Missoula Plan Meeting
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Overview

- Thank-you for this opportunity to present the Wisconsin perspective.
  (The Wisconsin Commission has not taken a formal position on the Missoula Plan.)
- We would like to support a consensus plan that serves the interest of consumers, providers and regulators.
- The Missoula Plan with some modifications provides a good basis for such a consensus plan.
- This presentation covers issues important to consumers that are somewhat unique to Wisconsin and that other commissions may not address:
  - Track 2
    - "Pegged" rate, now and future
    - Long-term sustainability of USF and Restructure Mechanism
    - Speed of change
  - Restructure Mechanism Availability to CLECs
  - Flow Through of Cost Savings
- Issues we are also concerned about that are likely to be presented by other state commissions:
  - First Adoptor
  - Rural Areas of Non-rural Carriers
  - Area Code Exhaust
  - State Flexibility

Outline of Presentation

- Wisconsin Evaluation Standards
- Wisconsin as a Microcosm
- Positive Features of the Missoula Plan
- Wisconsin's Specific Concerns
  - Track 2
  - Restructure Mechanism Availability to CLECs
  - Flow Through of Cost Savings

Wisconsin Evaluation Standards

- Goals identified in PSCW comments to FCC, filed May 23, 2005

- *Goal 1: Rely on rate uniformity to avoid arbitrage.*
- *Goal 2: Maintain technological and competitive neutrality by requiring compensation for exchange of traffic regardless of type of provider.*
- *Goal 3: Encourage maintenance and use of the Public Switched Telephone Network (PSTN) infrastructure without discouraging the development and use of alternative networks.*
- *Goal 4: Avoid sudden and dramatic changes in wholesale and retail rates.*
- *Goal 5: Promote universal service, especially in rural and high cost areas.*
- *Goal 6: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under- recovery or windfalls.*
- *Goal 7: Promote jurisdictional cooperation between the FCC and state Commissions to implement a national policy.*

Wisconsin as a Microcosm

- All tracks of carriers
  - Wisconsin lines- Track 1, 68%, Track 2, 23%, Track 3, 9%
  - Nationally lines- Track 1, 88%, Track 2, 8%, Track 3, 4%
- All forms of regulation
  - ROR, Price Cap, Alternative Regulation
  - Access/local rate rebalancing by price and alternatively regulated companies
- Significant facilities-based CLEC presence
- Heavy penetration of cable and wireless
- If you can reconcile the interests for Wisconsin, then you are likely to be able to reconcile issues nationally.

Supporting charts and graphs provided separately

Positive Features of the Plan

- Addresses Arbitrage
- Provides Transition
- Contains Competitive Features

Addresses Arbitrage

Goal 1: Rely on rate uniformity to avoid arbitrage

- These issues have been subject to extensive litigation.

- Provides the same rate for reciprocal compensation, intrastate access and interstate access for all companies by the end of the Plan.

- Addresses phantom traffic:
  - Identifies traffic
  - Identifies points of financial responsibility (“Edge”)
  - Establishes required billing information

Provides Transition

Goal 2: Maintain technological and competitive neutrality by requiring compensation for exchange of traffic regardless of type of provider.
Goal 4: Avoid sudden and dramatic changes in wholesale and retail rates.

- The Missoula Plan provides an opportunity to get from "here-to-there", considering the starting points for all carriers based on a history of regulation.
- Not all carriers transition at the same time or over the same path.
- Considers the financial consequences on various providers.
- A Consensus Plan can develop practical solutions that recognize the unique operational difficulties of various carriers.
- Balances short-run operational concerns with the need for long-run competitive neutrality.
- A plan with broad consensus is more likely to avoid picking winners or losers than regulation alone.

Competitive Features

Goal 3: Encourage maintenance and use of the Public Switched Telephone Network (PSTN) infrastructure without discouraging the development and use of alternative networks.

