



FCC USF/ICC Order Workshop

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USF Reform



VantagePoint

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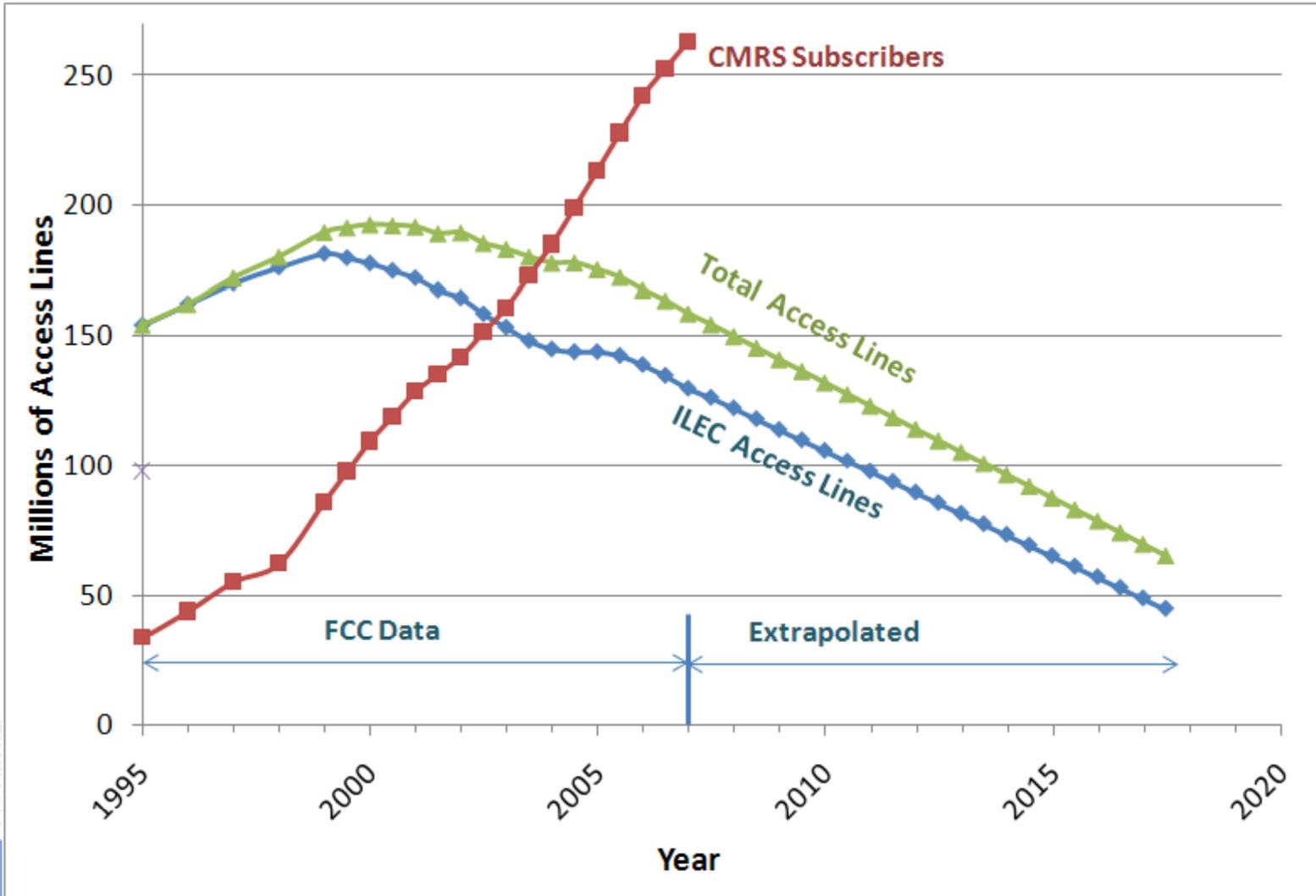
GM After Reading FCC Order



