INDIANA TELECOMMUNICATIONS ASSOCIATION
FCC USF/ICC ORDER WORKSHOP

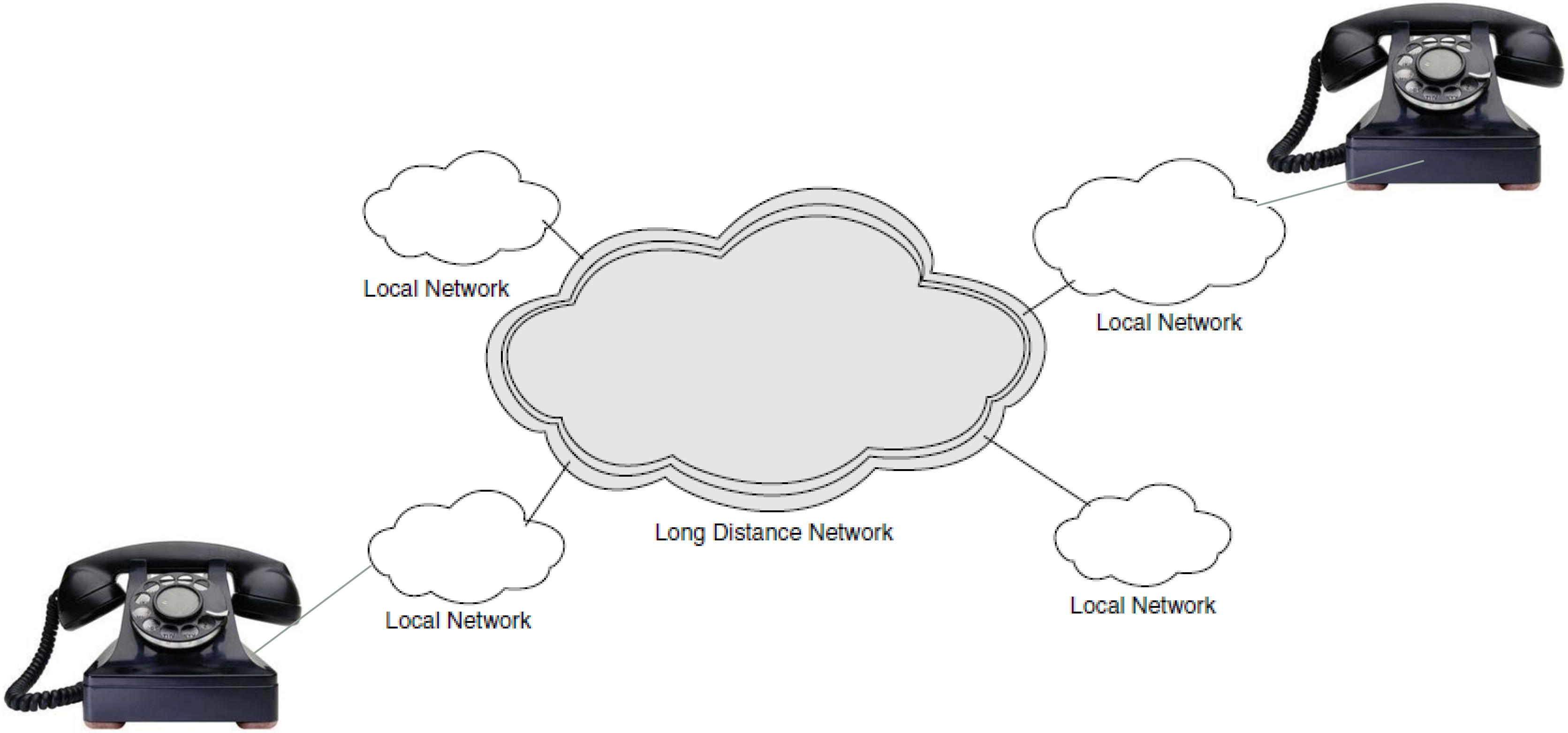
WEDNESDAY, MARCH 14, 2012

Intercarrier Compensation Reform

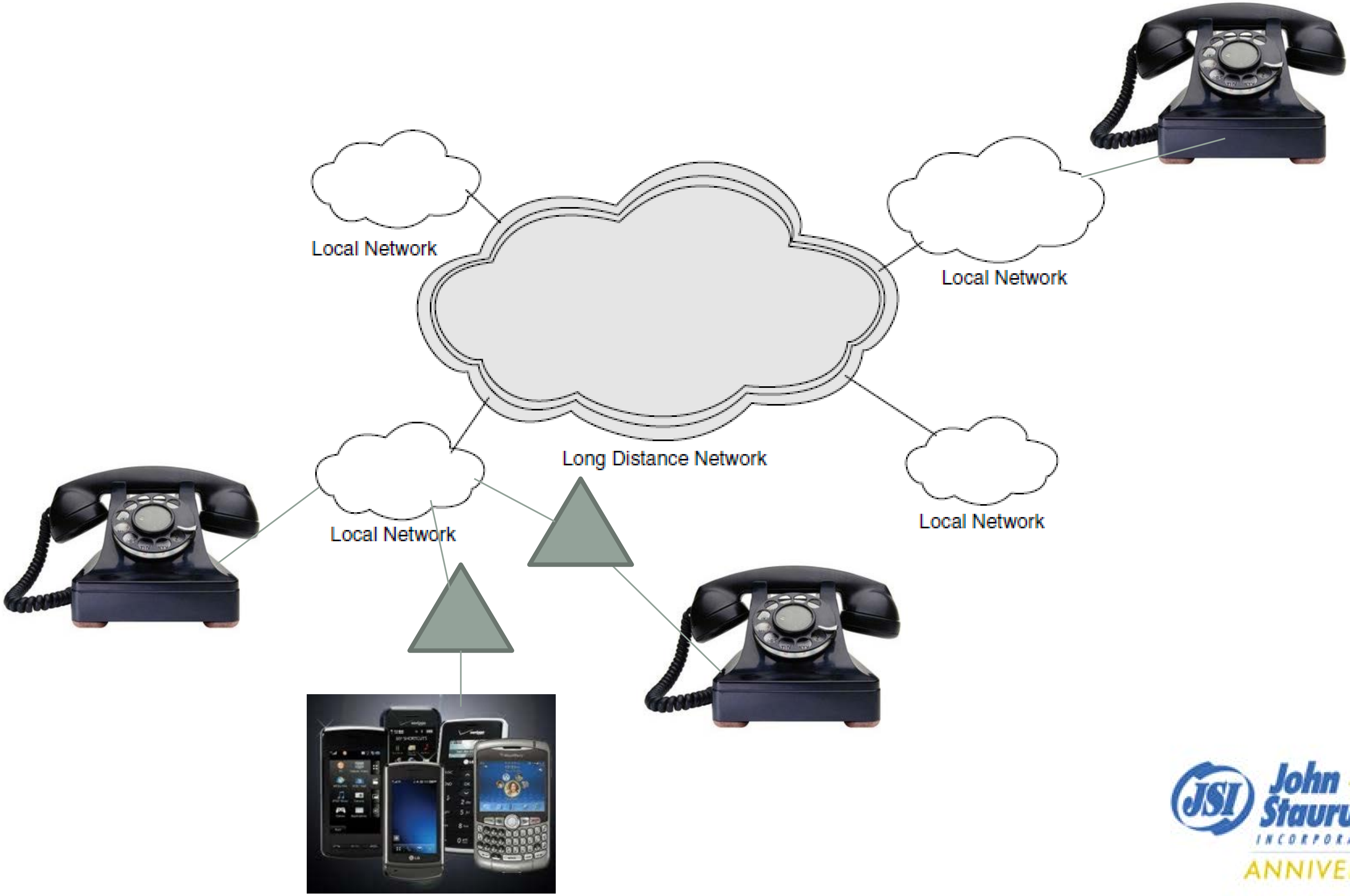
ICC Reforms

- Monumental Changes for ICC
- Major reform designed to eliminate loopholes and arbitrage opportunities
- Establish a bill-and-keep rate structure and transition to bill-and-keep over time