- Provides competitive alternatives for transport
  - Indirect, common transport
  - Direct transport
  - Install your own facilities
- Carriers pick the mode of transport based on their particular circumstances, such as their ability to aggregate traffic to a particular location.
- Existence of alternatives is a driving force for ICC Reform.
- Plan does not deny alternatives, but instead embraces and reflects alternatives.

Wisconsin Concerns

- Track 2 Issues
- Restructure Mechanism Availability to CLECs
- Flow Through of Cost Savings

Track 2 Overview

- Who are Track 2 carriers?
- Inequity to Track 2 consumers
  - Wisconsin Track 2 consumers already have the highest rates in Wisconsin and will face the risk of even higher rates under the Plan.
- Track 2 threatens the sustainability of the Restructure Mechanism and existing USF.
- There is an imbalance between wholesale and retail rates for Track 2 due to “Pegged” rates.
- The level of future “Pegged” rates are uncertain.

Who Are Track 2 Carriers?

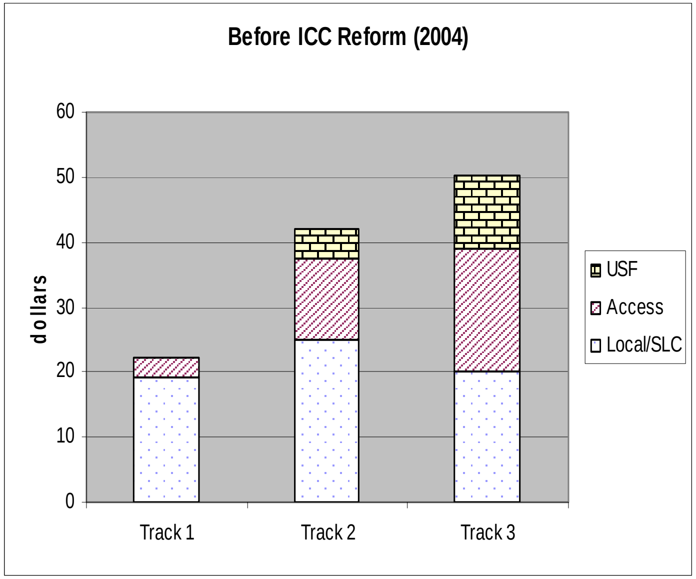
- CenturyTel*
- Frontier/Citizens*
- Embarq (former Sprint local service)
- Winstream (former Alltel and Valor)
- Sure West-may select
- Based on Wisconsin's experience, areas sold by RBOCs are likely to be purchased by these mid-size Track 2 carriers. Specifically, these carriers have more than 10,000 lines, are part of holding companies that have more than 1,000,000 lines, and own some interstate price cap regulated companies.

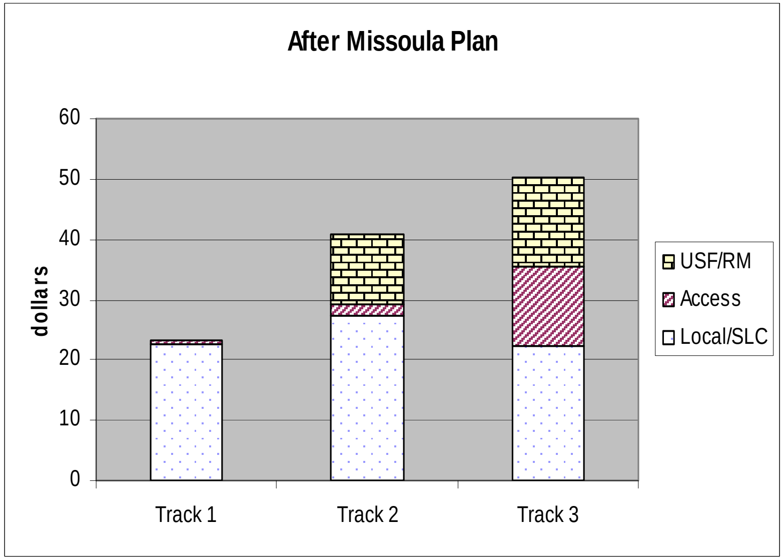
*Operate in Wisconsin

Inequity to Track 2 Consumers

Goal 6: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under- recovery or windfalls
Goal 4: Avoid sudden and dramatic changes in wholesale and retail rates

- Balance between three sources of recovery: Local/SLC, Access, USF/RM on a per line basis
- Wisconsin Track 2 consumers already have the highest rates in Wisconsin and will face risk of even higher rates under the Plan.