FCC Reform Sunrise or Sunset



POTS vs. Wireless



End-User Telco Industry Revenues



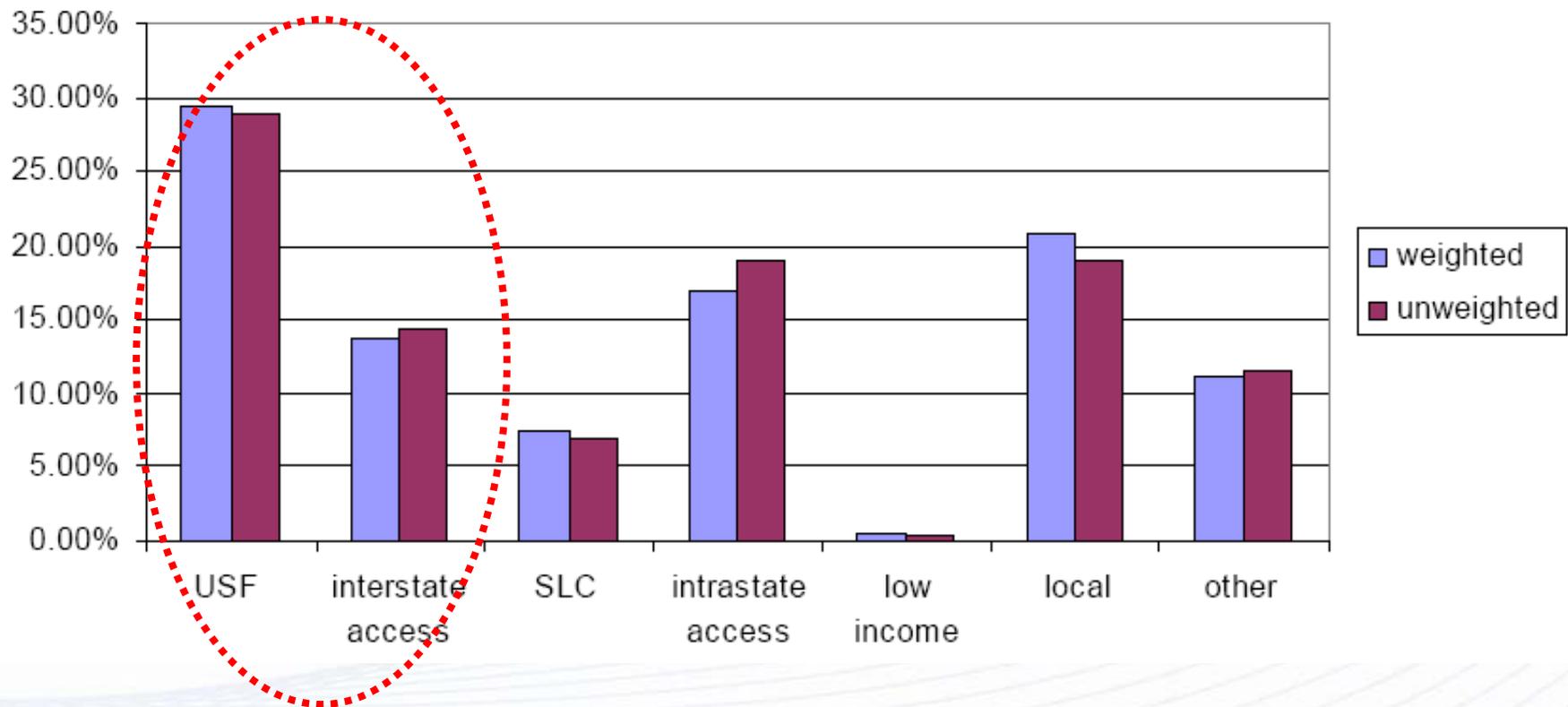
	2003	2004	2005	2006	2007	2008	2009	2010
Toll Service	\$59.0	\$55.5	\$52.4	\$49.3	\$48.7	\$47.3	\$43.2	\$40.7
Mobile Service	\$85.3	\$94.4	\$100.7	\$110.1	\$115.9	\$118.9	\$113.9	\$110.9
Local Service	\$86.5	\$83.4	\$82.4	\$78.2	\$75.0	\$72.5	\$68.5	\$64.9

*In Billions of Dollars

Source: FCC's Industry Analysis and Technology Division, Wireline Competition Bureau, released May 2011



Current Rural ILEC Revenue Sources¹



¹ OPASTCO White Paper: "The Next Three Years: Likely Revenue Scenarios for Rural Incumbent Local Exchange Carriers" prepared by Dale Lehman

FCC RoR Impact Estimates



- Based on calendar year 2010 support levels FCC estimates following RoR carrier support impacts:
 - 70% will see reductions less than 10% annually
 - 10% will see reduction greater than 20% annually
 - 34% will see no reductions
 - 12% will see increase in support
 - Where will your company fall?

Connect America Fund Budget



- Annual CAF funding target = FY2011
- \$4.5B target until Commission changes
 - \$500M – Mobility Fund
 - \$100M reserved for Tribal Lands
 - \$100M – Remote Areas Fund
 - \leq \$1.8B – Price Cap Carriers after transition
 - \leq \$2B – RoR Carriers

