REPORT REVIEWING STATE TELECOMMUNICATIONS POLICIES ON UNIVERSAL SERVICE

Docket UT-100562

Prepared by:

Washington Utilities and Transportation Commission

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TABLE OF CONTENTS

EXECUTIVE SUMMARY

The Washington Utilities and Transportation Commission (Commission) convened a proceeding to review state telecommunications policies concerning universal service at the request of certain members of the Washington Legislature. The Commission held three workshops on the issue and received written comments from a number of interested persons. After considering information received in the workshops and comments, the Commission identified the following five options for addressing the issue of universal service and preserving telecommunications network in this state:

1) Maintain the status quo;
2) Require flash-cut or phased-in reductions of intrastate access charges to interstate access charge levels;
3) Undertake selective examination of incumbent local exchange company earnings for potential reductions to intrastate access charges;
4) Subject to a thorough earnings review of the state's smaller telephone companies, create a targeted state universal service fund, with rigid funding criteria and of limited duration, for the transitional support of voice services; and
5) Create a broad state universal service fund that would support voice services for all ILECs serving rural areas of Washington, and which could be transitioned to support broadband services at some point in the future.

The Commission recommends pursuing Option 4, only after completion of a thorough examination of the financial condition of the state's smaller telephone companies to be completed by October 1, 2012. Legislation consistent with this recommendation could be considered during the 2013 legislative session.

INTRODUCTION

On April 7, 2010, the Commission initiated a proceeding to consider development of a policy statement and potential revisions to state universal service policies. The Commission initiated this proceeding in response to a request from six legislators dated March 2, 2010.[1] The letter requested that the Commission "adopt the schedule of workshops to begin in early

[1] The March 2, 2010, letter from Representatives McCoy and Crouse and Senators Rockefeller, Honeyford, Kastama and Zarelli to Chairman Goltz and Commissioners Oshie and Jones is attached to this report as Appendix 1.

April 2010, and ... report to us on the outcomes of those discussions, including any policy or legislative recommendations."

To facilitate our inquiry into the state's Universal Service policies the Commission conducted three workshops, solicited written comments on a number of policy questions posed to interested parties, and, through our Staff, gathered additional information. Collectively, more than ten interested parties provided input in varying degree reflecting the views of companies from all major sectors of the telecommunications industry including, but not limited to, incumbent local exchange carriers (ILECs) including representatives of the Washington Independent Telecommunications Association (WITA), wireless carriers, cable television companies, and various other competitive telecommunications carriers. The Commission was fortunate to have participation by the Public Counsel Section of the State Attorney General's office which, like the Commission, provides input from the broader consumer perspective.

This report presents an overview of existing federal and state laws and policies relating to universal service (Part I); provides a summary of the evolution of the competitive telecommunications landscape in Washington in recent years and how it impacts the implementation of state and federal universal policies (Part II); summarizes the process the Commission undertook in this proceeding (Part III); and presents the Commission's findings and recommendations for further action (Part IV).

I. Overview of Existing Federal and State Universal Service Law and Policy

Universal service is the long standing policy of the United States and the State of Washington to enable every American, regardless of location, to have access to affordable high-quality telecommunications and, more recently, information services. The policy encourages certain designated telecommunications carriers to invest in and operate telecommunications networks that enable the provision of telecommunications services in less dense and higher cost areas of the country at prices that are reasonably comparable to those offered in more dense and lower cost areas. As explained below, the policy has been accomplished through a variety of specific, and sometimes obscure, mechanisms that provide for significant financial transfers (in effect, subsidies) between various providers of telecommunications services and, therefore, to and from their customers.

Prior to the advent of local telephone service competition from other telecommunications carriers, and via new platforms such as wireless, Voice over Internet Protocol (VoIP), and broadband, universal service was advanced under a regulatory regime that relied upon a significant transfer of revenues from long distance ("LD") carriers to local telephone companies. These transfers have been commonly known as interstate and intrastate access charges. Historically, these access charges have transferred a material portion of the revenues that long distance companies receive from their customers to local exchange companies, referred to as incumbent local exchange companies or ILECs. These charges are collected through the rates that ILECs apply to long distance carriers that use their networks to originate and terminate LD calls.

The access charge structure, and the federally-established subsidies created by it, were very successful in promoting the development and maintenance of local telephone infrastructure and universal service.[2] The system could be properly administered because most major service providers, be they local or long distance, were to a significant degree under the jurisdiction of both state and federal regulatory bodies that were, in turn, jointly responsible for, and focused on, the preservation and advancement of universal service. While successful in advancing universal service for voice services, the historical relationships between traditional telecommunications providers, their customers and state and federal regulatory policies have become increasingly challenged by the advent of new technologies and new service providers that offer end users competitive alternatives to traditional wireline services.

A. Federal Law and Policy

1. The Federal Telecommunications Act of 1996

Pursuant to the Telecommunications Act of 1996 (1996 Act),[3] which materially amended the provisions of the Communications Act of 1934 (1934 Act), Congress sought to preserve and advance universal service while, at the same time, opening all telecommunications markets to competition. At the time of enactment, considerable competition existed in the interexchange (i.e., long distance) market as a result of certain pro-competitive policies

[2] While successful, the use of access charges in association with specific federal subsidy programs and objectives often resulted in disputes between local telephone companies and long distance providers.

[3] *Telecommunications Act of 1996*, Pub. L. No. 104-104, 110 Stat. 56, 47 U.S.C. §§151 et seq.

adopted by the Federal Communications Commission (FCC); and, although competition was emerging in the local exchange marketplace, it was rather nascent.

In the 1996 Act, Congress sought to introduce competition into local telephone service that historically had been provided through regulated monopolies. The Act delegated authority to the FCC to establish the terms and conditions for breaking open the local exchange marketplace to competition while retaining those aspects of the legacy monopoly-based environment that, through various inter and intra-company transfer mechanisms, preserved and protected universal service. Recognizing that in introducing local telephone service competition it was threatening the implicit subsidy system that had traditionally supported universal service, the 1996 Act directed the FCC to reform its universal service rules to make support explicit and sustainable in the face of developing competition.[4]

Section 254(b) of the Act, directs the Federal-State Joint Board on Universal Service (Joint Board) and the FCC to base policies for the preservation and advancement of universal service on six general principles plus other principles that the FCC may establish. Among these policies are requirements that federal and state support mechanisms should be specific, predictable, and sufficient; that quality services should be available at just, reasonable, and affordable rates; and that consumers in all regions of the nation should have access to telecommunications services that are reasonably comparable to those services provided in

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[4] In large measure, Washington was ahead of the curve in promoting local exchange competition prior to enactment of the 1996 Act. The Washington Supreme Court ruled on a Commission decision regarding the registration and service offerings of a competitive local exchange carrier (Electric Lightwave, Inc.) and the extent to which the Commission's authority to establish service area boundaries of telecommunications carriers conveys certain exclusive rights to provide service within such areas. *Electric Lightwave, Inc v. Washington Utils. & Transp. Comm'n,* 123 Wn.2d 530, 869 P.2d 1045 (1994). A subsequent Commission proceeding established rules concerning interconnection by new entrants to existing telecommunications providers in Washington. *See Washington Utils. & Transp. Comm'n v. US West Communications, Inc.*, Docket UT 941464, 1995 WL 735315 (4th Supp. Order, Oct. 31, 1995). There, the Commission stated:

> The record clearly establishes that unbundling of the local loop is essential to the rapid geographic dispersion of competitive benefits to consumers and is in the public interest. Unbundling allows customers greater opportunity to choose between a diversity of products, services, and companies. Unbundling also allows for efficient use of the public switched network, reduces the likelihood of inefficient network over-building, and ensures that competition is not held hostage by being bundled with bottleneck functions.

Id., 1995 WL 735315, at 30.

urban areas at reasonably comparable rates. Section 254(e) of the Act provides that only eligible telecommunications carriers (ETCs) designated by state commissions (or the FCC in the absence of state commission action) under section 214(e) shall be eligible to receive federal universal service support, and that any such support should be explicit and sufficient to achieve the purposes of that section.

2. The Federal Universal Service Fund

At the federal level, the universal service support is provided primarily through the Federal Universal Service Fund (FUSF), which directly supports construction and maintenance of extensive telecommunications infrastructure that provides nearly ubiquitous, high-quality local voice telecommunications service to some of the nation's most remote and difficult to serve areas. The provision of modern telecommunications infrastructure in these areas would never have been possible were it not for the nation's long-established policy of supporting universal service and the FUSF. The purpose of "high-cost" universal service support always has been to help ensure that consumers have access to telecommunications services in areas where the cost of providing such services would otherwise be prohibitively high.

One of the primary criticisms of the FUSF is the fact that support is generally provided to certain carriers depending on the size and regulatory classification of the carrier, not the characteristics of the area to which support is directed.[5] Additionally, because only voice is a supported service, there is no requirement to provide broadband service to consumers, nor is there any mechanism to ensure that support is targeted toward extending service to unserved areas.[6] Moreover, there are many critics of the FUSF that contend the program does not provide support in an economically efficient manner.[7] For example, several components of the FUSF provide support based on an incumbent carrier's embedded costs, whether or not a

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[5]Notice of Inquiry and Notice of Proposed Rulemaking, *In the Matter of Connect America Fund, A National Broadband Plan for Our Future, High-Cost Universal Service Support (NOI and NPRM Connect America Fund)*, WC Docket No. 10-90, GN Docket No. 09-51, WC Docket No. 05-337, released April 21, 2010.

[6] However, many ILEC recipients of FUSF support in effect have used such funding to facilitate the offering of broadband service because the monies have been used to construct and maintain facilities that can be used by both narrowband voice and broadband services.

[7] *See, e.g.*, Comments of AT&T Corporation, Verizon and Verizon Wireless, Qwest Corporation, *NOI and NPRM Connect America Fund*, dated July 12, 2010.

competitor provides, or could provide, service at a lower cost. Despite these criticisms, however valid, it is indisputable that the current system of high-cost support has achieved considerable success in helping ensure there is widespread and affordable access to voice services in most regions of the nation. Currently, carriers designated by the Commission in Washington receive approximately $100 million annually from the FUSF, and local telephone service is available to more than 99 percent of the residents of the state.[8]

Until recently, rural ILECs were the only providers of ubiquitous, high-quality, facilities-based service throughout their respective service areas. Over the past decade other carriers, particularly wireless carriers, have been receiving financial support from the FUSF, thereby extending significantly the reach of wireless technology into rural areas of the state, although not to the same ubiquitous level that has historically been achieved by their wireline-based competitors.[9]

As competition has developed, federal policy supporting universal service has been made increasingly difficult because the 1996 Act directs the FCC and states to achieve many important, but potentially conflicting, goals. All parties agree there is a compelling need to restructure the current universal service components of the FUSF and make them more sustainable and compatible with a competitive marketplace by wringing out implicit subsidies that, heretofore in a monopoly-based environment, helped to fund universal service. Additionally, there is enormous momentum towards redirecting support to more advanced services such as broadband.

The telecommunications landscape has undergone many fundamental changes that were scarcely anticipated when the 1996 Act was adopted. The Internet was only briefly mentioned in the 1996 Act, and even then not by name.[10] However, now the Internet has come into widespread use, with broadband Internet access service increasingly viewed as a

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[8] *See generally* 2009 FCC Universal Service Monitoring Report, CC Docket 98-202.

[9] Although subject to strong debate among interested parties, wireless carriers have also been able to extend the reach of their networks using, in part, certain "special access" services offered by ILECs pursuant to federal and state tariffs. The reach of wireless networks would not be as extensive but for the availability of such services from the ILECs.

[10] Section 706(c)(1) of the 1996 Act states: "The term 'advanced telecommunications capability' is defined, without regard to any transmission media or technology, as high-speed, switched, broadband telecommunications capability that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology."

necessity. Consistent with this trend, carriers are converting from circuit-switched networks to Internet Protocol (IP)-based networks. These changes have benefited consumers and should be encouraged. Competition has resulted in lower prices for telephone service, and the introduction of innovative broadband products and services has fundamentally changed the way we communicate, work, and obtain our education, news, and entertainment.