Data is author's estimate using simplifying assumptions based on data from PSCW annual reports and USAC.

Inequity to Track 2 Consumers, continued

Goal 6: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under- recovery or windfalls
Goal 4: Avoid sudden and dramatic changes in wholesale and retail rates

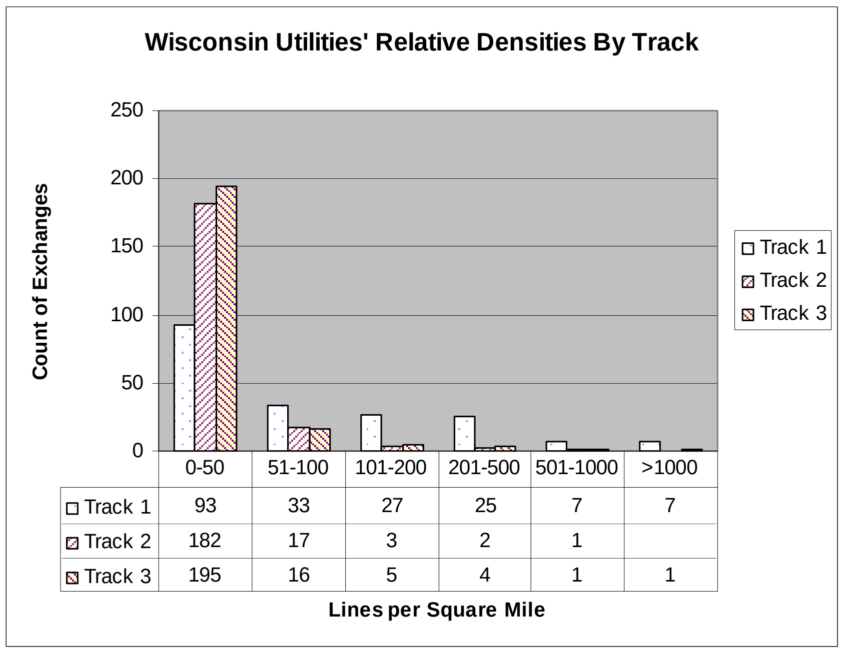
- Geography of various tracks of Wisconsin companies
- Wisconsin average lines per square Mile:
- <u>Track 1</u> <u>Track 2</u> <u>Track 3</u>
- 188 21 24
- Track 2 is more similar to Track 3 than Track 1.

Data is from PSCW annual reports.

Inequity to Track 2 Consumers, continued

Goal 6: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under- recovery or windfalls
Goal 4: Avoid sudden and dramatic changes in wholesale and retail rates

- Variability of densities within tracks for Wisconsin companies
- Track 2 is more similar to Track 3 than Track 1.