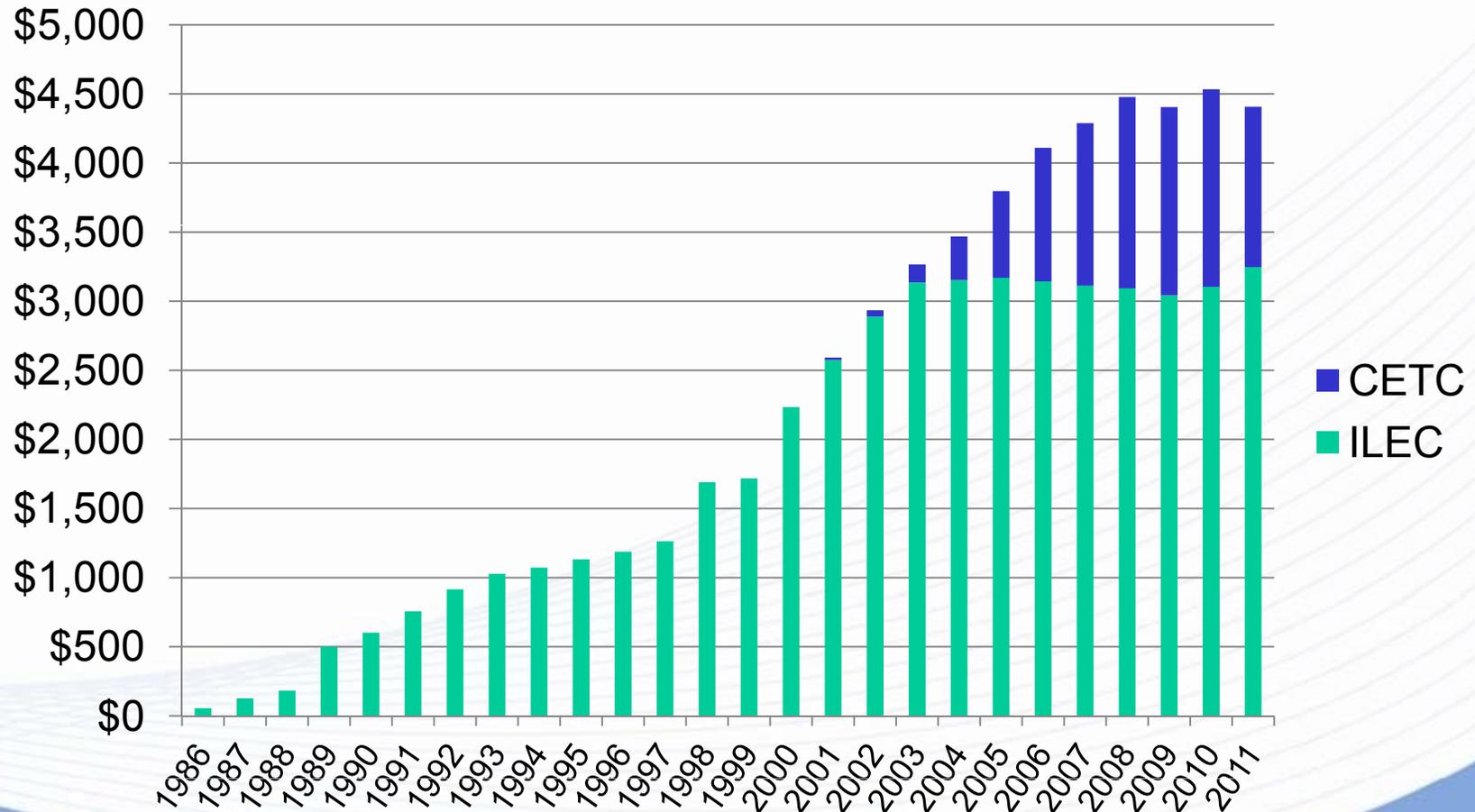


\$4.5B Annual Cap Through 2017

Growth of High Cost Fund



\$ in Millions



Public Interest Obligations



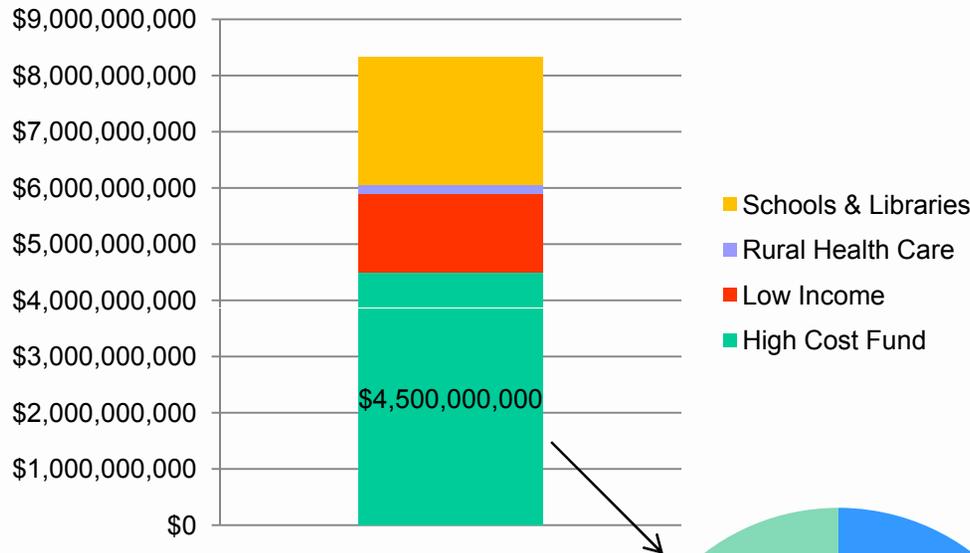
- ETCs must now offer BB in addition to voice
 - At least 4 Mbps downstream and 1 Mbps upstream, upon reasonable request from their customer
 - Provide latency suitable for real-time apps (i.e. VOIP)
 - Provide capacity comparable to urban R1 fixed BB
 - Provide new annual monitoring report on voice and BB services
- ETCs required to report annually number of unfilled requests for service and number of customer complaints