At the same time, these developments have challenged the regulatory assumptions underlying the nation's universal service and intercarrier compensation regimes, forcing regulators to reassess existing approaches. The FUSF has seen unprecedented growth, driven in large part by increased support for competitive ETCs. Additionally, the growth of competition has eroded the universal service contribution base as the prices for interstate and international services have dropped. Finally, it appears that numerous competitors have been able to exploit arbitrage opportunities created by a patchwork of above-cost intercarrier compensation rates.[11]

3. The National Broadband Plan

The American Recovery and Reinvestment Act (ARRA) enacted in February 2009[12] required the FCC to prepare a "National Broadband Plan" (NBP) to establish an ambitious agenda for shifting the nation's telecommunications policy towards support of robust deployment of broadband service. As a result of the broadband provisions of the ARRA, the FCC established a broadband task force that gathered information for the plan pursuant to 36 public workshops, 9 field hearings, and 31 public notices that produced more than 75,000 pages of public comment.

The FCC issued the NBP on March 16, 2010.[13] Its primary goal is to put into place the necessary rules, resources, and support mechanisms to enable utilization and availability of broadband service in all corners of the nation. About half of the NBP's recommendations

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[11] *Access Charge Reform*, 12 FCC Rcd 15982, ¶¶ 31-32 (1997); *Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, 16 FCC Rcd 9610, ¶¶ 11-18 (2001); *Developing a Unified Intercarrier Compensation Regime*, Further Notice of Proposed Rulemaking, 20 FCC Rcd 4685, ¶ 3 (2005).

[12] American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (2009) (Recovery Act). The Recovery Act was signed into law on February 17, 2009.

[13] *Connecting America: The National Broadband Plan*, (National Broadband Plan), Staff of the Federal Communications Commission, Released March 16, 2010.

will be addressed directly by the FCC, while other recommendations will require action by Congress, the Executive Branch, and state and local governments working closely with private and nonprofit sectors.

The actions contemplated in the NBP reflect four strategic objectives intended to influence positively broadband availability and utilization:[14]

a. Design policies to ensure robust competition and, as a result maximize consumer welfare, innovation and investment.
b. Ensure efficient allocation and management of assets government controls or influences, such as spectrum, poles, and rights-of-way, to encourage network upgrades and competitive entry.
c. Reform current universal service mechanisms to support deployment of broadband and voice in high-cost areas; and ensure that low-income Americans can afford broadband; and in addition, support efforts to boost adoption and utilization.
d. Reform laws, policies, standards and incentives to maximize the benefits of broadband in sectors government influences significantly, such as public education, health care and government operations.

While each of the objectives will require significant effort by federal and state policymakers, it is the third objective, the reform of the FUSF, which has material long-term implications for federal and state universal service policies.

Although many of the contemplated changes are simply conceptual in nature and the process for altering federal rules applying to universal service is rather lengthy, some of the changes, if implemented, could significantly reduce or even eliminate the current FUSF support flowing to Washington ILECs. Specifically, three potential changes to FUSF support are (1) elimination of so-called "Interstate Access Support" (IAS), (2) freezing of "Interstate Common Line Support" (ICLS), and (3) phase out of interstate "High Cost Loop Support" (HCLS), which would greatly curtail existing FUSF support to Washington's ILECs.[15] Such

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[14] *Id.*, Executive Summary, at XI.

[15] Interstate access support (IAS) is a FUSF support mechanism that was established in 2000 for price-cap carriers to replace the "implicit" support previously collected through interstate access charges with a direct federal subsidy. The purpose of this mechanism is to provide "explicit" support to ensure reasonably affordable interstate access charge rates. Interstate Common Line Support (ICLS) is another

support may eventually be phased out completely in favor of direct support to competitive broadband providers in rural areas through some form of competitive award process. Such an outcome may or may not result in continuing support to Washington ILECs as the nation's focus is shifted to broadband. In other words, although the contemplated changes could have significant impacts on the ILECs, it is not a foregone conclusion that future federal support would not be directed to such carriers. It is simply too soon to predict with any certainty the outcome of the federal proceedings intended to reform the FUSF.

Nevertheless, as a result of such changes, rural ILECs may lose the ability or incentive to continue investing in their networks. Insufficient funding also threatens these carriers' ongoing efforts to offer advanced services to greater numbers of consumers, as well as to schools, libraries and rural health care facilities. It is clear from the WITA companies' perspective, that their ability to sustain the availability of high-quality, modern service to rural consumers may be threatened by federal policy decisions that could place the future financial health of these companies at risk.

In the next month or two, the FCC is expected to release two important Notices of Proposed Rulemakings (NPRMs) on these subjects: the first dealing with comprehensive USF reform and the retargeting of federal USF support through the proposed "Connect America Fund" and the second addressing the unresolved issues of intercarrier compensation reform. Both rulemakings are expected to be difficult and contentious. The FCC is expected to propose a menu of "carrots" and "sticks" to urge states to adopt such reforms, including potentially incentives or credits for states that have already acted to reform intrastate access rates or establish a state-based USF program. If this proves to be true and we judge federal reforms to be likely, we may recommend a more accelerated schedule in order to take advantage of such proposals by the FCC.

FUSF support mechanism. In November 2001, the Commission created the ICLS mechanism for rate-of-return carriers to convert another level of "implicit" support in carrier's interstate access rate structure to "explicit," portable support. ICLS recovers any shortfall between the allowed federal common line revenues of rate-of-return carriers and their subscriber line charge revenues and gradually replaces the carrier common line charge. Finally, embedded High-Cost Loop Support (HCLS) is provided to all rural ILECs based on their embedded costs. Such federal support provides assistance for non-traffic sensitive (NTS) local loop costs -- a term that refers to the costs of outside telephone wires, poles, and other facilities that link each telephone customer's premises to the public switched telephone network. NTS costs are allocated between the state and interstate jurisdictions because all local loops can be used for making and receiving both intrastate and interstate telephone calls. Historically, the interstate allocation was made using the Subscriber Plant Factor (SPF), which is now 25 percent for all companies.

B. State Law and Policy

1. State Statutory Framework

Two sets of provisions of state law address universal service. First, RCW 80.36.300 establishes the preservation of affordable universal telecommunications service as the official policy of the State of Washington. It states:

> The legislature declares it is the policy of the state to:
> (1) Preserve affordable universal telecommunications service;
> (2) Maintain and advance the efficiency and availability of telecommunications service;
> (3) Ensure that customers pay only reasonable charges for telecommunications service;
> (4) Ensure that rates for noncompetitive telecommunications services do not subsidize the competitive ventures of regulated telecommunications companies;
> (5) Promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state; and
> (6) Permit flexible regulation of competitive telecommunications companies and services.

Second, RCW 80.36.600 and RCW 80.36.610 require the Commission to plan and prepare to implement a program for the preservation and advancement of universal telecommunications service which shall not take effect until the Legislature approves the program.[16] RCW 80.36.600(1) states:

> The commission shall plan and prepare to implement a program for the preservation and advancement of universal telecommunications service which shall not take effect until the legislature approves the program. The purpose of the universal service program is to benefit telecommunications ratepayers in the state by minimizing implicit sources of support and maximizing explicit sources of support that are specific, sufficient, competitively neutral, and technologically neutral to support basic telecommunications services for

[16] RCW 80.36.600 was adopted in 1998 pursuant to Engrossed Substitute Senate Bill 6622 (ESSB 6622).

customers of telecommunications companies in high-cost locations.

Subsequent subsections of RCW 80.36.600 and RCW 80.36.610(2) detail what should be in a universal service program.[17]

2. State Policy – Access Charges

To date, Washington has not established a specific universal service fund as contemplated by the state statutes identified above.[18] Nevertheless, in addition to various elements of the FUSF discussed previously, there are certain non-fund subsidy mechanisms that the Commission has established to provide support to ILECs or directly to their customers.

Over time, by virtue of a number of tariff proceedings and specific rulemakings, the Commission has established the rates, terms and conditions regarding intrastate access charges that enable ILECs to assess and collect a variety of rate elements applied to LD carriers for the origination and termination of intrastate LD calls.[19] As a consequence of these proceedings, there are four specific components of the Washington ILEC's intrastate access charge rate structure that provide direct or indirect subsidization of the local telephone services provided by the ILECs;

(1) universal service fund rate,

(2) non-traffic sensitive interim terminating access charge rate (NTS ITAC),

(3) traffic sensitive interim terminating access charge rate (TS ITAC), and

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[17] The provisions of RCW 80.36.300, RCW 80.36.600, and RCW 80.36.610 are set forth in Appendix 2 to this report.

[18] In 1991, the Commission established a "community calling fund" (CCF) administratively that was intended to provide financial support to certain ILECs for conversion of a number of long distance calling routes to local calling capability (commonly referred to as extended area service or EAS). The CCF would have compensated ILECs for any direct revenue shortfalls associated with the financial effects of the conversions. However, the Washington Court of Appeals invalidated that effort as being without statutory authority. *Washington Independent Telephone Ass'n v. Telecommunications Ratepayers Ass'n for Cost-Based and Equitable Rates*, 75 Wn. App. 356, 880 P.2d 50 (1994).

[19] The state also has a subsidy mechanism, the Washington Telephone Assistance Plan (WTAP), which provides indirect financial assistance to low income telephone consumers in tandem with a federal funding mechanism known as the Federal Lifeline Assistance Program. Together these programs provide a discount to wireline telephone consumers for a reduction to the prices assessed on their monthly telephone bills.

(4) carrier common line charge (CCLC).

Billed on a per minute of use basis, these "subsidy" components of intrastate access charges are used in part by each ILEC to offset the cost of providing local telephone service within their designated franchised service areas in Washington. In 2008, for example, such charges generated $41 million.[20]

The NTS ITAC and TS ITAC rates were established as "interim" measures pursuant to a rulemaking under which the Commission required that terminating intrastate access charges not exceed the rate charged for comparable local termination service rates or the actual cost of termination based upon the total service long-run incremental cost (TSLRIC) costing methodology, plus reasonable common or overhead costs (WAC 480-120-540). This rule does not set rates directly, but instead establishes the methodology that ILECs must use in setting terminating intrastate access rates. After it was adopted, WITA challenged the Commission's authority to impose the rule on its members but, ultimately, the Washington Supreme Court ruled that the Commission did not exceed its statutory authority when promulgating the rule.[21]

3. Prior Commission Review of Universal Service Funding

Beginning in 1998, in compliance with RCW 80.36.600, the Commission undertook an examination of state universal service funding conditions,[22] wherein it developed an assessment of the annual cost of supporting universal service.[23] At that time, the cost of universal service was estimated to be approximately $125 million per year, an amount many interested parties found both financially untenable and politically objectionable.

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[20] An excellent overview of these state subsidy mechanisms is contained in the presentation of Mark Vasconi of Commission Staff (see Appendix 3 to this report).

[21] *Washington Independent Telephone Ass'n v. Washington Utils. & Transp. Comm'n*, 148 Wn.2d 887, 64 P.3d 606 (2003). The court's ruling is important in light of the previous action involving the CCF where the Commission was found to have exceeded its statutory authority in establishing a fund to compensate ILECs for lost revenues associated with changes to long distance calling routes.

[22] See Docket UT-980311. The documents in this docket are available on the Commission's web site www.utc.wa.gov.

[23] The Commission's methodology compared the estimated cost of providing telephone service in rural areas with the revenues available to support universal service.