Long Distance Basics

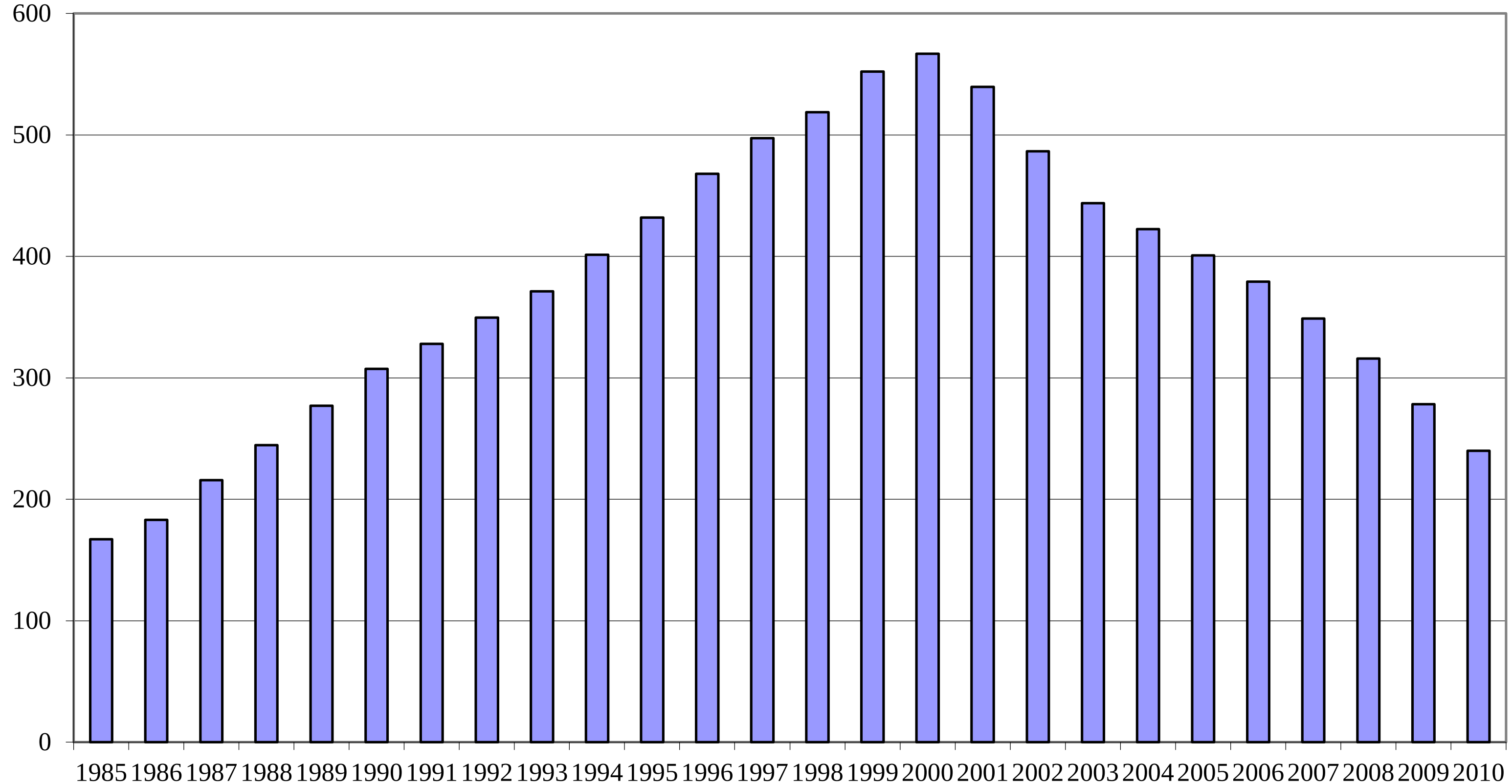


Reciprocal Compensation



Interstate Switched Access

Chart 5.1
Interstate Switched Access Minutes of Use for Incumbent Local Exchange Carriers
(in Billions)



FCC Abandons Access Policy

- We reject the notion that only the calling party benefits from a call and therefore should bear the entire cost of originating, transporting, and terminating a call. As a result, we now abandon the calling-party-network-pays model that dominated ICC regimes of the last century.
- Although we adopt bill-and-keep as a national framework, governing both inter- and intrastate traffic, states will have a key role in determining the scope of each carrier's financial responsibility for purposes of bill-and-keep.

Bill-and-Keep Access Regime

- We believe setting an end state for all traffic will promote the transition to IP networks, provide a more predictable path for the industry and investors, and anchor the reform process that will ultimately free consumers from shouldering the hidden multi-billion dollar subsidies embedded in the current system.
- Under bill-and-keep arrangements, a carrier generally looks to its end-users—which are the entities and individuals making the choice to subscribe to that network—rather than looking to other carriers and their customers to pay for the costs of its network. To the extent additional subsidies are necessary, such subsidies will come from the Connect America Fund, and/or state universal service funds.