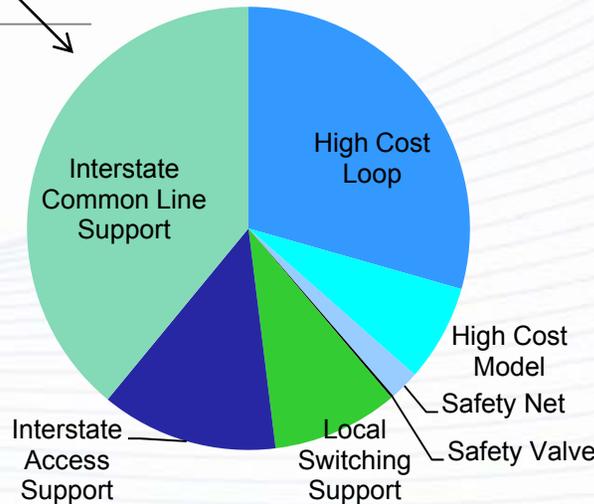
Universal Service Fund

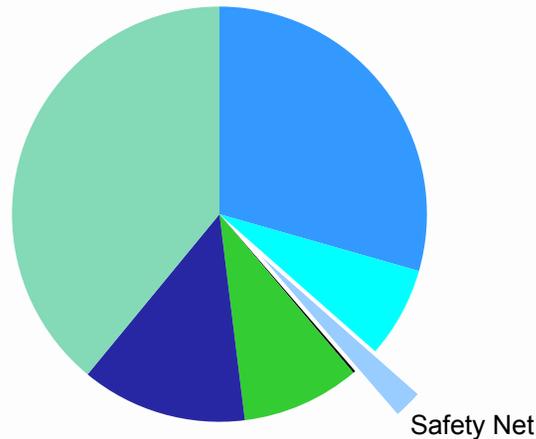


Total Universal Service Fund (USF)



- \$8B in 2011
 - \$4.5B High Cost Fund
 - high-cost loop support
 - safety net
 - safety valve
 - local switching
 - interstate common line
 - high cost model
 - interstate access



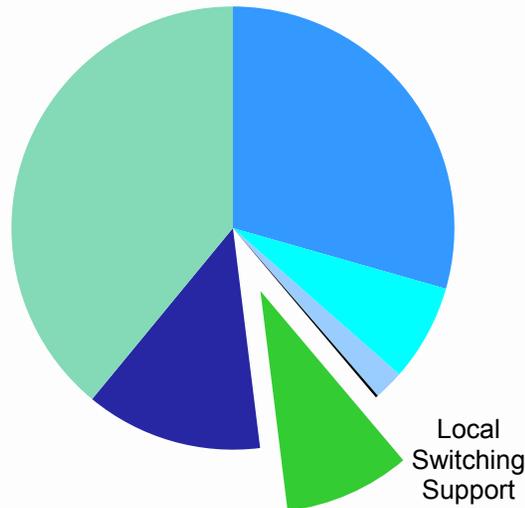


Safety Net

- 2011 - \$62 Million (RoR)
- Phased out over time for all RoR
- No Safety Net for costs incurred after 2009
- Existing recipients
 - TPIS per line increased by more than 14% will continue to receive SNA per your current schedule
 - TPIS per line not increased by more than 14% (assumed to be line loss) - SNA reduced by 50% in 2012 & eliminated in 2013



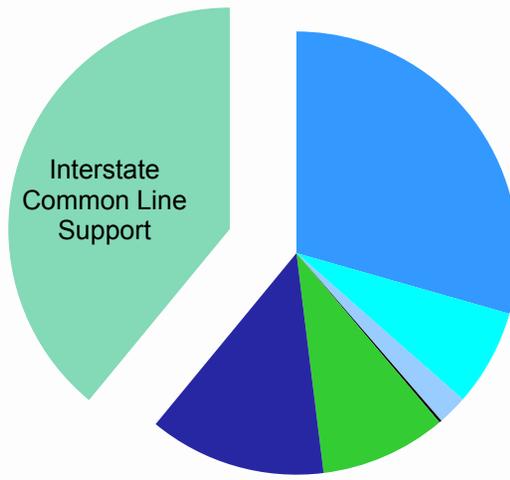
Local Switching Support



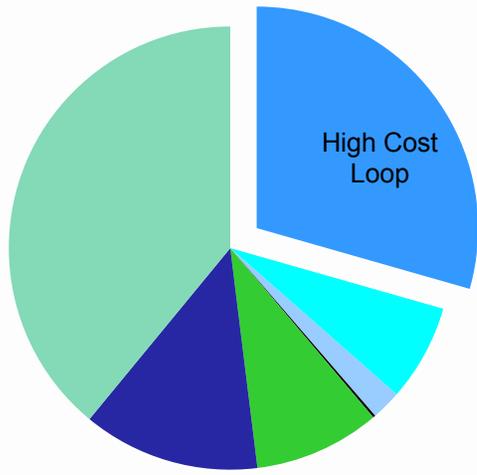
- 2011 - \$238 Million (RoR)
- January 1-June 30, 2012 LSS payments frozen at 2011 support levels subject to true-up based on 2011 operating results
- Beginning July 1, 2012 LSS eliminated and moved into RM



Interstate Common Line Support



- 2011 - \$933 Million (RoR)
- Existing corporate operations expense limits extended to ICLS
 - effective January 1, 2012



High Cost Loop



- 2011 - \$810 Million (RoR)
- Adjusted High Cost Loop Cap for 2012
 - Reduced by amount that price cap companies would have received in 2012
- Reduce HCL support dollar-for-dollar for carriers below benchmark R1 voice rates
 - \$10 between July 1, 2012 and June 30, 2013
 - \$14 between July 1, 2013 and June 30, 2014
 - Thereafter based on annual survey (est \$15.62)

Corporate Operating Expense Caps



- Existing corporate operations expense limits revised for HCLS and extend to ICLS
 - Effective January 1, 2012
- Corporate operations expenses include
 - Overall administration & management
 - Accounting & financial services
 - Legal services
 - Public relations