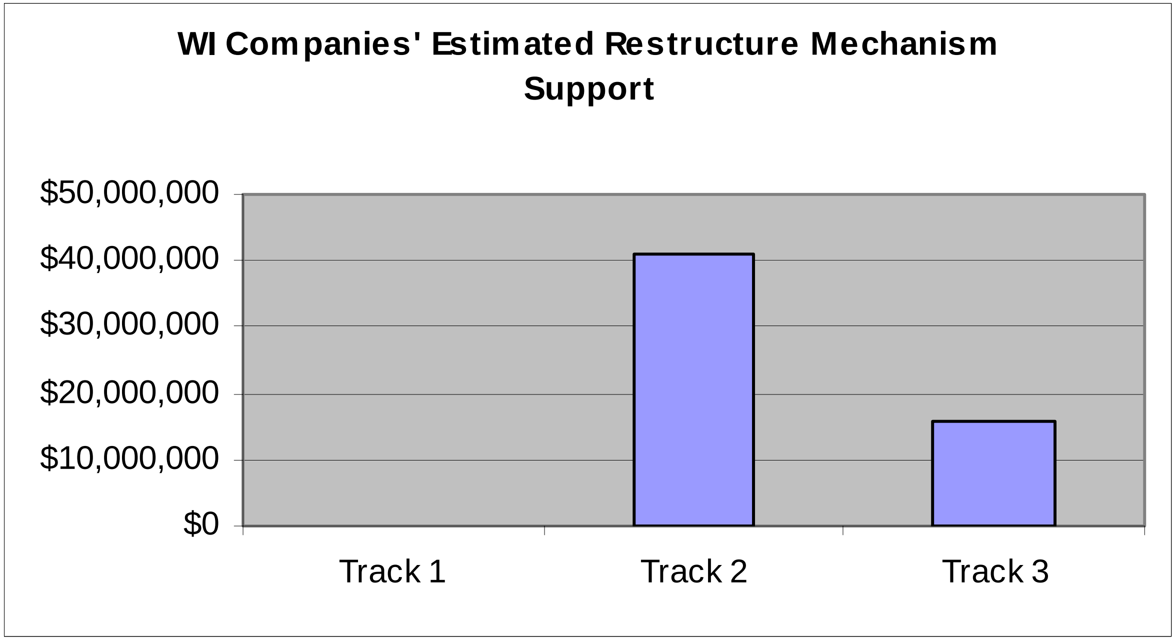
	0-50	51-100	101-200	201-500	501-1000	>1000
Track 1	93	33	27	25	7	7
Track 2	182	17	3	2	1	
Track 3	195	16	5	4	1	1

Data is from PSCW annual reports.

Track 2 threatens the sustainability of the Restructure Mechanism and existing USF

Goal 5: Promote universal service, especially in rural and high cost areas.

- Relative need for Restructure Mechanism support
- If the terms of the Plan were changed for Track 2 companies, the overall amount of Restructure Mechanism Support could be significantly reduced.

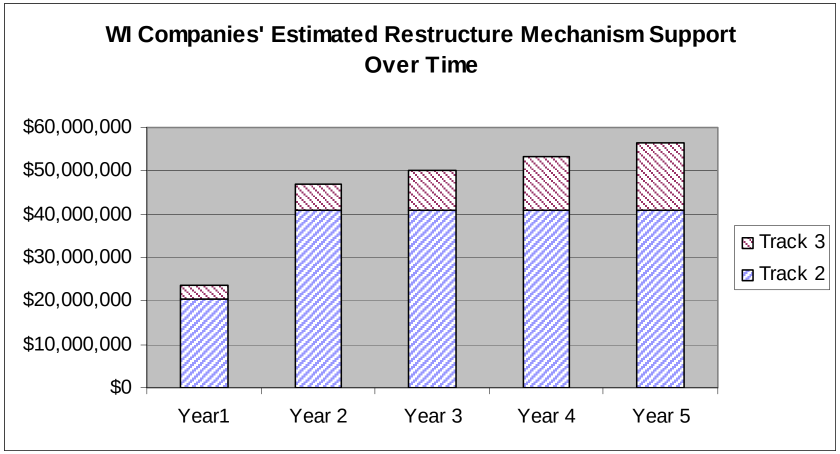


Data is author’s estimate using simplifying assumptions based on data from PSCW annual reports and USAC.

Track 2 threatens the sustainability of the Restructure Mechanism and existing USF, continued

Goal 5: Promote universal service, especially in rural and high cost areas.

Timing of the need for Restructure Support: Track 2 Restructure Support is needed primarily in the first two years, whereas the need for Track 3 Restructure Support falls over five years.