In its final report, entitled *State Telecommunications Policy and Federal Requirements – Promoting Competition and Reforming Universal Service* (1998 USF Report),[24] the Commission proffered a series of recommendations, including the establishment of an explicit state universal service fund for all telephone lines in high-cost rural areas of the state. In support, the Commission drafted request legislation and proposed rules, which the Commission was prepared to implement had the Legislature authorized doing so. It also recommended adoption of a revenue bench-mark as a targeted offset to such costs and a proposal to require contributions to a new state universal service support mechanism supported by all providers of telecommunications services in the state, including wireless carriers and those entities using newly emerging technologies as a means to compete with traditional wireline carriers. Although legislation was introduced,[25] none of the Commission's recommendations or the "Model Universal Service Legislation" incorporated as Appendix H to the 1998 USF Report were adopted by the Washington Legislature.

II Evolution of the Competitive Telecommunications Landscape in Washington - Factors Affecting Universal Service

A. Market Structure Changes

The telecommunications landscape has changed dramatically since the Commission issued its 1998 USF Report. What once was expected to be a fierce competitive battle for local telephone customers between long distance carriers such as AT&T and MCI, on the one hand, and the traditional Bell companies and larger independent telephone companies on the other, has not come to pass. Instead, it is robust and well-funded competition from wireless, cable companies, and new technology providers such as those using voice over internet protocol (VoIP) platforms that have made significant and demonstrable inroads to the ILECs' traditional wireline service offerings.

New telecommunications providers, be they wireless companies, cable TV providers, or VoIP companies, typically offer end users compelling service alternatives at affordable prices that are often broader in scope than the services typically offered by local telephone

[24] A copy of the report in Docket UT-980311 is available on the Commission's website at www.utc.wa.gov.

[25] Senate Bill 5811, 56th Legislature, 1999 Regular Session.

companies. Additionally, wireless service providers offer voice and data communications services using advanced networking technologies that provide mobility to Washington consumers. Cable TV providers offer end users a suite of services that add voice service and broadband internet service on top of highly valued video entertainment services that, in many respects, "glue" an end user to a bundle of services.

While these competing services are distinct end user alternatives from those typically offered by traditional telephone companies, they rely, in varying degree, on the infrastructure that has been historically provided and managed by traditional local telephone providers. As an example, when a wireless customer places a call using a cellular phone, that call uses not only the cell tower and wireless antennas provided by the cellular company, but also high capacity circuits and possibly switching resources owned and maintained by traditional incumbent telephone companies. When a cable company's customer places a voice call, if that call is destined for an end user who subscribes to a traditional telephone company, the call must traverse assets owned by the cable provider and then be interconnected to assets owned and maintained by a traditional wireline telephone company. Therefore, while companies offering communications services over newer technologies compete vigorously with traditional telecom providers for end user revenues, they must, at some level and in varying degrees, purchase services from an underlying local telephone company to provide reliable service to their end users. And while new service providers either lease or interconnect with assets owned by traditional phone companies, the relationships between these new providers and traditional wireline companies are not governed or regulated in the same manner as the relationship between local and traditional long distance providers. These marketplace changes pose significant competitive challenges for the WITA companies, particularly its smaller members that do not have the economies of scale and scope of operations associated with Washington's larger carriers to respond effectively to the new service providers and their bundled service offerings.

B. Weakening Revenue Streams

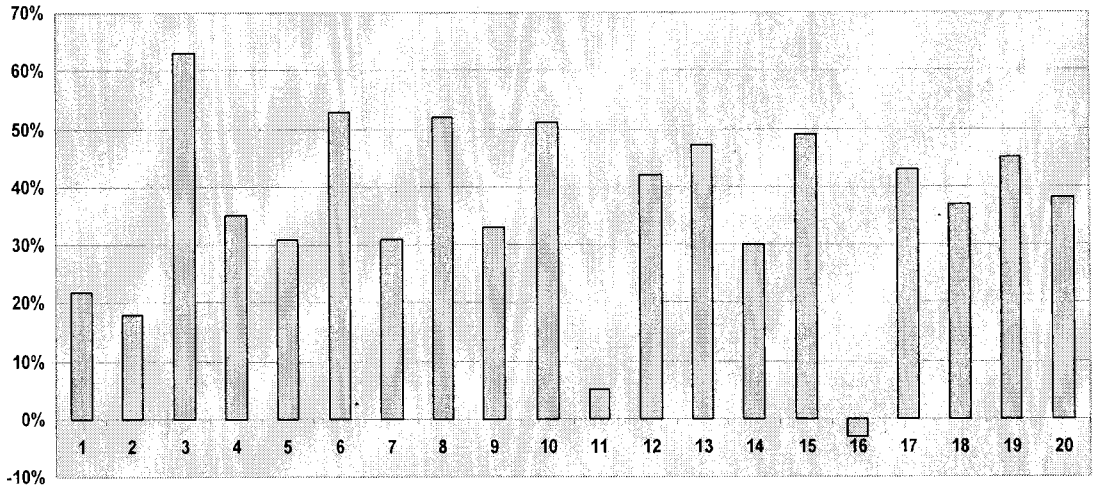
The narrowband voice services that ILECs provide in rural areas of Washington have been and continue to be supported by three principal revenue streams: (1) the local revenues derived directly from telephone consumers within their respective service areas, (2) interstate and intrastate access charge revenues, and (3) significant federal subsidy support from the FUSF.[26] All three "legs of the stool" are atrophying in varying degree. Access lines, the basic element of the carrier's local revenue stream are declining, as consumers "cut the cord" and go wireless, eliminate second lines, or even switch to the competitive offerings of other wireline carriers such as the cable companies. Similarly, access revenues are declining as minutes, and the corresponding revenues associated with them, are shifted to other carriers and technological platforms. As traditional long distance services have shifted from conventional telecommunications technologies to new platforms such as VoIP, the access charge revenues that ILECs have historically enjoyed have declined. In fact, during the course of our proceeding, WITA companies provided tangible evidence surrounding the challenges facing their businesses, particularly the substantial declines in intercarrier compensation that its member companies are experiencing as a consequence of intercarrier compensation arbitrage, access avoidance (often referred to as phantom traffic), and dramatic declines in intrastate access charge usage as a result of minutes shifting to other technological platforms. Finally, the FCC may adopt measures that curtail the level of FUSF support historically enjoyed by rural ILECs.

Indeed, as demonstrated in Table 1 below, which was produced by WITA, it appears that the decline in intrastate access minutes – the basis upon which access charge revenues flow to the companies and are used to support their rural operations – is the most pressing issue facing these companies. Intrastate minutes have declined approximately 42 percent over the six year period (2004 – 2009).

[26] In addition, all but one of the ILECs in Washington receive revenue derived from intrastate access charge rate elements, including subsidy elements, approved by the Commission.

Table 1

WECA Member Companies[27]
Percentage Intrastate Access Minute Loss
Total Minutes (2004-2009)
Average (All Companies): 42%

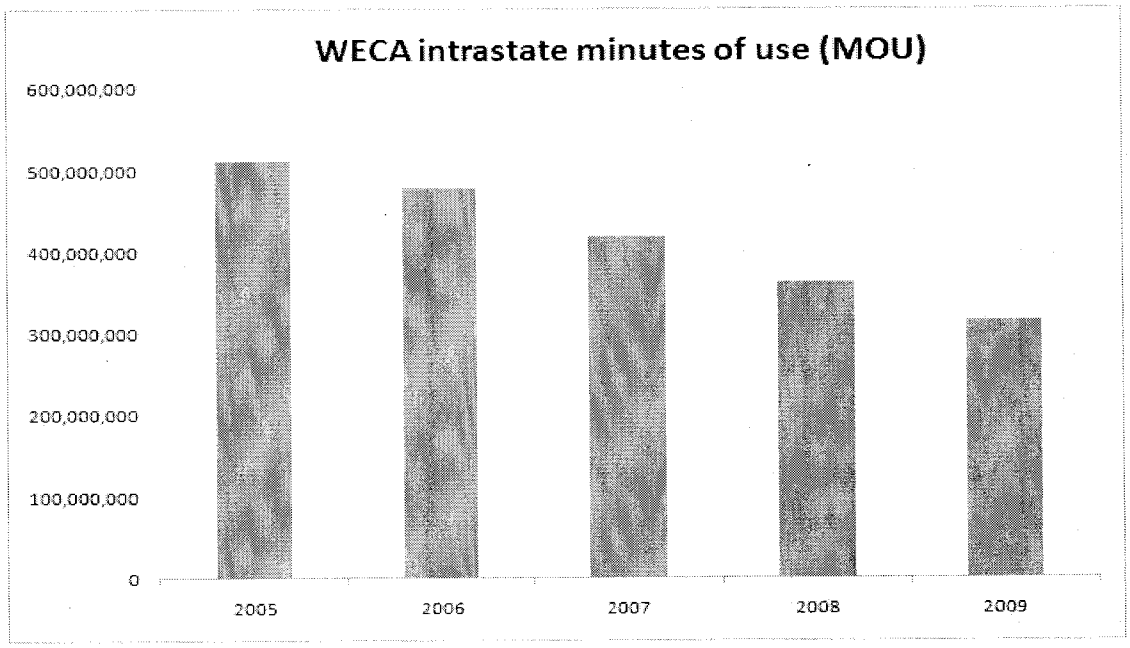


Source: Calculated from data reported by the Washington Exchange Carrier Association for calendar years 2004 and 2009.

As Table 1 demonstrates, virtually all of the ILECs in Washington are experiencing declines in intrastate access usage, a result illustrated collectively in Table 2 below, which shows the overall decline in usage between 2005 and 2009 for all members of the Washington Exchange Carrier Association (WECA).

[27] All members of WITA, except for the company formerly known as Embarq, now part of Century Link, are members of the Washington Exchange Carrier Association (WECA). WECA members include all ILECs in Washington except Qwest, Frontier, and Embarq. For reasons of confidentiality, WITA assigned numbers to each company rather than providing the company's name.

Table 2
Total Intrastate Access Minutes of Use
WECA Members



Source: WECA annual filings.

Although there are a variety of factors that are challenging the ILEC's business models, it is the substantial and accelerating reduction to their intrastate access charge revenue streams that became the focus of discussion during our workshops.

C. Potential Impact of the National Broadband Plan on the FUSF

As discussed above, the FCC contemplates a substantial overhaul for the FUSF as a consequence of the nation's shifting priority to support of broadband services and implementation of the NBP. On April 21, 2010, the FCC released a Notice of Inquiry (NOI) and companion Notice of Proposed Rulemaking (NPRM) regarding use of an elaborate computer model to help determine universal service support levels in areas where there is no private sector business case to provide broadband and voice services. The NOI also seeks comment on the best way to create an accelerated process to target funding toward new deployment of broadband networks in unserved areas as the FCC considers development of new rules to implement fully a new Connect America Fund (CAF) funding mechanism that

would be aimed at ensuring universal access to broadband and voice services. The accompanying NPRM seeks comment on specific reforms to cap growth and cut inefficient funding in the FUSF and to shift certain savings associated with the revisions toward support of broadband service. The Commission understands that other FCC initiatives, in the form of additional NOIs and NPRMs aimed at reform of the FUSF, may be issued prior to the end of this year.

III. Overview of Commission Inquiry and Workshop Process

In response to the request from legislators, the Commission convened three workshops to address the issues we were requested to address.

A. First Workshop

The first workshop took place on May 5, 2010, at the Commission's office in Olympia, Washington. Three panels were convened consisting of senior-level representatives from small or predominantly rural ILECs, larger ILECs, and wireline-based competitors that have significant telecommunications operations in Washington.[28] The panels and their participants were:

Universal Service – Rural Company Perspective

- Bob Debroux, Director Federal Affairs and Public Policy – TDS Telecom
- John Jones, Vice President State Government Affairs – CenturyLink
- Robert Smith, Director of Government Relations and Regulatory Affairs – Kalama and Tenino Telecom

Universal Service – Large Provider Perspective

- Joel Lubin, Vice President – Public Policy, AT&T
- Steve Davis, Senior Vice President, Public Policy and Government Relations, Qwest Communications

[28] The presentations by panel participants are available from the Commission's website at www.utc.wa.gov/100562.