HCL Modeling Limits

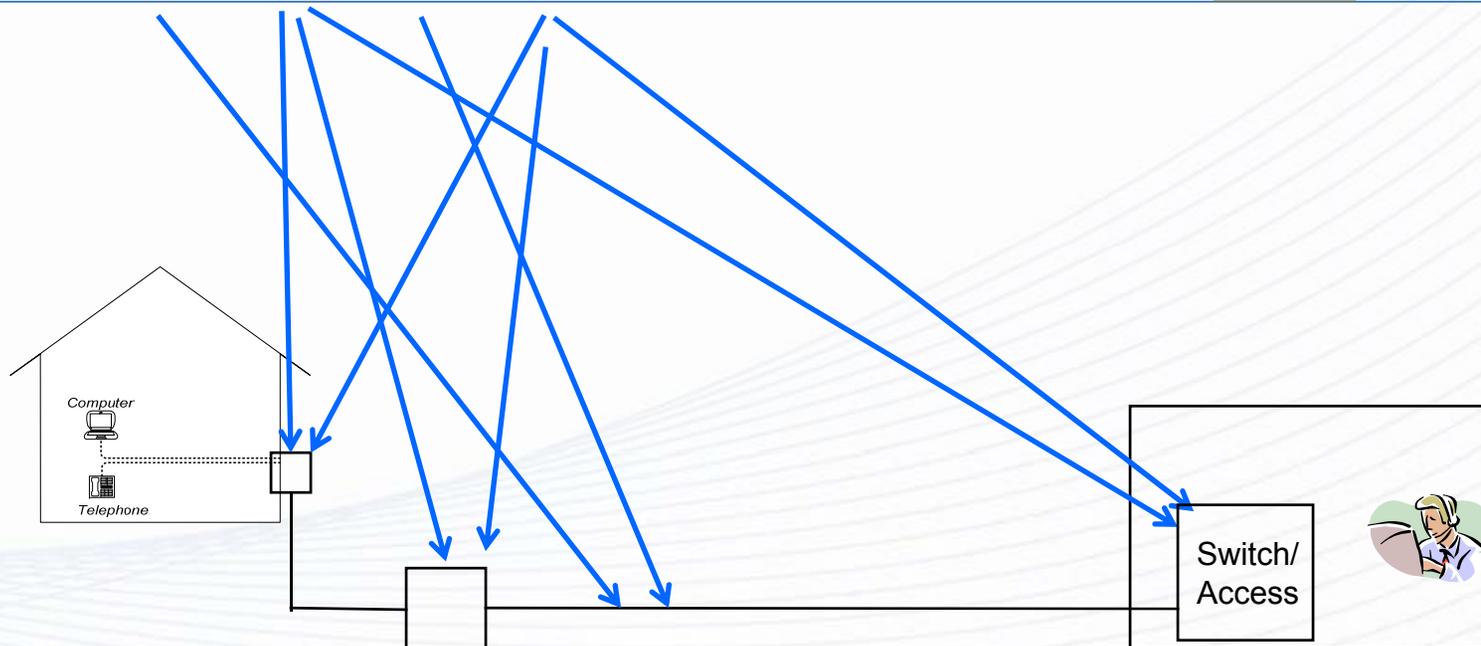
- Limits on Reimbursable Capital & Operating Costs based on new FCC regression formula
 - Implemented no later than **July 1, 2012**
 - Carrier amounts above 90% reduced to 90%
- CapEx Caps
 - Loop cable, loop electronics, and associated depreciation expense
- OpEx Caps
 - Material & Supplies, maintenance expense, network expense and general support expense





Cap Ex Accts via Network

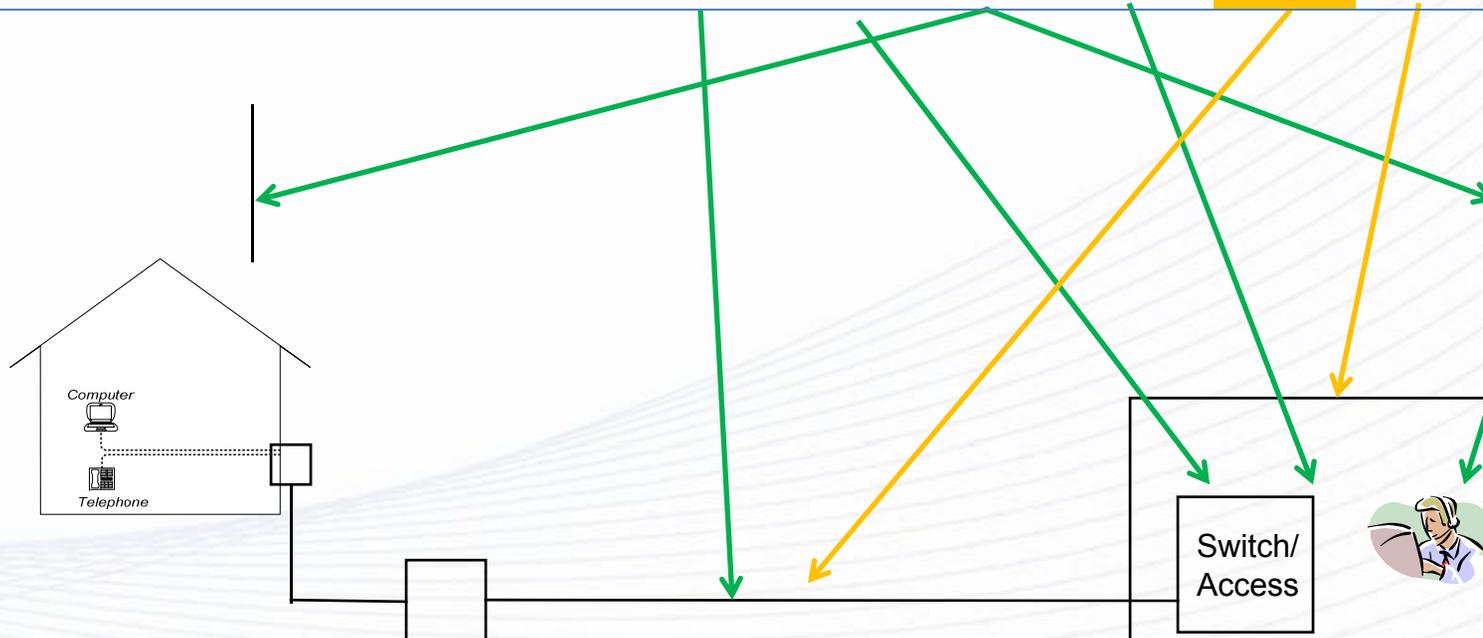
Src	CFW	COE	M&S CWF	M&S COE	CFW Maint	COE Maint	Net Sup + GSE	Net Ops	Depr CWF	Depr COE	Benefits
Act	6327	1353	34	7	48	44	36	19	397	67	47
Mdl	6821	1777	91	22	137	92	75	89	344	146	129
Use	6327	1353	34	7	48	44	36	19	344	67	47