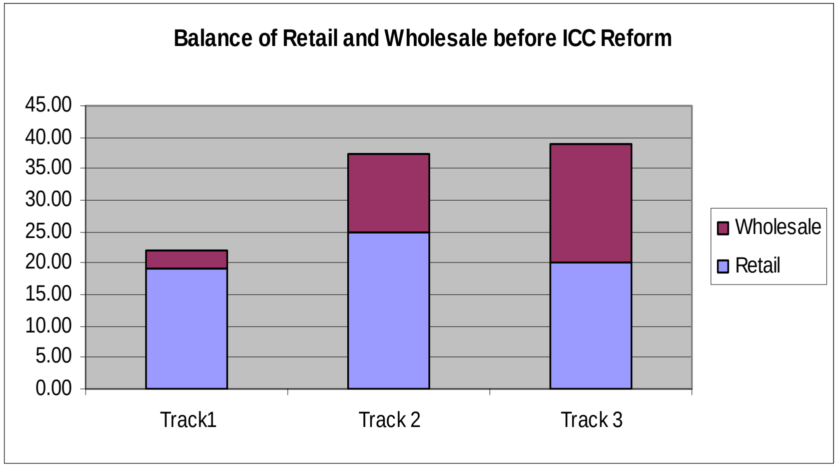


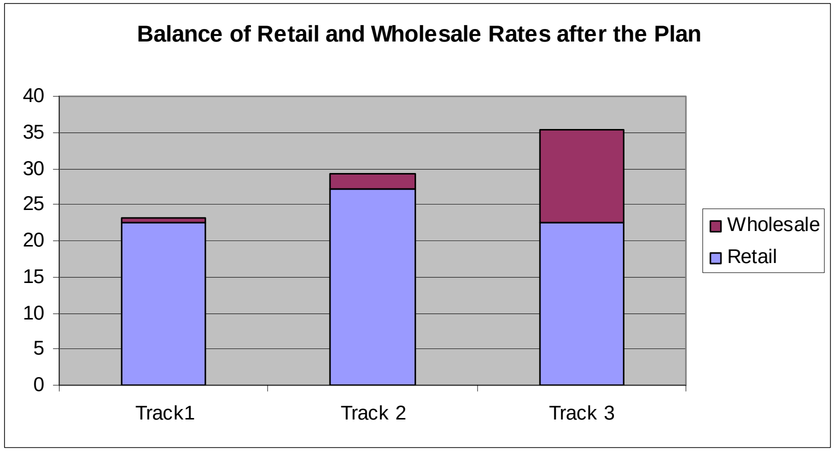
Data is author's estimate using simplifying assumptions based on data from PSCW annual reports and USAC.

There is an imbalance between wholesale and retail rates due to the “Pegged” rates

Goal 6: Provide for timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and wind falls.

- Imbalance of cost recovery from retail (Local/SLC), and wholesale (ICC) for Tracks 1, 2, and 3
- “Pegged rates” determine the balance of cost recovery between retail rates, and ICC for Track 1 and Track 2 carriers. Track 2 should be more similar to Track 3 than Track 1.





Data is author’s estimate using simplifying assumptions based on data from PSCW annual reports and USAC. Does not include Restructure Mechanism Support.

There is an imbalance between wholesale and retail rates due to the "Pegged" rates, continued

Goal 6: Provide for timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and wind falls.

- The balance of wholesale and retail rates is determined by "Pegged" rates for consumers of Track 1 and Track 2 carriers.

	Track 1	Track 2	Track 3
•	"Pegged" rates	"Pegged" rates	Separations rates
•	Not cost-based	Not cost-based	Cost based

- Where the "Peg" gets put will determine the balance of wholesale and retail rates in the long-term. Track 2 should be more similar to Track 3 than Track 1.

- Wholesale rates should recover all costs that are traffic sensitive. This will assign costs to cost causers.