Universal Service – Wireline Competitor Perspective

- Michael Pelcovits, Industry Consultant Comcast
- Greg Kopta, Attorney, Davis Wright Tremaine – Competitive Local Exchange Carriers
- Doug Denney, Director Costs and Policy – Integra Telecom

Additionally, the Commission was fortunate to receive a comprehensive presentation from Ms. Carol Mattey, Deputy Chief, Wireline Competition Bureau of the FCC. Her presentation provided a sweeping overview of the FCC's National Broadband Plan including likely proceedings and issues her agency will be dealing with over the next few years as federal policy shifts from narrowband voice services to a broadband environment.

Finally, Mark Vasconi of the Commission Staff provided a detailed overview of existing state universal service mechanisms.[29]

B. Written Comments – Questions Concerning Appropriate Universal Service Policies in Washington

At the close of the first workshop, interested parties were informed that the Commission would be releasing a set of questions regarding the various issues raised by presenters. On May 26, 2010, the Commission issued a notice inviting responses to 16 policy questions and providing for two rounds of written comments (direct and reply) prior to the second workshop. The questions posed by the Commission are included as Appendix 4. The Commission made available to workshop participants a summary of the direct and reply comments provided by interested parties.[30] Not surprisingly, the responding parties did not agree on the need for and potential structure of a state universal service fund. Those likely to be able to receive financial support encouraged the Commission to recommend a fund. On the other hand, those likely to be required to pay into a fund were generally opposed or would only support a fund as a last resort. Even then, their support was conditioned upon a finding by the Commission that potential recipients of fund dollars were of actual need of such support. Such need would have to be determined only after significantly scrutiny had

[29] A copy of Mr. Vasconi's presentation is attached to this report as Appendix 3.

[30] This summary is available on the Commission's web site at www.utc.wa.gov/100562.

been applied to the financial conditions of the fund's potential recipients, including an analysis of other funding avenues.[31]

C. Second Workshop

The Commission conducted a second workshop on July 27, 2010, at which a panel of the following representatives for wireless carriers presented their views on state universal service policies:

Universal Service – Wireless Carrier Perspective

- Dave Conn, National Director – State Regulatory, T-Mobile USA
- Pete Sywenki, Director – Government Affairs, Sprint Nextel Corporation
- Milt Doumit, Vice President – NW Governmental Affairs, Verizon Communications

The second workshop also focused on a specific proposal offered by representatives of WITA. That proposal, which eventually came to be known as the WITA Concept Paper (Concept Paper), reflected the establishment of a state universal service fund offering two funding approaches based on the relative size of the carrier seeking support.[32]

The first funding approach would provide state universal service support to those ILECs serving fewer than 2 percent of the access lines in Washington. State funding would be available to them for the financial effect of reducing their intrastate access charges to interstate levels minus the calculated difference between their existing local rates and a statewide benchmark local rate the Commission would be authorized to proscribe at some point in the future.[33] To establish the financial need of these smaller carriers, WITA proposed a simplified earnings review[34] the Commission would conduct to determine eligibility for state funding.

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[31] Such funding sources could include: contributions from the federal universal service fund, wholesale revenues (if any), and increased local telephone service rates.

[32] A copy of the Concept Paper is attached as Appendix 5.

[33] The Commission has not established such a benchmark for companies now receiving support. The benchmark's purpose is to set a price for basic telephone service for rural regulated telecommunications companies that is reasonably comparable to that paid by non-rural companies operating within the state.

[34] The term "simplified earnings review" was the subject of extensive discussion among interested parties and the Commission. Despite such discussions, at this time, there is no consensus regarding the scope of

WITA proposed a two-step approach for carriers serving more than 2 percent of the access lines in the state. Step 1 would require the Commission, presumably with the assistance of interested parties, to develop a "forward-looking cost model" to estimate the cost of providing service in high cost areas of the state. The total modeled cost amount would be offset by all revenues derived from "supported services" to determine an initial level of available state universal service funding. Step 2 is essentially the same as the approach proposed for the smaller carriers (i.e., those serving less than 2 percent of the access lines in the state). Carriers serving more than 2 percent of the access lines in the state would calculate the financial effect of eliminating the difference between intrastate and interstate access rates minus a local rate benchmark. Once determined, this amount would serve as a cap on any eligible amount determined pursuant to Step 1.

WITA also proposed, for both methods, a widening of the base of contributors that would be required to pay into any state universal service mechanism; relief from, or determination of continued carrier of last resort responsibilities, depending on whether the company received funds; establishment of certain narrowband and broadband service commitments; and formation of specific Commission rules to establish eligibility requirements, funding procedures, and enforcement abilities.

At the close of the second workshop, the Commission asked WITA to consider the feedback it received from interested parties and make adjustments to its Concept Paper, and submit a revised version, if any, to be subject to written comment prior to our third and final workshop.[35]

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the process and the manner in which it would be conducted. As discussed in Section IV. B. 4, the Commission believes that eligibility for any state fund, should one be established at some point in the future, would require considerable examination of a number of financial matters of the companies seeking to participate in the fund.

[35] As noted above, the latest version of the Concept Paper is attached to this report as Appendix 5. A complete description of the WITA Concept Paper is presented in Appendix 6 and a summary of the written comments of interested parties on the proposal is attached as Appendix 7.

D. Third Workshop

The Commission scheduled a third workshop to focus less on details of WITA's Concept Paper and more on possible areas of consensus. The purpose was to allow the Commissioners and interested parties to engage in a frank discussion regarding any possible conditions under which a new state universal service mechanism could be embraced. The result was such a frank exchange of views, but no consensus was reached, with interested parties generally holding fast to their initial positions either for or against establishment of a state universal service fund.

IV. Policy Options and Recommendations

A. Initial Commission Observations

The substantial and accelerating reduction to ILECs' intrastate access charge revenue streams became the primary focus of the universal service discussions that occurred during the Commission's workshops. The issue served as the focal point for WITA and AT&T's contention that immediate action is required to address the declining financial condition of rural ILECs. During the course of our proceeding, WITA provided a specific proposal to shore up the revenues associated with intrastate access so that recipients of state funding could better maintain and operate the telecommunications network facilities through which they meet their carrier of last resort responsibilities, an approach they contend embodies the preservation of universal service. In essence, the proponents of change advocated reducing intrastate access charges, creating a state universal fund to make up the difference (offset by a statewide local service rate benchmark), and passing potential savings to Washington consumers in the form of lower long distance rates. Before assessing the WITA proposal or the range of policy options available to us, we believe several preliminary observations are warranted.

First, the policy approach we support here must recognize that lower rates are in the public interest and that rates in remote and rural areas should be reasonably comparable to those assessed on consumers in more dense urban areas of the state. Furthermore, we must strive to balance the inherent tension between the rates telecommunications carriers impose on each other for transporting and terminating calls and the rates that each carrier imposes on its own

end users.[36] It is this balance that has been challenged by the dramatic emergence of local exchange competition across multiple market segments. Furthermore, the goal of universal service has, by and large, become a reality, and our success in achieving this result has irreversibly affected the policy objectives we see for the future. The relationship between local rates and intercarrier access charges was originally defined by the financial support required to achieve the expansive goals of universal service. As telecommunication services are available to over 99 percent of the state's population,[37] we now face the task of maintaining the existing network while keeping local telephone rates affordable for customers.

Yet, high intercarrier compensation rates, such as intrastate access charges that have traditionally supported and promoted lower local telephone rates, particularly in the more rural and remote operating areas served by the WITA companies, are no longer sustainable. If we were to lower, or even eliminate intercarrier compensation rates, it would become necessary to require carriers to recover more of their ongoing investment and operating costs from their own end users, a condition that is clearly necessary in an increasingly competitive market. Thus, as competition supplants traditional monopoly-based delivery of telecommunication services there is a compelling need to revisit this balance, particularly the intercarrier compensation rates that competing companies impose on each other.

Second, given the genuine erosion in revenues associated with traditional local phone service and intrastate access charges, the Commission is sensitive to the ILECs' claim that if left unaddressed, a number of traditional telephone companies will, at some time in the future, be placed under financial duress which will likely limit their ability to maintain and invest in their telecommunications networks.

However, a number of stakeholders have argued that before the Commission recommends any specific course of action to the Legislature, the proposal must first involve a detailed examination concerning the true financial condition of each ILEC subject to our jurisdiction. They argue that such an examination should take into account new revenue streams primarily associated with high speed internet and video services which are not directly regulated by the Commission, and not just revenues associated with basic voice service. The extent to which

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[36] We also appreciate the historical context in which some intrastate access rate elements were established as "interim" support mechanisms intended directly to support state universal service objectives.

[37] 2009 FCC Universal Service Monitoring Report, CC Docket 98-202, Table 6.9.

these additional revenues have offset, in whole or in part, the weakening condition of their basic business is unclear at this point in time. Although WITA has presented the Commission with a snapshot of its member's revenue streams and overall financial condition, only certain aspects of their members' revenue streams and costs were represented in WITA's disclosures. As discussed in Subsection B.4 below, the Commission believes the process for determining actual financial need entails a thorough and comprehensive review of a company's revenues and costs in some fashion. The Commission is prepared to devote its resources to accomplish this task in a transparent and deliberate manner. Until this objective is accomplished, the Commission is reluctant to recommend a state universal service fund. Moreover, recognizing that telecommunications consumers already face a myriad of fees, taxes, and other surcharges on their monthly bills, we would not endorse yet another potential line item that is difficult to explain or even justify to consumers. Accordingly, as articulated below in the discussion of various options, the Commission concurs that, for several of the options discussed, a more detailed review of the companies' books and records (including all revenues and costs) would be warranted.[38]

Third, from the Commission's perspective, potential state universal service policy options range from maintaining the "regulatory" status quo to developing an explicit Washington Universal Service Fund (WUSF). The latter is an approach which could, at its extreme, compensate incumbent telephone companies for revenues lost due to further reductions in access charges as well as for the more extensive revenue reductions associated with competition from new providers using newer technology platforms. Regardless of which option is embraced, it is indisputable that significant marketplace developments are challenging the existing environment in which Washington's incumbent telephone companies operate. However, the Commission strongly believes that any changes to state universal service policy that we embrace must take into account such evolving conditions. Furthermore, any specific actions we would recommend must seek to minimize possible marketplace distortions that could occur if users of one relatively new technology platform (e.g., wireless or VoIP) are required to assist another technology platform such as wireline service offered through traditional telecom providers.

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[38] As part of our proceeding, WITA provided some general financial information to Commission Staff regarding the apparent financial condition of each of its members as a means to demonstrate, from their perspective, the deteriorating revenue streams to their companies.

Finally, we note that although the changes taking place in the telecommunications market have affected all incumbent telecommunications providers in Washington, the highest risk to universal service is borne by those smaller rural telephone companies that have experienced dramatic declines in access charge revenue. While Washington's larger telecom companies that serve both urban and rural locations are not immune to this risk, their deeper financial resources and more varied customer base and range of service offerings mitigates the risks posed to such companies by marketplace developments.

B. The Range of State Universal Service Policy Options

Given all these considerations, we turn to the policy options that we see as arising from our workshops. They are:

1) Maintain the status quo;
2) Require flash-cut or phased-in reductions of intrastate access charges to interstate access charge levels;
3) Undertake selective examination of ILEC earnings for potential reductions to intrastate access charges;
4) Create a targeted state universal service fund, with rigid funding criteria and of limited duration, for the transitional support of voice services; and
5) Create a broad state universal service fund that would support voice services for all ILECs serving rural areas of Washington, and which could be transitioned to support broadband services at some point in the future.