Expense & Dept Accts



Src	CWF	COE	M&S CWF	M&S COE	CWF Maint	COE Maint	Net Sup + GSE	Net Ops	Depr CWF	Depr COE	Benefits
Act	6327	1353	34	7	48	44	36	19	397	67	47
Mdl	6821	1777	91	22	137	92	75	89	344	146	129
Use	6327	1353	34	7	48	44	36	19	344	67	47



Regression Analysis Impact - Example



Src	CWF	COE	M&S CWF	M&S COE	CWF Maint	COE Maint	Net Sup + GSE	Net Ops	Depr CWF	Depr COE	Benefits
Act	6327	1353	34	7	48	44	36	19	397	67	47
Mdl	6821	1777	91	22	137	92	75	89	344	146	129
Use	6327	1353	34	7	48	44	36	19	344	67	47

Regression Breakout - Example



<u>Algorithm Step</u>	<u>Description</u>	<u>Actual Per Loop</u>	<u>Capped Per Loop</u>	<u>Reimbursable Per Loop</u>	<u>Actual Costs</u>	<u>Capped Costs</u>	<u>Reimbursable Costs</u>
1	Cable & Wire Facilities assigned to Category 1	\$6,327	\$6,821	\$6,327	\$26,199,347	\$28,245,761	\$26,199,347
2	Central Office Equipment assigned to Category 4.13	1,353	1,777	1,353	5,601,422	7,358,557	5,601,422
7	Materials & Supplies assigned to C&WF Cat 1	34	91	34	139,151	376,831	139,151
8	Material & Supplies assigned to COE Cat 4.13	7	22	7	29,750	91,102	29,750
9	Accumulated Depreciation assigned to C&WF Cat 1				6,752,669	7,280,118	6,752,669
10	Accumulated Depreciation assigned to COE Cat 4.13				3,151,469	4,140,067	3,151,469
13	C&WF Maintenance Expense assigned to Cat 1	48	137	48	198,509	567,317	198,509
14	COE Maintenance Expense assigned to Cat 4.13	44	92	44	184,008	380,972	184,008
15	Network Support Exp plus General Support Exp to Cat 1 & 4.13	36	75	36	148,201	310,575	148,201
16	Network Operations Expenses assigned to Cat 1 & 4.13	19	89	19	77,752	368,549	77,752
17	Depreciation and Amortization Expense to C&WF Cat 1	397	344	344	1,644,719	1,424,504	1,424,504
18	Depreciation and Amortization Expense to COE Cat 4.13	67	146	67	278,201	604,586	278,201
19	Corporate Operations Expense assigned to Cat 1 & 4.13				527,888	591,027	527,888
20	Operating Taxes assigned to Cat 1 & 4.13				204,616	229,089	204,616
21	Benefits other than Corporate Operations Exp to Cat 1 & 4.13	47	129	47	196,152	534,189	196,152
22	Rents assigned to Cat 1 & 4.13				24,610	27,553	24,610
23	Return Component for C&WF Category 1				2,203,406	2,401,028	2,203,406
24	Return Component for COE Category 4.13				278,967	372,329	278,967
25	Total Unseparated Costs (Sum 13 through 24)				5,967,029	7,811,718	5,746,814
26	Study Area Cost per Loop				\$1,440.96	\$1,886.43	\$1,387.78
	National Average Cost per Loop				\$505.97	\$505.97	\$505.97
	Total Annual High Cost Loop Support				\$2,579,748	\$3,955,248	\$2,415,564
	Reduction in High Cost Loop Support						(164,184)

Limits on Total per Line High Cost Support



- Monthly \$250 per access line cap, with a 3 yr. phase down to cap if you exceed cap
 - **July 1, 2012 - June 30, 2013** \$250 per line plus 2/3 difference between uncapped per line and \$250
 - **July 1, 2013 - June 30, 2014** \$250 per line plus 1/3 difference between uncapped per line and \$250
 - **July 1, 2014** capped at the monthly \$250 per access line
- Currently 18 ILECs exceed limit



