reserve price would be eligible for this preference. Any implementation details will be adopted when the Commission finalizes the procedures for the Remote Areas Fund auction after observing the outcome of the Phase II auction.

32. The Commission acknowledges that this approach may mean that some areas in declined states have to wait longer to get service than if support was awarded through the Phase II auction. Nevertheless, on balance the Commission concludes this approach serves the public interest because it reasonably enables us to achieve its objectives by first using the Phase II auction to maximize its budget by prioritizing cost-effective bids and then targeting support to areas that remain unserved in the Remote Areas Fund. Indeed, the areas where support has been declined are, according to the Commission's cost model, lower cost than the extremely high-cost areas that are eligible nationwide. While it is possible that some areas that would have received support if the Commission implemented preferences in the Phase II auction may be left unserved after the Phase II auction, it is also possible that bidders will be attracted to serve these lower-cost areas and will be awarded support through the Phase II auction to the extent that they place cost-effective bids when compared to the reserve price and bids nationwide.

33. For these reasons, the Commission concludes that this approach is preferable to adopting weights for the Phase II auction for states where Phase II auction support was declined, or adopting other measures like support thresholds, ceilings, or rankings in the Phase II auction. Instead, the possibility that state preferences in the Phase II auction could divert funding from more cost-effective and higher service

quality bids in the Phase II auction, and the added complexity they would introduce to the Phase II auction, outweigh the potential benefits. The Commission concludes that any inequitable distribution issues would be better addressed after the Phase II auction, after bidders have had the opportunity to place cost-effective competitive bids in all states.

34. The Commission disagrees with commenters that argue that the Commission should not implement any preferences for states where Phase II model-based support was declined. Instead, the Commission has acknowledged that an incumbent price cap carrier's decision to decline Phase II model-based support does not diminish the Commission's universal service obligation to connect consumers in areas that would have been reached had the offer been accepted and to provide sufficient universal service funds to do so. To the extent unserved areas remain in declined states after cost-effective bids have been awarded in the Phase II auction and bidders are willing to serve those areas with support equal to or less than the relevant reserve price, the Commission concludes that it is reasonable to spend at least as much support through the Phase II and Remote Areas Fund auctions that the Commission was willing to spend through the Phase II offer of support to address a similar number of unserved consumers in these states. And as the Commission explained above, it is using this approach as a backstop, once it has had the opportunity to select bids based on cost-effectiveness and service quality through the Phase II auction.

35. The Commission is not persuaded that it should adopt weights or any other kind of preferences for states where the state has either provided state broadband funding or has committed to co-invest funds for winning Phase II auction bids, or where the state is a net payer to the universal service fund. First, as noted above, these proposals would add additional complexity to the Phase II auction, both for the Commission in designing and executing an auction that would incorporate these preferences and for bidders that may face difficulty in putting together a cost-effective bid that accounts for such preferences. Second, if a state has implemented a broadband program, Phase II bidders could use those funds to supplement the funds they are seeking from the federal Connect America program, thereby lowering their bids so that they are more competitive. The state's contribution to a project will already effectively lower the amount of support a bidder needs from the federal universal service fund. Third, the

Commission's universal service programs are designed to target areas where there is not a business case for service providers to offer reasonably comparable services at reasonably comparable rates. By virtue of the geography of each state, some states have more of these areas than others and thus require more support to achieve the Commission's universal service objectives. It would contradict the Commission's statutory responsibility to connect all Americans with reasonably comparable services if the Commission were to target federal universal service support to certain states for the sole reason that their ratepayers contribute more into the universal service fund than the states receive from all disbursement programs in the aggregate.

36. The Commission is not convinced that it should set up a separate mechanism to allocate support directly to declined states—either in lieu of those states participating in the Phase II auction or for those states that do not receive a certain level of support in the Phase II auction—or work in partnership with the states to choose winning projects based on specified criteria. Not only would this cause further delay in getting support to those areas because the Commission would need to establish rules for a new mechanism, it would also contradict its decision to allocate unclaimed Phase II support using market-based mechanisms—the Phase II auction and the Remote Areas Fund auction. For all the reasons explained above, the Commission continues to conclude that requiring bidders to compete for support rather than using more subjective measures to select awardees will lead to a more efficient use of its finite budget.