1. Maintain Status Quo

In maintaining the status quo, no state universal service fund would be established, intrastate access charges would not be reduced to interstate levels, and WITA's member companies likely would continue to experience declining intrastate access charge revenues as intrastate long distance minutes continue the pattern of erosion. As is true today, any WITA company would have the option of petitioning the Commission to establish a new revenue objective (i.e., intrastate access charge revenue target) based upon its current costs and intrastate access minute volumes. If a company were to proceed down this path, the Commission would continue its practice of conducting moderate earnings examinations including, a review of the ILECs' jurisdictional financial condition in order to determine their proper intrastate revenue objective and resulting intrastate access rates. Given that intrastate minute volumes

have declined by approximately 42 percent since 2004, it is likely that intrastate access rates would increase above current levels, which would, in turn, increase interexchange carriers costs, and could lead to an increase in intrastate long distance rates. In today's competitive telecommunications environment, a company subjects itself to increased competitive pressures when it raises rates. Loathe to provide such an advantage to its competitors, companies have not sought increases to basic rates in order to minimize the current trend of consumers to migrate from the ILEC to competitive alternatives to place intrastate long distance calls. The WITA companies' collective failure to address access charge declines by increasing their customers' rates is one of the chief criticisms expressed by other parties.

The WITA companies have known for a considerable time that the dynamics of an increasingly competitive local telephone exchange marketplace could jeopardize their historical role in delivering rural telecommunications services. Despite this, none of the WITA members has filed tariff revisions, or initiated a proceeding before the Commission, to address specifically the imbalance that exists in their intrastate rate structures (i.e., by seeking to decrease intrastate access charge rates and increase local rates to statewide or more market-based levels).[39] This apparent hesitancy or disinterest in proactively addressing some of the financial challenges associated with their businesses may imply that company revenues were sufficient to meet costs, plus provide a sufficient return on investment. Said another way, one can surmise that the benefits of maintaining the status quo outweighed the risks associated with seeking rate relief. At least for some companies, this calculation today leads them to propose a new course of action.

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[39] In this vein we also note that, other than Qwest, no Washington ILEC has availed itself of existing opportunities under state law to pursue and establish an alternative form of regulation (AFOR) plan according to RCW 80.36.135, or sought to obtain competitive classification for its telecommunications operations or services pursuant to RCW 80.36.310 – 330. The Qwest proceedings involving these provisions of state law are:

(1) Docket UT-000883, Competitive Classification of Business Services,
(2) Docket UT-021257, Competitive Classification of Digital Switched Service, Integrated Digital Switched Network Services, and Uniform Access Solution,
(3) Docket UT-030614, Competitive Classification of Basic Business Exchange Telecommunications Services,
(4) Docket UT-050258, Competitive Classification of Digital Business Switched and Private Line Services,
(5) Docket UT-061625, Petition of Qwest Corporation For an Alternative Form of Regulation Pursuant to RCW 80.36.135.

On a related point, the prospect of the status quo would encourage existing long distance providers to continue to file formal complaints against one or more ILECs to reduce intrastate access charges. Interestingly, successful complaints would likely result in increases to consumer rates – a form of "rate rebalancing" we describe below. This type of action was used recently and aggressively by Verizon in a formal complaint filed against Embarq in 2008.[40] That matter was resolved pursuant to Commission approval of a settlement agreement among Verizon, Embarq, and other interested parties under which Embarq agreed to a phased-in reduction of its intrastate access rates through 2012. Embarq, subject to a rate freeze expressly negotiated in its merger settlement, did not seek to rebalance its consumer rates to recover its access revenue shortfall. In an earlier proceeding, AT&T brought a similar action against Verizon, which resulted in a $32 million decrease in Verizon's intrastate access revenues. This decision was followed by a rate case filed by Verizon to recover in part the lost revenues. This case eventually settled for $39 million, with customer rates increasing by $3.90 per month for most residential and business customers according to a two-year phase in period.[41] While a case-by-case review of access charges would eventually result in access charge reform, the process would take much longer to accomplish, is less straightforward from a policy standpoint, and would not provide the timely resolution of the imbalance issues facing the smallest companies most likely in need of assistance.

2. Lower Intrastate Access Charge Rates to Interstate Levels

This option would require all WITA companies to reduce their intrastate access charges to interstate levels, either immediately or over a prescribed period in order to phase in the effects of the reductions. The Commission possesses the statutory authority to order such a result.[42] To make up for lost access revenues, the Commission would establish a

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[40] *See Verizon Select Services, Inc.; MCIMetro Access Transmission Services, LLC; MCI Communications Services, Inc.; Teleconnect Long Distance Services and Systems Co. D/B/A Telecom USA; and TTI National, Inc. v. United Telephone Company of the Northwest,* Docket UT-081393, Complaint to Reduce Intrastate Switched Access Charges, filed July 25, 2008.

[41] *See AT&T Communications of the Pacific Northwest, Inc. v. Verizon Northwest Inc.,* Docket UT-020406, Eleventh Supplemental Order, Order Sustaining Complaint, Directing Filing of Revised Access Charge Rates (Aug. 12, 2003).

[42] See RCW 80.04.110, which empowers the Commission to review and set rates charged by telecommunications companies not classified as competitive carriers. Also, pursuant to RCW 80.36.140, the Commission has full authority to proceed on the basis that any particular company's practices

"benchmark" local exchange rate, along the lines of the benchmark proposal set forth in the WITA Concept Paper, and order those WITA companies whose local service rates are below the "benchmark" to increase their local rates to recover part of the revenues lost through the reduction in intrastate access rates. While this type of two-part movement, lowering intrastate access rates and increasing rates on local lines, could equalize intrastate and interstate access charges and require that local service customers in rural areas shoulder more of the costs associated with local exchange service, it could still result in a "gap" relative to revenues currently received through the combination of intrastate access charges and local rates. Recovery of any remaining revenue gap would be left to each ILEC through further expansion into new non-regulated lines of business or through further price increases on regulated and/or non-regulated services already offered by the ILECs.

To accomplish the rate revisions contemplated by this policy option, the Commission has two procedural alternatives. First, it could adopt revisions to the rule governing terminating access charges, WAC 480-120-540, or otherwise promulgate new rules in furtherance of the pro-competitive goals of the state telecommunications act of 1985[43] and the 1996 Act by setting industry-wide requirements applying to intrastate access charges, particularly terminating access charges. This result would be consistent with the authority the Commission exercised, and that the courts upheld, when the Commission initially adopted WAC 480-120-540.[44] Second, the Commission could effect the same result by filing complaints against the WITA companies, individually or collectively, to reset any excessive access charges even if they had been established in accordance with our existing rules.

3. Selective Examination of Certain ILECs for Potential Reductions of Intrastate Access Charges to Interstate Levels

As with Policy Option 2 above, using existing authority pursuant to RCW 80.36.140, and without the need for further legislative authority, under Option 3 the Commission would selectively initiate earnings investigations of each rural ILEC, and, upon a showing of need, reduce intrastate access rates while increasing local service rates to compensate for all or part

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affecting rates, including intrastate access rates, are unjust, unreasonable, discriminatory, preferential or in violation of law

[43] Chapter 450, Laws of 1985.

[44] *WITA*, 148 Wn.2d 887 (2003).

of the access revenue reduction. This type of action would, effectively, be a targeted variant of Policy Option 2 above that would focus only on specific companies, examined independently from one another and performed sequentially, such that once the examination of one company is completed, examination of another could begin. The Commission believes that under this approach, intrastate access charges could be reduced to interstate levels on a company-by-company basis over a three to five year period.[45]

4. Targeted Washington Universal Service Fund

Under this policy option, the Commission would oversee a limited universal service fund to be created by the Legislature[46] that would be targeted to those ILECs currently serving less than 2 percent of the total number of lines in the state and which are deemed to be earning less than their authorized revenue requirement. The fund would compensate the ILEC for reduced access revenues after increasing local service rates to a "benchmark" but would not make the ILEC "whole" relative to its overall shortfall relative to its total intrastate revenue requirement.

The fund would be directed solely to support existing voice services currently offered by qualifying ILECs in order to give such companies and their customers a reasonable period of time to embrace the impending transition to a broadband era. It would serve as a transitional mechanism during which ILECs could make the investments and operational adjustments necessary to further develop their networks and pursue business objectives and opportunities. From its inception, the funding mechanism should expire in no more than five years.
To determine the appropriate level of support, the Commission would conduct a detailed earnings examination, including a review of the financial impact of reducing intrastate access rates to interstate levels. If a "qualifying condition" regarding insufficiency of earnings is met, funding would be available. However, support would be limited to the revenue gap resulting from lowering intrastate access rates to interstate levels, so long as the funding recipient has increased local service rates to a Commission-determined statewide local service "benchmark" rate. In other words, if a small ILEC is not achieving its revenue

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[45] We note that existing Commission Staff workload issues on other proceedings as well as current budgetary restraints including scheduled mandatory layoffs of Commission employees could affect the pace at which individual company reviews could be conducted.

[46] This approach would trigger the provisions of RCW 80.36.600 and RCW 80.36.610 requiring legislative approval before it could be implemented.

requirement after reducing intrastate access rates and increasing local service rates to the prescribed benchmark, then that company would be eligible to receive an amount sufficient to recover the revenue lost from reducing its access charges. It could not, however, use the fund to recover the total deficiency relative to its overall revenue requirement.[47]

The fund would be financed through an explicit surcharge assessed on each retail customer's monthly telephone bill, regardless of the type of provider. The surcharge could represent a percentage of intrastate revenues or an assessment per line. Should the assessable base expand from wireline telephone customers to include every working telephone number in use in Washington regardless of technology (i.e., wireline, wireless, and VoIP), the assessment per retail customer would drop considerably.[48]

At this juncture, it is premature to state definitively the total funding requirement for this option.[49] To make this determination, the Commission would have to establish a benchmark for local service rates and determine the scope of the surcharge (i.e., wireline users or all telephone numbers in use for wireline, wireless and VoIP services). However, written comments submitted by AT&T on September 17, 2010, provide a useful estimate on the size of such a fund depending on the local service rate "benchmark" adopted by the Commission. Specifically, AT&T estimates the fund size to range between $2 million per year, using a local rate benchmark of $22.00 per line, to $5.6 million per year using a benchmark rate of

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[47] As an example, if a small ILEC (i.e., a company that serves less than 2 percent of the access lines in Washington) was under earning its revenue requirement by $1,000,000 prior reducing access charges, the ILEC would be eligible for WUSF payments. However, the payment from the WUSF would not be $1,000,000. Instead, the payment to the ILEC from the WUSF would be the amount of revenue lost as a consequence of lowering its intrastate access rates to interstate levels while also increasing local service rates. Regardless of the fact that an ILEC was earning below its intrastate revenue requirement by $1,000,000, if the reduction in access rates to interstate levels forced a drop in revenues of $800,000 while its increase in local service rates generated $200,000, this option would only entitle the ILEC to seek recovery of the net revenue "gap" of $600,000, not the overall deficiency of $1,000,000.

[48] The FCC recently adopted a Declaratory Ruling allowing state commissions to require providers of nomadic VoIP services to contribute to state universal service funds so long as any state requirements are consistent with federal law and policy. *In the Matter of Universal Service Contribution Methodology, Petition of Nebraska Public Service Commission and Kansas Corporation Commission for Declaratory Ruling or, in the Alternative, Adoption of Rule Declaring that State Universal Service Funds May Assess Nomadic VoIP Intrastate Revenues*, WC Docket No. 06-122, Released November 5, 2010.

[49] Without knowing the actual size of the fund, the Commission cannot state the customer surcharge necessary to finance the fund.

$16.00 per line per month.[50] As there are approximately 2 million wireline telephone customers in Washington, the annual surcharge could range from $1.00 - $2.80 per customer. Rounded up, the monthly charge could range from $.10 and $.25 per customer. While AT&T's estimates are helpful, the approximate size of the fund and the related customer surcharge will require significantly more analysis by Commission Staff and industry participants.