Other High-Cost Rule Changes

- Study Area Waiver
 - Streamlined basis granted within 60 days of the close of the comment and reply process for waiver
- “Parent Trap” Rule
 - Modified due to the freezing of support for price cap carriers
 - Effective **January 1, 2012**, the acquiring company will receive the lesser of the price cap carrier’s frozen support or its own actual costs



Elimination of Support in Areas with 100% Overlap

- Phase out support
 - In study areas that overlap **completely** an unsubsidized facilities-based terrestrial competitor providing voice/fixed BB service
 - at least 4 Mbps downstream/1 Mbps upstream
 - How will fixed wireless be treated?
 - Areas not completely overlapped reviewed in FNPRM
- Freeze incumbent's high cost support
 - At 2010 support or \$3,000/line
 - whichever is lower
 - Then reduce by 33% per year for 3 years

Identical Support Rule



- Eliminate the rule effective Jan. 1, 2012
 - Includes CETC wireline and wireless providers
- Five year reduction starting July 1, 2012
 - Baseline support = lesser of total 2011 support or \$3,000/AL
 - Reduced to 80% July 1, 2012 – June 30, 2013
 - 60% July 1, 2013 – June 30, 2014
 - 40% July 1, 2014 – June 30, 2015
 - 20% July 1, 2015 – June 30, 2016
 - No support after July 1, 2016

Remote Areas Fund



- Order establishes the annual budget
 - At least \$100 million per year allocated
- Relaxed BB performance obligations
 - Encouraging alternative technology platforms
- FNPRM seeks comment on implementation
 - Program structure
 - Remote area determination (should be some in IN)
 - Provider qualifications
 - Public interest obligations
- Goal to be implemented by year end 2012



Petitions for Waivers

- Case by case explicit waiver mechanism
 - FCC does not expect to grant waivers routinely
 - Rigorous and thorough review, similar to a total company earnings review
- Authority to review/grant in WCB and WTB
- Petitions placed on Public Notice
 - Minimum of 45 days provided for comments and reply comments

Petition for Waiver (cont.)



A petition for waiver must include, but is not limited to:

- Density characteristics of the study area
- Information regarding alternative providers
- Part 32 account and 36 separations category for spare equipment
- Corporate operation expense details (corporate salaries, # of employees, nature of any overhead expenses allocated from affiliated or parent companies, or other expenses)
- All end user rate plans
- Additional services provided over the supported plant (video or Internet)
- Procedures allocating shared costs
- Most recent three years of audited financials and applicable notes
- Detailed information regarding outstanding loans
- Identification of specific facilities that will be taken out of service absent the waiver

Petitions for Waivers (cont.)



- Carrier must demonstrate reduction in support would:
 - Put consumers at risk of losing voice service
 - No alternative terrestrial providers available to provide voice
 - Cause a provider to default on existing loans and/or become insolvent
 - Very hard standard

Enforcing Universal Service Budget



- FCC grants USAC greater flexibility to manage demand fluctuations
 - To eliminate past dramatic changes
- To set quarterly demand to meet budget
- Draw down Corr Wireless reserve account as a cushion if needed





Accountability and Oversight

- States continue existing role in designating and monitoring ETCs – Except FCC ETCs
- Modifies and extends existing federal reporting requirements to all ETCs (Ross)
- Created new section 54.313 for annual reporting
 - Includes existing plus new requirements
- WCB and WTB granted authority to determine the form in which recipients must report the information – forms still to come



Accountability and Oversight (cont.)

- Elimination of separate certifications for IAS/ICLS after **December 31, 2012**
- New section 54.314, states and federally-designated ETCs certifications
 - Due to Commission by October 1 each year (beginning 2012)
 - All federal high-cost and CAF support
 - Used for provision, maintenance, and upgrading of facilities and services for which the support is intended
 - used in the preceding calendar year
 - will be used in the new calendar year



Accountability and Oversight (cont.)

- Failure to meet all requirements
 - Reasons:
 - Untimely filed reports and certifications
 - Not meeting public interest obligations
 - May not necessarily result in a total loss of support
 - Each quarter filing is late will result in lost support for additional quarter
 - On or before Jan 1 – receive support Q2, Q3 & Q4
 - On or before Apr 1 – receive support Q3 & Q4
 - On or before July 1 – receive support Q4
 - After July 1 – no support for that year
 - Debarment possible for those convicted of crime or found civilly liable for defrauding govt.



Accountability and Oversight (cont.)

- Revise record retention period to 10 years
- Direct USAC to annually assess compliance
 - ETCs subject to random compliance audits and other investigations
 - USAC right to obtain information submitted to NECA
- Anticipate USAC and NECA to submit summary filing to Commission on regular basis
- FCC seeking comment on the appropriateness of additional enforcement mechanisms