37. While the Commission acknowledges that it conditionally waived the Phase II auction program rules to make available up to an amount of support that is equivalent to the amount of support Verizon declined in New York to be allocated in partnership with New York's New NY Broadband Program, the Commission did not guarantee that carriers in New York would be awarded the full \$170.4 million if winning bidders were not authorized for this amount by the Commission in coordination with New York's program. Moreover, such support will be allocated to service providers rather than directly to the state. Such bidders are required to compete for funds through New York's broadband program and will only be eligible to be authorized for Phase II support if they are selected as winning bidders and if

New York commits a matching amount of support at the minimum. The Commission also finds that the public interest considerations in that context are different than the considerations here. The Commission's decision to allocate up to \$170.4 million in coordination with New York's program was premised on the fact that New York had committed a significant amount of state support and had already established a program that is compatible with the objectives of Connect America Phase II and that will lead to faster build out and potentially higher speeds than if the Commission had waited for the Phase II auction to allocate the support. Working in partnership with New York also meant that the Commission could eliminate potential overlaps between the two programs that could otherwise thwart the Commission's Connect America objectives. No other state has demonstrated that they have adopted a similar program that would achieve the same or similar public interest benefits.

38. While the Commission remains committed to promoting deployment on Tribal lands, it declines to adopt a Tribal-specific preference for Tribal entities or entities choosing to serve Tribal lands in the Phase II auction. For the reasons described above, the Commission concludes that it serves the public interest to award Phase II support to the most cost-effective bids, subject to the performance and latency weights it adopts above. The Commission's decision to score a bid's cost-effectiveness relative to the reserve price will ensure that service providers that place cost-effective bids that commit to serve Tribal lands will be competitive. Furthermore, the Connect America Cost Model used to set reserve prices already takes into consideration many factors causing varying deployment costs. With this approach, the auction is able to use a market-based mechanism to award support for the purposes of connecting all consumers, including those on Tribal lands. The Commission's action today does not preclude us from adopting preferences for Tribal entities or entities serving Tribal lands in the Remote Areas Fund auction if Tribal lands remain unserved after the Phase II auction and after the Commission has had the opportunity to observe the outcome of the Phase II auction.

39. It is unclear at this time what the effect of a Tribal bidding credit would be given the Commission's decision to adopt weights for service and latency tiers. The Commission concludes that it serves the public interest to maximize its budget by first determining whether the Commission's recent

policy decisions will result in cost-effective competitive bids on Tribal lands in the Phase II auction. If not, the Commission will be able to observe bidders' behavior in the Phase II auction to determine how to best implement a targeted preference that will encourage deployment on Tribal lands that remain unserved.

40. The Commission is not persuaded that Tribal governments should instead select the service providers that will be serving Tribal lands or that Tribally-owned or -controlled carriers should have the right of first refusal. The Commission's paramount goal must be to maximize the value of the universal service dollars it is spending on behalf of consumers—including those on Tribal lands—and creating artificial barriers to competing for support or deploying service on Tribal lands will only serve to delay the build out of high-quality services that rural Americans on Tribal lands want and need. Such an approach would be contrary to the Commission's decision to conduct a competitive bidding process in these areas to select service providers that will efficiently use support to offer reasonably comparable services. Moreover, eligible Tribally-owned or -controlled carriers will have the opportunity to participate in the Phase II auction and potentially win support if they place competitive bids.

41. The Commission concludes that it would not serve the public interest to adopt alternative interim service milestones for non-terrestrial service providers or service providers that already have deployed the infrastructure they intend to use to fulfill their Phase II obligations. The Commission expects that determining whether a recipient has sufficiently built out its network and thus would be subject to the alternative milestones would be a subjective and possibly time-consuming fact-specific inquiry. Also, tracking and verifying different milestones for a subset of Phase II auction recipients that are based on the timing of consumer requests would complicate the Commission and USAC's oversight responsibilities. Additionally, subjecting such providers to more aggressive interim milestones could potentially undermine both their incentives to participate in the Phase II auction and their willingness to take steps to deploy facilities prior to being awarded Phase II auction support.