There is an imbalance between wholesale and retail rates due to the "Pegged" rates, continued

Goal 6: Provide for timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and wind falls.

- Pros and Cons of "Pegged" rates

- Pros
  - Simplicity
  - Uniform national ICC rate
- Cons
  - The Plan is not simple. Track 3 companies all have different rates.
  - Pegged rates will cause new forms of arbitrage.
    - Rates below cost lead to overuse.
    - Rates above cost lead to bypass.
    - Track 1 may not have significant cost variability, but cost variation between Track 2 carriers is more similar to Track 3 than Track 1.
  - ICC rates should recover traffic sensitive costs.
  - The market may be able to sustain higher Track 2 rates than the "Pegged" rates, but one will only know whether those rates can be sustained by trying the higher rates. Rates could be lowered in the future if the market provides evidence of unsustainability.
  - Standard rates, with a backstop of full arbitration, can provide almost the same amount of uniformity without the downside problems.

The level of future “Pegged” rates is uncertain

Goal 2; Maintain technological and competitive neutrality by requiring compensation for the exchange of telecommunications traffic regardless of the type of provider (wireline, wirelss, cable, VoIP, etc.)

- Is the “Pegged” rate for Track 2 less than the separations-determined, traffic sensitive, cost-based rate?
- Will the Restructure Mechanism or USF always recover the difference between the separations-determined traffic sensitive book cost and the “Pegged” ICC rate?
- What will the Track 2 “Pegged” rate be in the future, such as after the four year evaluation? Is there any floor limiting how much lower this rate could be “Pegged”?
- If Track 2 is now determined by a “Pegged” rate, will Track 3 be moved to a “Pegged” rate at the four year evaluation?
- There is no standard by which to set a “Pegged” rate in the future.

Possible Solutions to Track 2 Issues

- Merge Track 2 and 3.
- Change the transition speed for Track 2 companies.
- All Rate-of-Return carriers should be Track 3.
- Change criteria defining Track 2 companies to be based on density (average lines/sq. mi.).
- Define methods to update “Pegged” rates.
- Use ICTF approach of standard-default rates, subject to full negotiation and/or arbitration.
- Start with higher “Pegged” rates and evaluate what level of rates the market will sustain.
- Provide assurance that all traffic sensitive costs will be recovered in wholesale rates or long term USF.
- Other

Note: Some solutions are not mutually exclusive.

Restructure Mechanism Availability to CLECs

Goal 5: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and windfalls.

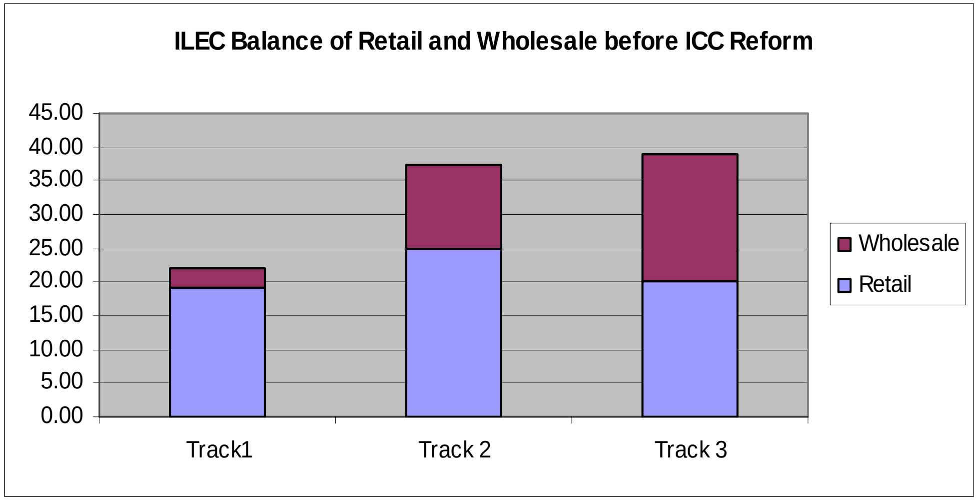
- The terms for Restructure Mechanism availability are not complete and should be defined, such as portable support or “access shift per line.”