ROR USF Reform Timeline



Task	Due Date	Fund
ICC - all interstate access rate elements, originating/terminating rates and recp comp and intrastate terminating capped at 2011 levels	12/29/2011	ICC
Begin billing VoIP traffic at rates specified in Order (for usage dates of 12/29/11 forward)	12/29/2011	ICC
IntraMTA rule strictly enforced (billing/recording issues)	12/29/2011	ICC
Phantom Traffic rules implemented - requires all carriers to pass CPN and call signal information in call record	1/1/2012	ICC
Safety Net Additive reduced by 50% in 2012 if due to lost access lines, if not, receive remainder of current SNA per schedule	1/1/2012	CAF
Identical Support eliminated - no new support and existing phased out over 5 year with transition to CAF beginning July 1, 2012	1/1/2012	CAF
Local Switching Support payments frozen at 2011 support levels between January 1, 2012 and June 30, 2012 - subject to true-up based on 2011 operating results	1/1/2012	CAF
Corporate Operations expense cap revised for HCLS and new for ICLS	1/1/2012	CAF
Parent Trap Rule - acquiring company will receive lesser of price cap carrier's frozen support or it's own actual costs	1/1/2012	CAF
Annual ETC progress report filing	4/1/2012	CAF
Annual Audit report filing (** FCC may change this reporting date in order to provide sufficient time once PRA approval is obtained) - May file RUS reports in lieu of audited financial statement	4/1/2012	CAF
Report all flat rates for residential local service and state fees	4/1/2012	CAF
Certify in annual access tariff filing that CAF ICC requirements were met	4/1/2012	ICC
ICLS - final certification	6/30/2012	CAF

ROR USF Reform Timeline



Task	Due Date	Fund
Local service rate floor \$10 between July 1, 2012 and June 30, 2013 *Includes local R1 end user rate, state SLC and/or state USF fee, mandatory extended area service (EAS) charges, other state mandated fees - HCLS reduced \$ for \$ if under	7/1/2012	CAF
Local Switching Support eliminated - moved to RM	7/1/2012	CAF
Overlapped by unsubsidized facilities-based terrestrial competitor - support phased out over 3 years	7/1/2012	CAF
High Cost Support - capped at \$250 per month support per line phased in over 3 years	7/1/2012	CAF
Required broadband speed of at least 4Mbps down/1Mbps up	7/1/2012	CAF
Capital and operational expense recovery limitations implemented	7/1/2012	CAF
Existing CETC support reduced to 80%	7/1/2012	CAF
CMRS/LEC IntraMTA recp comp moves to Bill and Keep (unless an interconnection agreement is in effect then rate applies to end of agreement)	7/1/2012	ICC
Intrastate terminating rates reduced by 50% of difference between intrastate and interstate rates	7/1/2012	ICC
ARC - Residential and single line business rates - maximum of \$0.50 per line month (\$30 Residential Rate Ceiling)	7/1/2012	ICC
ARC - Multi line business rates - maximum of \$1.00 per line	7/1/2012	ICC
Recovery Mechanism - Baseline RM calculated and reduced by 5%	7/1/2012	ICC
Mobility Fund Phase I reverse auction target date - 3rd Quarter 2012	7/1/2012	CAF

FNPRM: CAF for RoR Carriers



- Seek comment on Appendix G (Rural Associations' Proposal)
 - Budgetary framework
 - Benefits/costs of providing Middle Mile / Internet backbone support
 - Impact on USF for RoR if offer standalone BB
 - Transitional Stability Plan mechanism
 - Metrics and/or build-out milestones

USF High Cost Fund Contributors



Most providers of Interstate Telecommunications Services including, but not limited to:

- Wireless telephony
- Paging & messaging services
- Dispatch services
- Mobile radio services
- Operator services
- Access to Interexchange services
- Special access
- Wide Area Telecommunication Services
- Subscriber toll free services
- 900 services
- Message telephone services
- Telex
- Telegraph
- Video services
- Satellite services
- Resale services
- Interconnected VoIP providers



The FCC Plan – The Good

- Maintains RoR regulation (except for ICC)
- Preserves existing \$2B in USF support for 6 years
- Does not use model to determine support levels – just caps
- Some RoR may get recycled support from others who are capped
- No carve-out for USF in the donut holes (competitive areas)
 - Mobile Wireless/Satellite do not qualify as unsupported overlap carrier
- Eliminates Identical Support Rule (hurts your CLEC/CMRS)
- Reduce CABs collection/litigation costs (Not in short term?)





The FCC Plan – The Bad

- Does nothing to advance broadband for ROR – No CAF Plan for RoR LECs
- Potential Reduction in Interstate Rate of Return (9%?)
- High Ceiling Benchmark Rates (\$30)
- Implementation of OpEx and CapEx Caps
- Reductions for RoR receiving more than \$3,000/loop in support
- Carriers with 100% overlap of unsupported carrier will lose all support – future of those less than 100%?
- Time and expense to determine impacts of massive changes



RoR Carrier Concerns



- Evaluate near and long term impacts
 - Ensure 4M/1M service capable to customers or make plans to do so ASAP
 - Will the FCC reduce RoR? What impact would a reduced RoR have on my operations?
 - How will CapEx/OpEx constraints impact my operations?
 - Perform long term forecast (10 years) to see impact of USF/ICC changes on your company
 - Look for new USF/Opportunities to mitigate any loss of current support

New Opportunities



- For most: fair to good recovery/support for BB/voice
 - Next six years could provide good opportunity to invest
 - ICC stable with RM v. actual MOU and AL losses
- More certainty – may help in securing capital
- Edge out into price cap areas during new unserved area auctions
- Potential to get new mobility support for new wireless initiatives
- \$100M new remote area fund
- New specific support for tribal lands





Summary

- Act now to avoid becoming FCC road kill
- Know the Orders impacts on your company
- Plan to mitigate/change those impacts to thrive
- Look for new opportunities to diversify revenues outside of ICC/USF



The Future Is In Our Hands



“The transition from the PSTN to a broadband ruled network equates with the move from telegraph to telephones in the early 20th Century”



John Rose
President,
OPASTCO
March 2004



Questions?