John Staurulakis Incorporated 50th Anniversary

Comprehensive Reforms

- Uniform Access Rate Structure
  - Bill and keep as the "ultimate end state for all telecommunications traffic exchanged with a LEC"
    - Begin with terminating switched access rates
    - Study originating and transport issues
  - Preempt state access regimes
  - States to have role
    - Scope of financial responsibility (e.g., transport responsibility beyond network edge)
    - Evaluate interconnection agreements
    - Ensure no cost shifting or other gaming of the reform

Reform Process

- FCC claims legal authority to reform all ICC
- Gradual transition to bill and keep (includes certain transport rates)
  - Cap most ICC rates as of the effective date of order
    - All interstate
    - Terminating switched intrastate, intrastate tandem switched transport and originating and terminating dedicated transport access service
  - Intra and interstate parity by 2013 in two steps using FY 2011 intrastate minutes for each rate element
  - Reduce termination (and some carriers' transport price cap) to bill and keep
    - Six years for price cap
    - Nine years for rate of return

Definitions

- End Office Access Service means: (1) The switching of access traffic at the carrier's end office switch and the delivery to or from of such traffic to the called party's premises
- A Transitional Intrastate Access Service means
  - terminating End Office Access Service that was subject to intrastate access rates as of December 31, 2011;
  - terminating Tandem-Switched Transport Access Service that was subject to intrastate access rates as of December 31, 2011; and
  - originating and terminating Dedicated Transport Access Service that was subject to intrastate access rates as of December 31, 2011.

ICC Reform Timeline (Rate-of-Return)

Dec 29 2011
- Interstate access rate elements (orig. and term. and reciprocal compensation (RC) are capped. Intrastate term. rates capped

July 2012
- Intrastate terminating end office (TESO)[1] and tandem transport, dedicated transport[2] and RC reduced by ½ of rate differential

July 2013
- Intrastate TESO, transport, and reciprocal compensation (RC) at interstate parity[3]

July 2014
- TSEO and RC reduced by additional 1/3 of end office rates and $0.005

July 2015
- TSEO and RC reduced by additional 1/3 of original differential

July 2016
- TSEO and RC at $0.005

July 2017
- TSEO and RC at $0.0036

July 2018
- TSEO and RC at $0.0021

July 2019
- TSEO and RC at $0.0007

July 2020
- TSEO and RC at bill-and-keep

NOTES:
1. Terminating end office rates include end office switching and terminating common line. (51.903(d) and (j))
2. Originating and terminating dedicated transport
3. If intrastate rates are above interstate rates

ICC Reform Timeline (Price cap)

Dec 29 2011

- Interstate access rate elements (orig. and term. and reciprocal compensation (RC) are capped. Intrastate term. rates capped

July 2012

- Intrastate terminating end office (TESO)[1] and tandem transport, dedicated transport[2] and RC reduced by ½ of rate differential

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July 2014

- TSEO and RC reduced by additional 1/3 of end office rates and $0.0007

July 2015

- TSEO and RC reduced by additional 1/3 of original differential

July 2016

- TSEO and RC at $0.0007

July 2017

- TSEO and RC at bill-and-keep.
- Tandem TSEO at $.00007

July 2018

- All TSEO and RC at bill-and-keep

NOTES:

1. Terminating end office rates include end office switching and terminating common line. (51.903(d) and (j))
2. Originating and terminating dedicated transport
3. If intrastate rates are above interstate rates

Reform Process (continued)

- FCC to assess originating and transport transition in further notice
- Carrier may seek a waiver of ICC reform but assessment will be on a total company earning review

Step 1: July 2012

- (b) Step 1. Effective July 1, 2012, notwithstanding any other provision of the Commission's rules:
- (1) Each Rate-of-Return Carrier shall file intrastate access tariff provisions, in accordance with §51.505(b)(2) [*sic*], that set forth the rates applicable to Transitional Intrastate Access Service in each state in which it provides Transitional Intrastate Access Service.

Step 1 (continued)

- (2) Each Rate-of-Return Carrier shall establish the rates for Transitional Intrastate Access Service using the following methodology:
  - (i) Calculate total revenue from Transitional Intrastate Access Service at the carrier's interstate access rates in effect on [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER], using Fiscal Year 2011 intrastate switched access demand for each rate element.
  - (ii) Calculate total revenue from Transitional Intrastate Access Service at the carrier's intrastate access rates in effect on [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER], using Fiscal Year 2011 intrastate switched access demand for each rate element.
  - (iii) Calculate the Step 1 Access Revenue Reduction. The Step 1 Access Revenue Reduction is equal to one-half of the difference between the amount calculated in (b)(2)(i) of this section and the amount calculated in (b)(2)(ii) of this section.