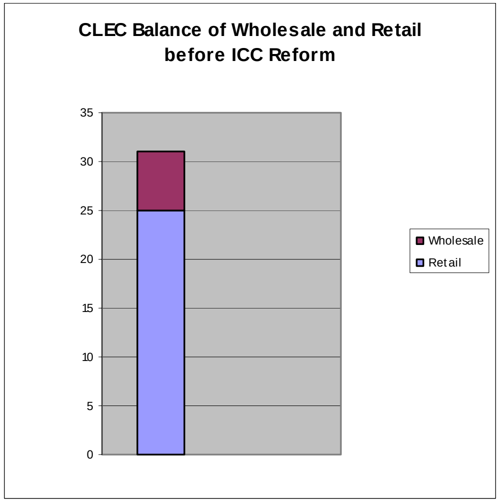
  *p. 74 “Restructure Mechanism dollars will be available to other carriers in circumstances to be determined in the future.”

- Competitive neutrality should provide all carriers with a path to get from “here-to-there” without threatening their financial stability.

Restructure Mechanism Availability to CLECs, continued

- CLECs balance of wholesale and retail rates before the Plan are more comparable to Track 2 and 3 carriers than Track 1. Equivalent SLC increases may not be sufficient to offset access revenue losses.





That portion of per minute access charges attributable to implicit support and that portion reflecting recovery of traffic sensitive costs have not historically been clearly defined. CLECs should get recovery of costs, but should not receive implicit support converted to explicit support unless the CLEC is an ETC. The problem is separating the two.

Data is author's estimate based on data from PSCW ILEC and ATU-Other annual reports.

Possible Solutions to Restructure Mechanism Availability to CLECs

- All carriers that lose access revenues should be recipients of Restructure Support using the methods applicable to Price Cap carriers and imputing SLC increases. Recognize the need for financial stability first.

- Provide CLEC support now, and further evaluate the difference between converted implicit support and actual cost recovery through a universal service proceeding.

- Consider the vulnerable position of CLECs at the beginning of ICC reform.

  – Make CLECs Track 2 or 3 carriers, not Track 1 carriers.
  – Provide CLECs participation in the Rural Transport Rule.

- Other

Note: Some solutions are not mutually exclusive.

Flow Through of Cost Savings

Goal 5: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and windfalls.

- Issue
  - One carrier's lost access revenue is another carrier's cost savings.
  - Should be a zero sum result to consumers as a whole.
- Estimated access savings falls mostly in early years ($Billions)

	Year	Cumulative
• Year 1	$2.9	$2.9
• Year 2	5.9	7.9
• Year 3	7.8	15.7
• Year 4	7.9	23.6
• Year 5	8.0	31.6

- Will competition flow-through access savings?

Flow Through of Cost Savings, continued

Goal 5: Provide timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and windfalls.

- Why flow-through of access savings might not happen.
  - Long-terms (2+ years) on business contracts
  - 1- or 2- year terms on cellular and wireline packages.
  - Competitiveness of the market may vary geographically

- Should carriers get to keep $2.9 Billion in Year 1 and $5.9 Billion more in Year 2 while consumers wait for benefits to flow-through?

Solutions for Flow Through of Cost Savings

- Other regulatory surcharges are not limited to starting only at the beginning of a new contract.
  - Require regulatory credits
  - Or forego other regulatory charges, such as number portability, 911, USF

- Require opportunity for contract amendments to reflect flow-through of access savings
  - So long-term business contracts can incorporate regulatory changes
  - Customers are likely to agree to lower rates

- Limit resulting prices on packages of service
  - Increase in SLC should be offset by decrease in package price
  - Or do not allow SLC increases on packages but impute SLC for computation of "Access Shift per Line"

- Other

Note: Some solutions are not mutually exclusive.