42. The Commission concludes that these considerations outweigh the public interest benefits of the potential that in some circumstances recipients will offer the required services faster if they have to

meet more aggressive milestones. Indeed, carriers that have deployed infrastructure already have an incentive to meet their obligations quickly. First, carriers will want to supplement universal service support with customer revenue. Second, Phase II auction recipients are required to maintain an open and renewed letter of credit only until they have certified they have met their 100 percent service milestone and that certification has been verified. As a result, Phase II auction recipients may choose to accelerate the rate at which they offer the required services so that they can close out their letter of credit sooner.

III. ORDER ON RECONSIDERATION

43. In this Order on Reconsideration the Commission considers several petitions for reconsideration of decisions made in the Phase II Auction Order. First, the Commission denies a petition for reconsideration of its decision to score bids relative to the reserve price. Second, the Commission grants a petition for reconsideration of its decision to retain the option to re-auction certain areas served by high latency bidders if a set subscription rate is not met. Finally, the Commission grants a petition for reconsideration of its decision to require bidders in the Above-Baseline and Gigabit performance tiers to offer an unlimited monthly usage allowance.

44. Discussion. The Commission declines to reconsider the decision to score bids relative to the applicable reserve price. While one of the Commission's objectives is to maximize the number of locations that are served with its finite budget and ranking bids based on the dollar per location would achieve that goal, the Commission has also made clear that it is focused on adopting an auction design that balances this objective with other goals, including efficiently and effectively allocating support among the states. The Commission concludes that ranking bids relative to the reserve price reasonably balances these objectives.

45. As the Commission explained in the Phase II Auction Order, it made the decision to adopt this bid-to-reserve price ratio methodology to prevent support from disproportionately flowing to those states where the cost to serve per location is, relatively speaking, lower than other states. It is the Commission's statutory duty to support universal service, which includes "[c]onsumers in all regions of the Nation," not just those living in denser areas. By ranking bids relative to the reserve price, the

Commission will be providing an opportunity for bidders across the country to make competitive bids while also working to maximize its available funds by awarding support to the most cost-effective bids nationwide. Awarding support to those areas where there are more locations might mean that the Commission would get “more bang for the buck” by serving more locations with its budget, but that approach might also preclude us from taking advantage of efficiencies in cases where service providers are able to serve areas with fewer locations but with support that is far below the applicable reserve price. While the Commission acknowledges that it could instead choose to award support to denser areas in the Phase II auction and address the remaining areas in the Remote Areas Fund auction, it concludes that on balance the public interest will be served by giving consumers nationwide the opportunity to be served sooner if cost-effective bids are placed in those areas. The Commission notes that its decision to cap reserve prices for extremely high-cost areas will help ensure that its budget is not disproportionately diverted to these extremely high-cost areas. Support will only be awarded to service providers that can make a business case to serve these areas with support below the capped amount and that submit cost-effective bids relative to other bids nationwide.

46. The Commission reconsiders the Commission’s decision with regard to re-auctioning areas served by high latency bidders where there is low subscribership. Instead, all authorized Phase II auction recipients will have a full 10-year term of support if they comply with the terms and conditions of Phase II support. While the Commission had adopted the subscriber standard to give high latency providers something objective and quantifiable that they could track to determine if the areas they serve would be placed in the Phase III auction, after further reflection, the Commission is persuaded that this approach does not necessarily reflect the quality of that service or the value to consumers.

47. First, the Commission agrees that it may be difficult for high latency service providers to obtain enough subscribers to meet the 35 percent threshold given that by the end of the third year of support, Phase II auction recipients will only be required to offer service to 40 percent of the required number of locations and may not have focused on adoption efforts while working on deploying their networks. And even if the Commission were to push this option to later in the support term, it would be

difficult to determine an appropriate timeframe at this point without knowing the timing for any subsequent auctions. Second, consumers may decide not to subscribe to a service for any number of reasons, and the Commission is persuaded by comments that suggest that many of the factors that are related to low adoption are likely to be present in more rural high-cost areas of the country.