Step 1 (continued)

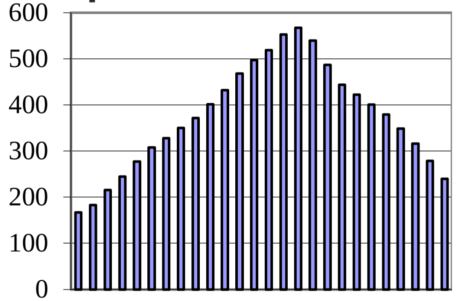
- (iv) A Rate-of-Return Carrier may elect to establish rates for Transitional Intrastate Access Service using its intrastate access rate structure. Carriers using this option shall establish rates for Transitional Intrastate Access Service such that Transitional Intrastate Access Service revenue at the proposed rates is no greater than Transitional Intrastate Access Service revenue at the intrastate rates in effect as of [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER] less the Step 1 Access Revenue Reduction, using Fiscal Year 2011 intrastate switched access demand. Carriers electing to establish rates for Transitional Intrastate Access Service in this manner shall notify the appropriate state regulatory authority of their election in the filing required by §51.907(b)(1).
- (v) In the alternative, a Rate-of-Return Carrier may elect to apply its interstate access rate structure and interstate rates to Transitional Intrastate Access Service. In addition to applicable interstate access rates, the carrier may, between July 1, 2012 and July 1, 2013, assess a transitional per-minute charge on Transitional Intrastate Access Service end office switching minutes (previously billed as intrastate access). The transitional per-minute charge shall be no greater than the Step 1 Access Revenue Reduction divided by Fiscal Year 2011 Transitional Intrastate Access Service end office switching minutes. Carriers electing to establish rates for Transitional Intrastate Access Service in this manner shall notify the appropriate state regulatory authority of their election in the filing required by §51.907(b)(1).
- (3) Nothing in this section obligates or allows a Rate-of-Return carrier that has intrastate rates lower than its functionally equivalent interstate rates to make any intrastate tariff filing or intrastate tariff revisions raising such rates.

Step 2 – July 2013

- Step 2. Effective July 1, 2013, notwithstanding any other provision of the Commission's rules, Transitional Intrastate Access Service rates shall be no higher than the Rate-of-Return Carrier's interstate Terminating End Office Access Service and Terminating Tandem-Switched Transport Access Service rates and subject to the same rate structure and all subsequent rate and rate structure modifications.

Recovery Mechanism

- The recovery mechanism is not 100 percent revenue-neutral relative to today's revenues, but it eliminates much of the uncertainty carriers face under the existing ICC system, allowing them to make investment decisions based on a full understanding of their revenues from ICC for the next several years.
- Absent reform, price cap and rate-of-return carriers alike face an increasingly unpredictable revenue stream from ICC, which will only get worse as demand for traditional telephone service continues to decline.



Eligible Recovery Amount

- Frozen Revenue for Recovery Mechanism (RM)
  - 2011 interstate switched access revenue requirement (forecast already filed)
    - Includes 2011 LSS revenue requirement
  - Fiscal Year 2011 intrastate terminating access revenues
    - Intrastate Transition Service
  - Fiscal Year 2011 net reciprocal compensation revenues
- This frozen amount is reduced 5 percent every year (Eligible Recovery Amount "ERA")
  - FCC asks if the reduction should increase to 10 percent starting in year 6
- Annual carrier revenues from ICC transition elements are applied to offset the ERA.

Access Recovery Charge (ARC)

- Single line monthly service benchmark $30
  - Includes basic local service rate plus federal SLC
  - ARC increases stop at this level if reached before completing ARC phase-in
- $0.50 per residential and single business line
  - Price cap five years
  - Rate of return six years
- $1.00 per line for multi-line businesses for 3 years if at SLC limit, otherwise double the single line level
- No charge of ARC on lifeline customers
- FCC to assess federal SLC levels in Further Notice

CAF-RM

- Recovery Mechanism
  - Eligible Recovery Amount (ERA)
    - LESS: Carrier revenues
      - Interstate switched access service
      - Intrastate terminating switched access service
      - Net reciprocal compensation revenue
    - LESS: ARC revenues
    - Equals: Net ERA
  - If net ERA is positive, this is recovered through the CAF Recovery Mechanism

THANK YOU

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