Should the Legislature direct the Commission to pursue this policy option, the Commission would engage in one or more rulemakings to define the mechanics for determining the size of the fund, the type and amount of a retail customer surcharge, and the specific procedures necessary for full and impartial administration of the fund. Further, the Legislature could direct the Commission to pursue one of two possible approaches. First, the Legislature could authorize a fund of no more than a predetermined size, reflecting a maximum level that would be available to eligible companies after satisfaction of the access charge and local rate change procedures set forth above. Alternatively, rather than creating the fund immediately, the Legislature could require the Commission to conduct the detailed analysis to determine the appropriate size of the potential fund before it is created. The Legislature could enact legislation that would direct those companies with fewer than two percent of the access lines in the state to provide all relevant financial and operational information the Commission deems necessary in order to review their earnings for the specific purpose of determining which companies would be eligible to receive monies from a state fund and to determine the overall size of a fund. The Commission would then present that information, and a proposal for a specific size of fund, for approval in a subsequent legislative session. Assuming full cooperation of the companies subject to the earnings examinations, the Commission believes that sizing of the fund could be completed no later than October 1, 2012, followed by a concrete fund proposal during a subsequent legislative session.

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[50] *See*, AT&T Comments on Washington Independent Telecommunications Association USF Concept Paper, Docket UT-100562, at 6-7 (September 17, 2010).

5. Comprehensive State Universal Service Fund

Unlike the targeted universal fund discussed in Option 4 that would be used solely to support voice services offered by small ILECs, a more comprehensive state universal service fund could be established to support the services offered not just by the small rural ILECs, but also by larger ILECs and their competitors, including the delivery of broadband service.

Currently, expanding wireline-based broadband services in rural Washington is challenging because of low population density, high development costs and relatively low adoption or "take" rates. When combined, these factors effectively limit broadband services to those areas of the state where broadband investments provide an opportunity for cost recovery plus a reasonable return on invested capital. As broadband is a competitive service not subject to economic regulation, it is apparent that market forces have operated to exclude customers located in remote regions of the state or even those who live some distance from towns in rural Washington. The Commission's experience with expanding the broadband services of certain ILECs[51] provides a glimpse into the significant capital necessary to build broadband capacity in rural Washington.[52] Although the cost and subsidy issues are significant, perhaps

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[51] *See In the Matter of the Joint Application of Embarq Corporation and CenturyTel, Inc. for Approval of Transfer of Control of United Telephone Company of the Northwest d/b/a Embarq and Embarq Communications, Inc.,* Docket UT-082119, Order 05, Final Order Approving and Adopting Settlement Agreement (May 28, 2009) (approving a settlement agreement requiring Joint Applicants (CenturyTel and Embarq) to expand broadband to an additional 2,200 households within the Embarq service area over a three year period following the close of the merger); *In the Matter of the Joint Application of Verizon Communications, Inc., and Frontier Communications Corporation for an Order Declining to Assert Jurisdiction Over, or, in the Alternative, Approving the Indirect Transfer of Control of Verizon Northwest, Inc.,* Docket UT-090842, Order 06, Final Order Approving and Adopting, Subject to Conditions, Multiparty Settlement Agreements and Authorizing Transaction (April 16, 2010) (approving a settlement agreement requiring Frontier Corporation to spend at least $40 million on broadband deployment in Washington in order to deploy broadband service to no less than 95 percent of its Washington wire centers within two years of closing of the transaction and to approximately 89 percent of the households within the existing footprint of the Verizon NW service area by December 31, 2014).

[52] The Commission is not aware of any estimates of cost to build broadband capacity throughout the state, however the FCC recently estimated that the cost of addressing the broadband "availability gap" (defined as the difference between the capital and operational costs of expanding the reach of broadband service to all Americans minus the available broadband revenues is approximately $24 billion nationwide. *See* National Broadband Plan, *supra* note 13 at 137.

the most complicated and controversial challenge would be deciding which companies would be permitted to draw from such a fund. The questions raised in our proceeding include:

- Would any carrier interested in serving the high cost area in question be allowed to tap the fund?
- Should access to the fund be restricted to existing ILECs, no matter what size?
- What if two or more providers seek funding for the same area?
- Is it good public policy to promote competition in areas that the free market has selected to ignore?
- Is it good public policy to encourage significant investment (cost) to reach a few customers in a certain area?
- What technology (e.g., wireless, satellite, wireline, cable) should be favored or disfavored?
- Should a preference be given to the speed of service?
- Should a preference be given to the functionality inherent in the technology?
- Should the fund subsidize the subscriber's monthly charges, either explicitly (lower monthly bill) or implicitly (by providing support to a service provider for operation and maintenance costs)?

All of these issues and more would need to be addressed and settled before the Commission could recommend the Legislature implement this course of action.

Finally, as with Policy Option 4 above, establishing a comprehensive fund would require legislative approval for implementation. Similarly, payments into such a fund would be accomplished through an explicit surcharge assessed on each Washington retail customer's monthly telephone bill and the surcharge itself could be a percentage of intrastate revenues, an assessment per line, or an assessment to each wireline, cable, wireless and VoIP telephone number in use in Washington. For this policy option, the Commission believes the best approach would be to require those that seek to draw from the fund to pay into the fund.

C. Commission Recommendation

The Commission recognizes the need for a small and targeted universal service funding mechanism of a limited duration and subject to phase-out. From the materials provided by WITA, we can assume that the financial condition of some WITA companies is deteriorating and new funding would be necessary to support the provision of local telephone service in

the state's more rural and high cost areas. It appears particularly true for the smallest WITA companies (i.e., those companies that provide service to fewer than 2 percent of the total number of access lines in the state). However, given the paucity of information presently made available by WITA, the scope and scale of such a fund cannot be accurately determined. Therefore, the prudent course is to undertake a series of detailed earnings investigations of the fund's recipients to determine its approximate size before recommending that the Legislature authorize a specific state universal service program in accordance with RCW 80.36.600 and RCW 80.36.610. In essence our approach is a blended one reflecting aspects of Policy Options 3 and 4 above.[53]

As to a state fund supporting broadband service, the Commission observes that while the National Broadband Plan is a comprehensive examination of the nation's broadband infrastructure and broadband needs, it reflects a dramatic shift in federal policy that has only just begun. Among other things discussed in the plan is the estimated nationwide cost of achieving universal availability of broadband service which, using public information and a complex cost model, an FCC task force estimated would cost approximately $24 billion, net of the estimated broadband revenues that would be derived in such areas.[54] We certainly support the nation's shifting focus towards support for broadband service and recognize there will be significant challenges and opportunities for providers of broadband service, including those ILECs that currently serve rural and high cost areas of Washington. There may well be sources for substantial financial assistance for Washington rural telecommunications carriers as federal support mechanisms are revised.[55]

Given the aspirations of the NBP, activities at the FCC, and the lack of information on Washington-specific broadband development costs in rural parts of the state, the Commission

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[53] We do not recommend the approach set forth in the WITA Concept Paper. We recognize it was merely a "straw-man" proposal, and we appreciate the effort that WITA put in to that Paper. It was intended as a means to generate a meaningful discussion of an appropriate way forward, and, to this end, it was successful. Nevertheless, we do not support an approach that simply shifts the financial effect of access charge rate decreases to a state fund under the guise of supporting universal service. While we agree that intrastate access charges must be reduced significantly we are not persuaded a fund is absolutely necessary to achieve such reductions over the near term.

[54] We note that the FCC is now engaged in issuing various rulemaking proceedings that will eventually establish regulations and procedures that will support the goal of universal availability and the means to fund it; however, the process of adopting and implementing such rules is likely to be lengthy and involve numerous procedural and legal challenges before implementation.

[55] See note 15, supra.

believes it is prudent essentially to adopt a "wait-and-see" approach and move slowly with consideration of any comprehensive state universal service mechanism what would include support for broadband deployment as one of its objectives. Federal efforts may supplant or obviate any measures that the Legislature is asked to consider and may ultimately substantially fund broadband expansion through revised national funding mechanisms. Therefore, until there is more definition around the NBP and related FCC efforts, the Commission believes it is premature to establish a Washington fund intended to directly support broadband development in the state.

APPENDIX 1

Washington State Legislature

March 2, 2010

Chairman Jeff Goltz
Washington Utilities and Transportation Commission
1300 South Evergreen Park Drive SW
Olympia, WA 98504-7250

Commissioner Patrick Oshie
Washington Utilities and Transportation Commission
1300 South Evergreen Park Drive SW
Olympia, WA 98504-7250

Commissioner Philip Jones
Washington Utilities and Transportation Commission
1300 South Evergreen Park Drive SW
Olympia, WA 98504-7250

Dear Chairman Goltz and Commissioners Oshie and Jones:

We understand that you have been meeting with AT&T, WITA and some of WITA's member companies to discuss issues related to universal service and to determine what changes, if any, might be needed to preserve and advance the telecommunications network in the State of Washington.

We are pleased that you are having this dialogue, and encourage you to give the matter your urgent attention. Universal service -- the widespread availability of telecommunications services at reasonable rates -- has been a long-standing policy of the State of Washington, and is essential to the economic well-being of the state and to consumers. A modern public network to which all consumers and communication providers in the state have reasonable access should be advanced as well as maintained.

We are aware that the Commission has tentatively established a series of three workshops on this subject. We urge you to adopt the schedule of workshops to begin in early April 2010, and ask that you report to us on the outcomes of those discussions, including any policy or legislative recommendations, by October 1, 2010 so that we may be prepared to address these issues in the 2011 legislative session.

Washington State Legislature

We recognize the complexity of the issues and the amount of work required to address them. However, we believe that a robust communications network is critical to the economic well-being of the state, and that these discussions are necessary to ensure that state policies and regulation are appropriate to maintain and advance that network.

Thank you for your attention to this request.

Sincerely,

John McCoy
State Representative, 38th LD

Larry Crouse
State Representative, 4th LD

Phil Rockefeller
State Senator, 23rd LD

Jim Honeyford
State Senator, 15th LD

Jim Kastama
State Senator, 25th LD

Joseph Zarelli
State Senator, 18th LD

APPENDIX 2
STATE STATUTES ADDRESSING UNIVERSAL SERVICE

RCW 80.36.300 – Policy Declaration

The legislature declares it is the policy of the state to:
(1) Preserve affordable universal telecommunications service;
(2) Maintain and advance the efficiency and availability of telecommunications service;
(3) Ensure that customers pay only reasonable charges for telecommunications service;
(4) Ensure that rates for noncompetitive telecommunications services do not subsidize the competitive ventures of regulated telecommunications companies;
(5) Promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state; and
(6) Permit flexible regulation of competitive telecommunications companies and services.

RCW 80.36.600 Universal service program — Planning and preparation — Commission's duties — Approval of legislature required — Definitions.

(1) The commission shall plan and prepare to implement a program for the preservation and advancement of universal telecommunications service which shall not take effect until the legislature approves the program. The purpose of the universal service program is to benefit telecommunications ratepayers in the state by minimizing implicit sources of support and maximizing explicit sources of support that are specific, sufficient, competitively neutral, and technologically neutral to support basic telecommunications services for customers of telecommunications companies in high-cost locations.

(2) In preparing a universal service program for approval by the legislature, the commission shall:

(a) Estimate the cost of supporting all lines located in high-cost locations and the cost of supporting one primary telecommunications line for each residential or business customer located in high-cost locations;

(b) Determine the assessments that must be made on all telecommunications carriers, and the manner of collection, to provide support for:

(i) All residential and business lines located in high-cost locations;

(ii) Only one primary line for each residential or business customer located in high-cost locations;

(c) Designate those telecommunications carriers serving high-cost locations that are eligible to receive support for the benefit of their customers in those locations;

(d) Adopt or prepare to adopt all necessary rules for administration of the program; and

(e) Provide a schedule of all fees and payments proposed or expected to be proposed by the commission under subsection (3)(d) of this section.

(3) Once a program is approved by the legislature and subsequently established, the following provisions apply unless otherwise directed by the legislature:

(a) All transfers of money necessary to provide the support shall be outside the state treasury and not be subject to appropriation;

(b) The commission may delegate to the commission secretary or other staff the authority to resolve disputes or make other decisions necessary to the administration of the program;

(c) The commission may contract with an independent program administrator subject to the direction and control of the commission and may authorize the establishment of an account or accounts in independent financial institutions should that be necessary for administration of the program;

(d) The expenses of an independent program administrator shall be authorized by the commission and shall be paid out of contributions by the telecommunications carriers participating in the program;

(e) The commission may require the carriers participating in the program, as part of their contribution, to pay into the public service revolving fund the costs of the commission attributable to supervision and administration of the program that are not otherwise recovered through fees paid to the commission.