48. While commenters suggest that they have had success in encouraging broadband adoption in high-cost areas, they do not address the Commission's timing concerns. Moreover, such a general statement about their success does not provide us with adequate assurance that high latency providers would have the same experience in the areas they are awarded support absent service quality issues. In fact, if the Commission uses a low adoption rate as the measure to determine if service is meeting consumers' needs, it would seem to follow that the Commission should also re-auction areas served by low latency service providers that have low subscribership. For these reasons, the Commission concludes that subscribership is not an appropriate measure for determining whether a high latency service is meeting the needs of consumers.

49. The Commission is also sympathetic to claims that even if it were to come up with an alternative objective and quantifiable standard, by simply retaining the option to shorten a high latency service provider's support term it will create uncertainty for such bidders. The Commission would be asking high latency providers to commit significant resources to deploy at a minimum 40 percent of their network while reserving the option to take away their support and potentially fund a competitor in that same area. Such conditions may mean that high latency providers will not participate in the auction or will inflate their bids to compensate for the risk, which would undermine the Commission's decision to include high latency providers in the Phase II auction to maximize the budget by increasing competition.

50. On balance, the Commission is persuaded that these harms outweigh the public interest benefits of having the opportunity to include areas served by high latency bidders in a subsequent auction prior to the end of the 10-year term. As the Commission discussed above, it acknowledges that some parties have significant concerns about whether high latency services will meet the needs of consumers. Nevertheless, the Commission concludes that the performance standards it has adopted for high latency

bidders will offer sufficient protection to consumers living in areas served by a high latency bidder. Moreover, as the Commission explains above, recognizing these concerns it has adopted weights that give a preference to low latency bids to achieve a reasonable balance between using its budget cost-effectively to maximize the deployment of service to unserved consumers with service quality. The Commission concludes that the potential that it would undermine competition by retaining the option to re-auction certain service areas could throw off this balance and potentially thwart its ability to leverage the Phase II auction to further the Commission's statutory objective of supporting reasonably comparable services nationwide within its finite budget.

51. In order to encourage robust bidding, the Commission grants Verizon's request for reconsideration of the Commission's prior decision to require bidders in the Above-Baseline and Gigabit performance tiers to offer an unlimited monthly usage allowance. Instead, the Commission will require bidders in these tiers to offer a monthly usage allowance of at least 2 terabytes (TB) per month.

52. As Verizon explains, a requirement of unlimited data could discourage bidding on those tiers, because a potential bidder would have to factor in additional investments and operating expenses to accommodate a small number of customers whose very high usage would be responsible for a disproportionate share of demand. Rather than require unlimited usage, Verizon argues that the Commission could set a very high allowance, which would provide a greater usage allowance than the baseline tier but still permit providers to address true outliers that increase the cost of providing rural broadband service. The Commission is persuaded by Verizon's argument that requiring bidders to offer unlimited usage would raise the cost of providing higher performance services in rural areas and could discourage bidding in these tiers.

53. Therefore, instead of requiring bidders in the Above-Baseline and Gigabit performance tiers to offer unlimited data allowances, the Commission will require bidders in these tiers to offer a monthly usage allowance of at least 2 terabytes (TB) per month. The Commission finds that a 2 TB usage allowance is sufficiently high to ensure that rural America is not left behind, and will enable more bidders to offer higher performance services in rural areas. Although Verizon originally suggested that

recent urban rate survey data shows that many urban providers have usage limits for services of 100 Mbps or more that range from 250 GB to 1,000 GB (1 TB) per month, it more recently suggested a usage allowance of 1 TB per month. Verizon cited usage limits from last years' urban rate survey data, and the Commission finds it reasonable to adopt a higher usage limit for a 10-year term of support. A data allowance of 250 GB was the lower end of the range for comparable services from this year's urban rate survey data. The Commission therefore disagrees with WISPA's suggestion that a usage tier of only 250 GB for the Above-Baseline tier is sufficient for a 10-year support term. Nor does the Commission agree with WISPA's argument there should not be any usage limits for the Gigabit tier. WISPA did not raise any substantive arguments to counter Verizon's arguments about the additional costs of requiring unlimited usage in high-cost areas. The Commission is therefore persuaded that an unlimited usage cap could impose additional costs on bidders that may discourage them from offering services that exceed its Baseline performance requirements in rural areas. As always, Phase II winners will be free to offer an array of service plans, including those with unlimited usage.

IV. PROCEDURAL MATTERS

54. This document does not contain new information collection requirements subject to the PRA. In addition, therefore, it does not contain any new or modified information collection burden for small business concerns with fewer than 25 employees, pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, see 44 U.S.C. 3506(c)(4).

55. As required by the Regulatory Flexibility Act of 1980 (RFA) as amended, an Initial Regulatory Flexibility Analyses (IRFA) was incorporated in the Further Notice of Proposed Rulemaking adopted in November 2011 (USF/ICC Transformation FNPRM, 76 FR 78384, December 16, 2011), the Further Notice of Proposed Rulemaking adopted in July 2014 (Rural Broadband Experiments FNPRM, 79 FR 44352, July 31, 2014), and the Further Notice of Proposed Rulemaking adopted in May 2016 (Phase II Auction FNPRM). The Commission sought written public comment on the proposals in the USF/ICC Transformation FNPRM, the State Action FNPRM, and the Phase II Auction FNPRM,

including comment on the IRFAs. The Commission did not receive any relevant comments in response to these IRFAs. This Final Regulatory Flexibility Analysis (FRFA) conforms to the RFA.

56. With this Report and Order and Order on Reconsideration (Order), the Commission takes another step towards implementing the Connect America Phase II (Phase II) auction in which service providers will compete to receive support of up to \$1.98 billion to offer voice and broadband service in unserved high-cost areas. The decisions the Commission makes in this Order aim to maximize the value the American people will receive for the universal service dollars it spends, balancing higher-quality services with cost efficiencies.

57. First, the Commission resolves issues raised in the Phase II Auction Order FNPRM. The Commission adopts weights to compare bids among the service performance and latency tiers adopted in the Phase II Auction Order. Additionally, the Commission declines to adopt specific preferences for certain states and Tribal lands in the Phase II auction and decline to adopt alternative interim deployment obligations for a subset of Phase II auction recipients. However, the Commission does adopt preferences that will be implemented in the Remote Areas Fund auction for states where the Phase II offer of model-based support was declined, subject to conditions.

58. Second, the Commission also considers several petitions for reconsideration of decisions made in the Phase II Auction Order. The Commission denies a petition for reconsideration of the Commission's decision to score bids relative to the reserve price and grant a petition for reconsideration of the Commission's decision to retain the option to re-auction certain areas served by high latency bidders if a set subscription rate is not met.

59. The RFA directs agencies to provide a description of, and where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted. The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction." In addition, the term "small business" has the same meaning as the term "small-business concern" under the Small Business Act. A small-business concern"

is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).

60. Total Small Entities. The Commission's proposed action, if implemented, may, over time, affect small entities that are not easily categorized at present. The Commission therefore describes here, at the outset, three comprehensive, statutory small entity size standards. First, nationwide, there are a total of approximately 28.2 million small businesses, according to the SBA, which represents 99.7% of all businesses in the United States. In addition, a "small organization" is generally "any not-for-profit enterprise which is independently owned and operated and is not dominant in its field." Nationwide, as of 2007, there were approximately 1,621,215 small organizations. Finally, the term "small governmental jurisdiction" is defined generally as "governments of cities, towns, townships, villages, school districts, or special districts, with a population of less than fifty thousand." Census Bureau data for 2011 indicate that there were 90,056 local governmental jurisdictions in the United States. The Commission estimates that, of this total, as many as 89,327 entities may qualify as "small governmental jurisdictions." Thus, the Commission estimates that most governmental jurisdictions are small.

61. The Report and Order and Order on Reconsideration do not impose any specific reporting, recordkeeping, or compliance requirements for entities, including small entities. Instead, the Report and Order adopts or declines to adopt measures that will affect all bidders participating in the Phase II auction. For example, the Report and Order adopts weights for the Phase II auction technology-neutral service and latency tiers, and indicates that the Commission will seek comment on requiring potential bidders to establish their eligibility for such weights. The Report and Order declines to take further action to give a preference to certain states, Tribal bidders, or other types of bids in the Phase II auction. However, the Report and Order does adopt a preference for certain states in the Remote Areas Fund auction where the Phase II offer of model-based support was declined, subject to conditions. The Report and Order also declines to subject entities that have already deployed a network capable of meeting their Phase II obligations to different interim build-out milestones than the interim build-out milestones that were adopted in the Phase II Auction Order.