(4) The commission shall establish standards for review or testing of all telecommunications carriers' compliance with the program for the purpose of ensuring the support received by a telecommunications carrier is used only for the purposes of the program and that each telecommunications carrier is making its proper contribution to the program. The commission may conduct the review or test, or contract with an independent administrator or other person to conduct the review or test.

(5) The commission shall coordinate administration of the program with any federal universal service program and may administer the federal fund in conjunction with the state program if so authorized by federal law.

(6) The definitions in this subsection apply throughout this section unless the context clearly requires otherwise.

(a) "Telecommunications carrier" has the same meaning as defined in 47 U.S.C. Sec. 153(44).

(b) "Basic telecommunications services" means the following services;

(i) Single-party service;

(ii) Voice grade access to the public switched network;

(iii) Support for local usage;

(iv) Dual tone multifrequency signaling (touch-tone);

(v) Access to emergency services (911);

(vi) Access to operator services;

(vii) Access to interexchange services;

(viii) Access to directory assistance; and

(ix) Toll limitation services.

(c) "High-cost location" means a location where the cost of providing telecommunications services is greater than a benchmark established by the commission by rule.

(7) Each telecommunications carrier that provides intrastate telecommunications services shall provide whatever information the commission may reasonably require in order to fulfill the commission's responsibilities under subsection (2) of this section.

RCW80.36.610 Universal service program — Authority of commission — Rules — Fees — Legislative intent.

(1) The commission is authorized to take actions, conduct proceedings, and enter orders as permitted or contemplated for a state commission under the federal telecommunications act of 1996, P.L. 104-104 (110 Stat. 56), but the commission's authority to either establish a new state program or to adopt new rules to preserve and advance universal service under section 254(f) of the federal act is limited to the actions expressly authorized by RCW 80.36.600. The commission may establish by

rule fees to be paid by persons seeking commission action under the federal act, and by parties to proceedings under that act, to offset in whole or part the commission's expenses that are not otherwise recovered through fees in implementing the act, but new fees or assessments charged telecommunications carriers to either establish a state program or to adopt rules to preserve and advance universal service under section 254(f) of the federal act do not take effect until the legislature has approved a state universal service program.

(2) The legislature intends that under the future universal service program established in this state:

(a) Every telecommunications carrier that provides intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the preservation and advancement of universal service in the state;

(b) The contributions shall be competitively and technologically neutral; and

(c) The universal service program to be established in accordance with RCW 80.36.600 shall not be inconsistent with the requirements of 47 U.S.C. Sec. 254.

Appendix 3

WASHINGTON UTC UTILITIES AND TRANSPORTATION COMMISSION

Background on Washington Universal Service Funding

Mark Vasconi, Manager-Telecom

May 5, 2010

UTC

Brief History of Telecom

	Pre-Divestiture	Post- Divestiture	Post- TCA 1996
Competition	Little or none	Long Distance	All encouraged
Services	Local & LD	Local & LD	Local, LD, Broadband & Wireless
Local Rates	Low	Affordable	Packaged with other services
LD Rates	High	Lower	Lower and Decreasing
Traditional LD Volumes	Steady	Increasing	Decreasing
LEC Cost Recovery	Local Rates and Settlements	Local Rates, Access and SLCs	Local Rates, De-reg Services , Access , SLC and FUSF

Foundations of Universal Service and Access Charges

Statutes

- RCW 80.36.300 — "The Legislature declares it is the policy of the state to preserve affordable universal telecommunications service..."
- RCW 80.36.600 — Directs the UTC to "...plan and prepare to implement a program for the preservation and advancement of universal telecommunications service..." subject to legislative approval.

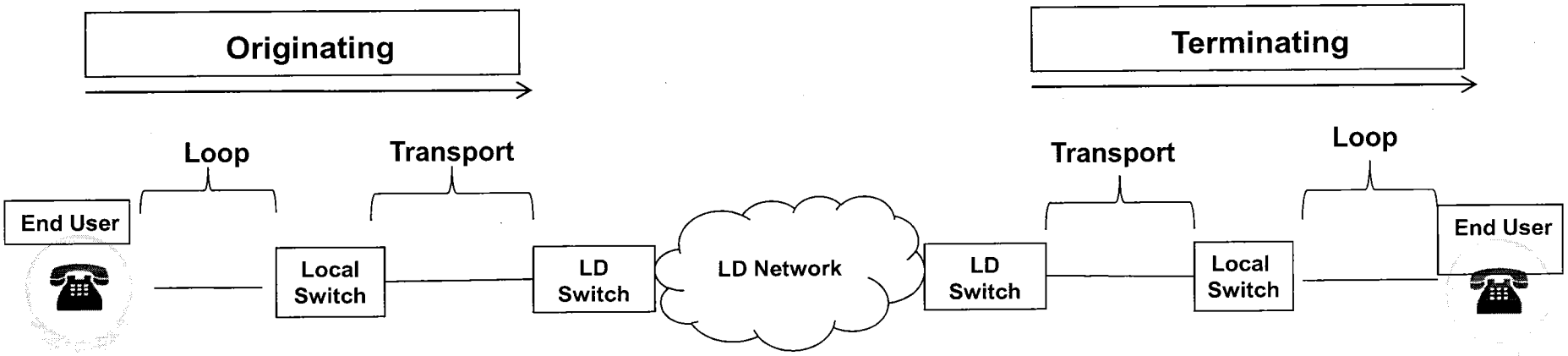
Regulations

- WAC 480-120-540 — Provides the ability of LECs to recover costs for support of universal service through access charges, as an "interim" rate element applied to terminating access service (ITAC).
- WAC 480-120-352 — Defines the scope of WECA's activities

Dockets

- **U-85-23** — **Established Access Charges and "Traditional USF" charge**
- **UT-970325** — **Established Term Access Charge Rule and "ITAC" charges**
- UT-971140 — Established "WCAP" as a "support" pool administered by WECA

Local Exchange Network and Switched Access Rate Elements



Access and Universal Service Rate Elements

CCLC | Sw &Transport | USF

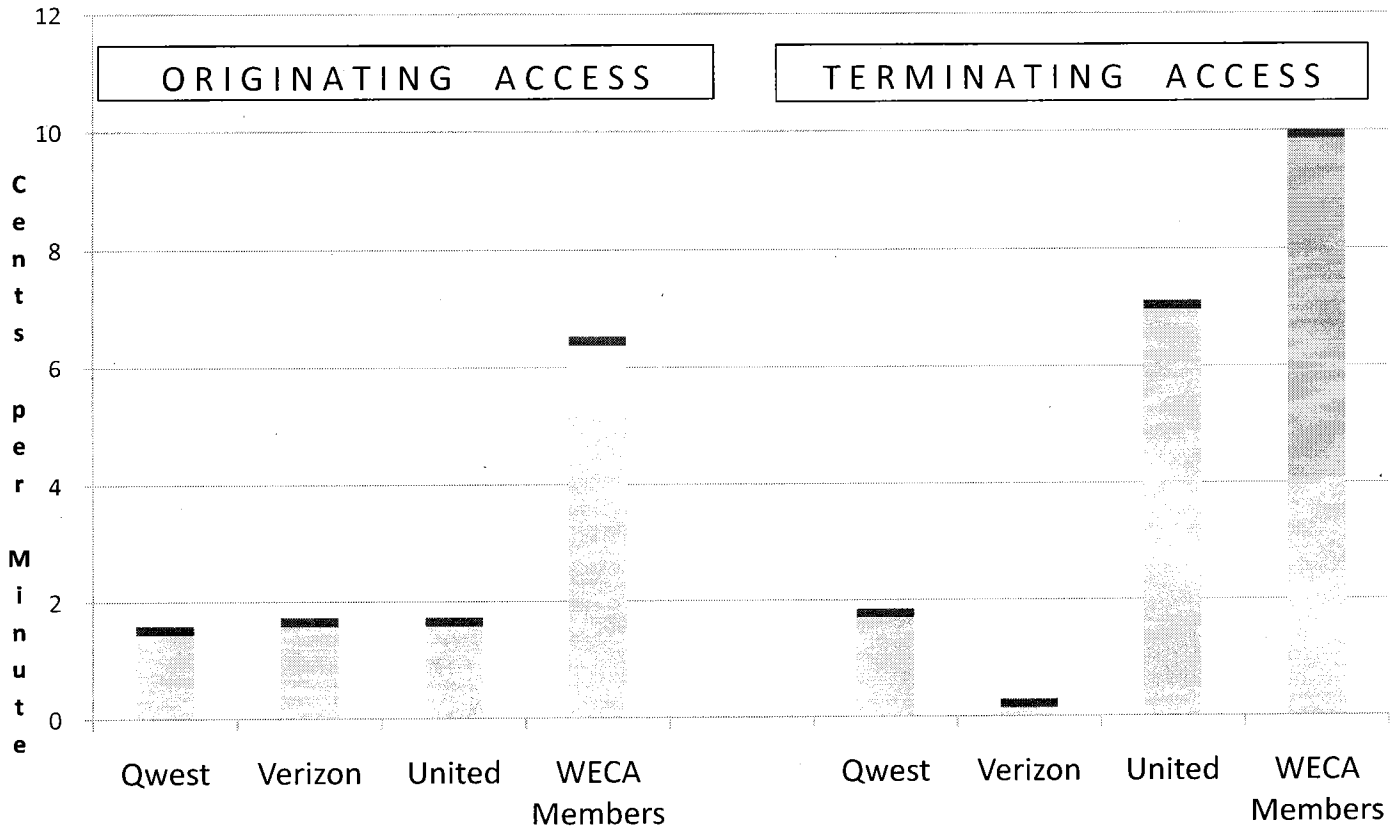
Sw & Transport | USF | TS ITAC | NTS ITAC

Access and Universal Service Rate Table

Rate Element	Traffic Type	Cost* ($/Minute)	Billed to LD Carriers By…	Distribution Mechanism	Revenue Generated
"Traditional" USF	*Orig. and Term.*	*$.00152*	*All LECs*	*WCAP Pool (WECA)*	*$5M*
NTS ITAC	*Term.*	*$.05791*	*WECA LECs*	*WCAP Pool (WECA)*	*$12M*
TS ITAC	*Term.*	*Varies By LEC*	*All LECs except Verizon*	*Bill and Keep*	*$22M*
CCLC	Orig.	$.01173	WECA LECs	WCAP Pool (WECA)	$2M
EO Switching	Orig. and Term	Varies By LEC	All LECS	Bill and Keep	$33M
Total					$74M

* Rates are on file at the UTC.