62. The Order on Reconsideration declines to reconsider the Commission's decision to score bids relative to the reserve price by instead ranking bids on a dollar-per-location basis. In the Order on Reconsideration the Commission also decides that all Phase II auction recipients will have a 10-year support term, thereby reconsidering the Commission's decision to retain the option to shorten the support term of certain high latency bidders that are unable to meet a set subscribership threshold.

63. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include (among others) the following four alternatives: (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities. The Commission has considered all of these factors subsequent to receiving substantive comments from the public and potentially affected entities. The Commission has considered the economic impact on small entities, as identified in comments filed in response to the USF/ICC Transformation FNPRM, the Rural Broadband Experiments FNPRM and the Phase II Auction FNPRM and their IRFAs, in reaching its final conclusions and taking action in this proceeding.

64. Generally, the decisions that the Commission makes in this Order will apply in equal force to all Phase II auction bidders, including small bidders. Thus, the decisions made in this Order generally do not impose unique burdens or benefits on small bidders. For example, the Commission's decision to adopt weights for the performance and latency tiers that will not grant an absolute preference to any kind of service is unlikely to uniquely impact small bidders, but it is likely to help maximize participation by making it possible for all entities, including small entities, to be competitive if they place a cost-effective bid. Additionally, like all bidders in the Phase II auction, to the extent smaller bidders choose to bid in less populated areas, they may benefit from the Commission's decision to retain a bid ranking method that will score bids relative to the applicable reserve price rather than a dollar per location basis.

65. In the Order, the Commission does decline to adopt proposals for other weights or preferences in the Phase II auction, including a preference specifically for small entities. The Commission concludes that such an approach would not further its objective of maximizing the effectiveness of its funds to serve consumers nationwide. Nevertheless, recognizing the important role that small entities can play in bringing voice and broadband services to unserved consumers, the Commission has already adopted specific eligibility requirements for the Phase II auction in an effort to facilitate the participation of small entities.

66. The Commission also indicates in the Order that it is persuaded that in some circumstances it may serve the public interest to require potential bidders to submit evidence that demonstrates that they can meet the service requirements associated with the tiers in which they will bid in their short-form applications. The Commission will seek comment on this issue and will consider the unique challenges faced by small entities in submitting any required information.

V. ORDERING CLAUSES

67. Accordingly, IT IS ORDERED, pursuant to the authority contained in sections 4(i), 214, 254, 303(r), 403, and 405 of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), 214, 254, 303(r), 403, and 405, and sections 1.1, 1.427, and 1.429 of the Commission's rules, 47 CFR 1.1, 1.427, and 1.429, that this Report and Order and Order on Reconsideration IS ADOPTED, effective thirty (30) days after publication of the text or summary thereof in the Federal Register. It is the Commission's intention in adopting these rules that if any of the rules that the Commission retains, modifies or adopts herein, or the application thereof to any person or circumstance, are held to be unlawful, the remaining portions of the rules not deemed unlawful, and the application of such rules to other persons or circumstances, shall remain in effect to the fullest extent permitted by law.

68. IT IS FURTHER ORDERED that, pursuant to section 1.429 of the Commission's rules, 47 CFR 1.429 the Petition for Reconsideration filed by Verizon on August 8, 2016 is DENIED IN PART to the extent described herein.

69. IT IS FURTHER ORDERED that, pursuant to section 1.429 of the Commission's rules, 47 CFR 1.429 the Petition for Reconsideration filed by ViaSat, Inc. on August 8, 2016 is GRANTED IN PART to the extent described herein.

70. IT IS FURTHER ORDERED that the Commission SHALL SEND a copy of this Report and Order to Congress and the Government Accountability Office pursuant to the Congressional Review Act, see 5 U.S.C. 801(a)(1)(A).

FEDERAL COMMUNICATIONS COMMISSION.

Marlene H. Dortch

Secretary.

[FR Doc. 2017-05468 Filed: 3/20/2017 8:45 am; Publication Date: 3/21/2017]