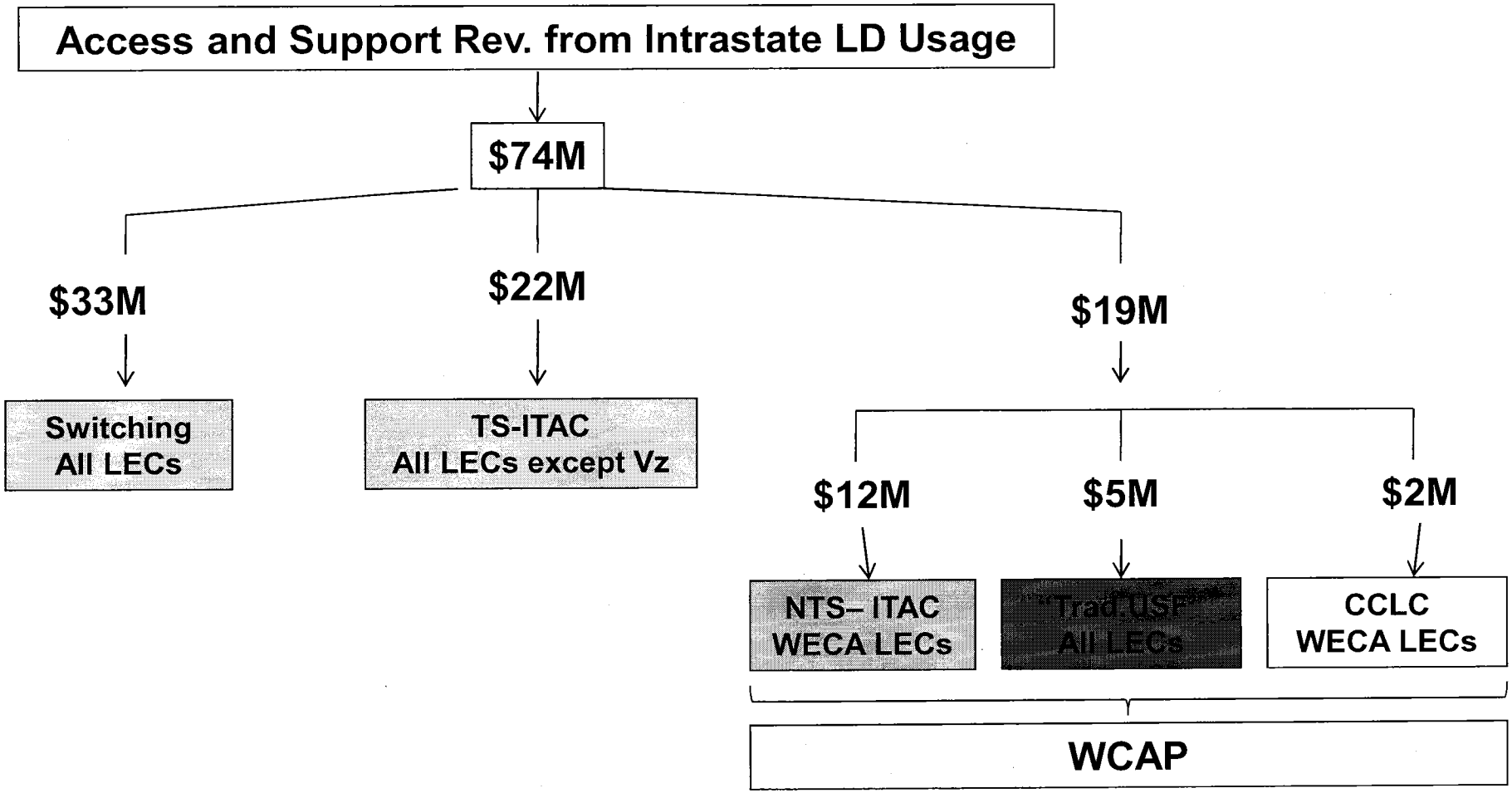
Washington
Switched Access Rates



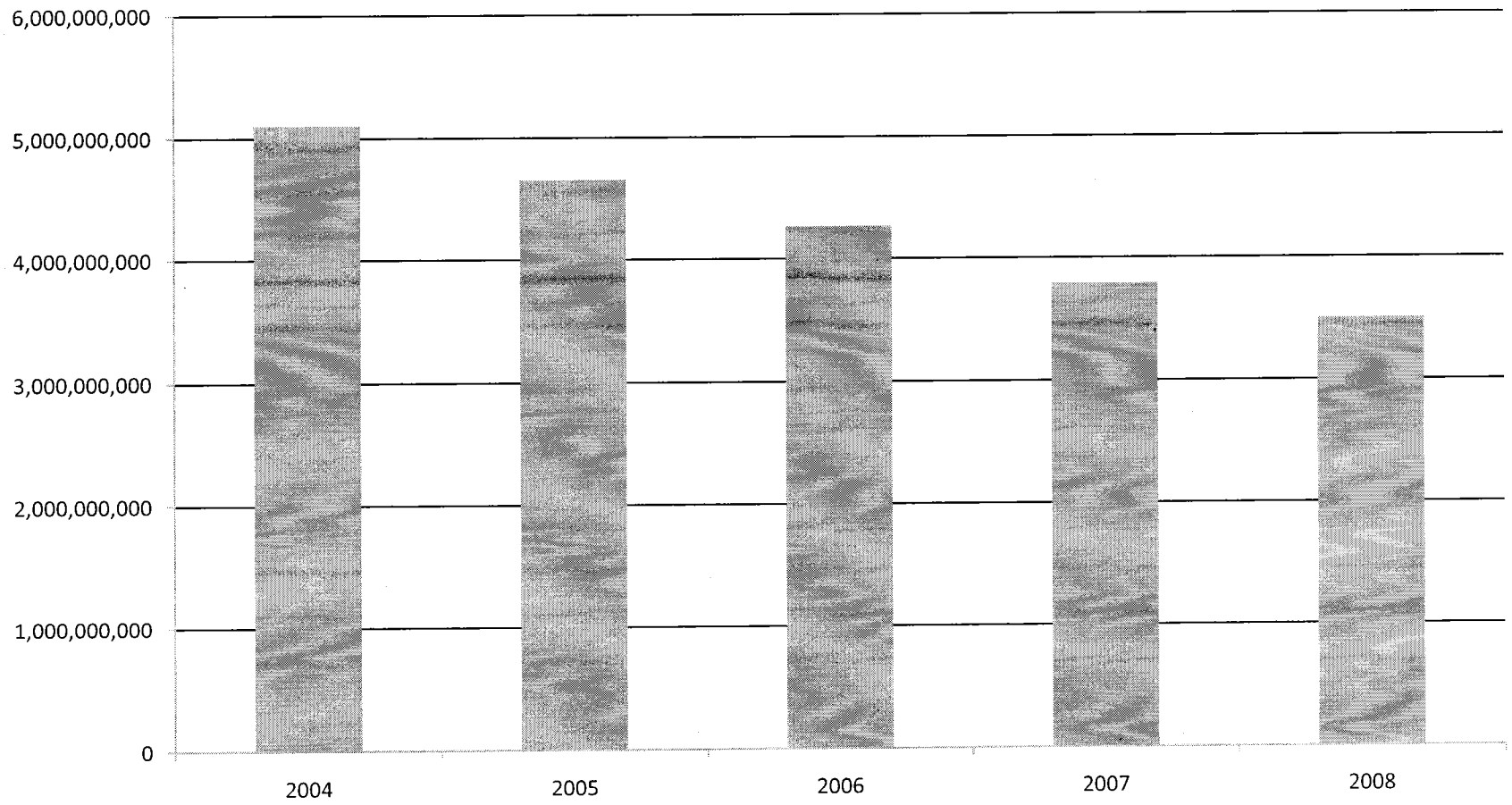
- USF rate = $0.00152*
- NTS ITAC = $0.05791*
- TS ITAC rates vary
- CCLC = $0.01173*
- EO SW rates vary

** The USF, NTS ITAC, and CCLC rate elements are pooled through the WECA WCAP*

Access and Universal Service Revenue Flows (CY 2008)



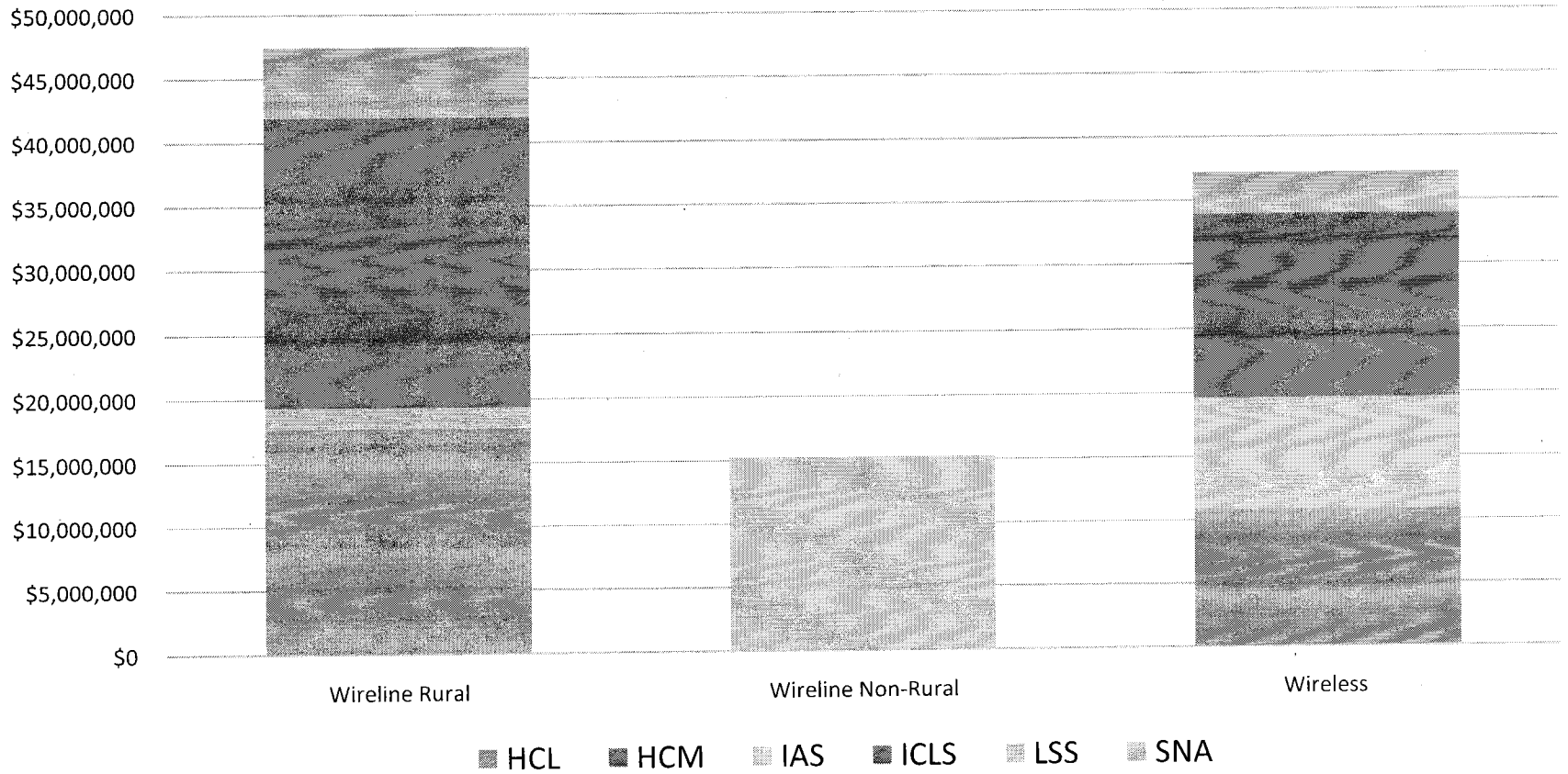
Intrastate Access Minutes of Use (All LECs)



Source: WECA Access Report, 2005 – 2009 (Redacted)

Total Federal USF Support

2009 Federal High Cost Fund Received by ETCs in Washington (Total = $100 Million)



Summary of Washington Universal Support

- Annual funding, State and Federal, is approximately $141M
  - $100M from FUSF
  - $41M from Washington intrastate LD usage via access charges
    - $19M is pooled via WECA/WCAP and distributed to WECA members
    - $22M is billed by all LECs except Verizon and kept by each as support
- Collections are dependent upon LD usage which is dropping
- Future considerations:
  - Carrier of Last Resort Obligations
  - What services need to be supported?
  - How much support is required?
  - How would support be collected?
  - How should it be distributed?

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• Jing Liu, Regulatory Analyst:	(360)664-1292	jliu@utc.wa.gov

DEFINITIONS and ACRONYMS

1) Access Charges: A set of fees charged by Local Exchange Carriers ("LECS") to Long Distance carriers for the cost of LEC facilities used to originate or terminate Long Distance ("LD") calls.

2) Carrier Common Line Charge (CCLC): In Washington, the access charge rate element levied on LD carriers by LECs for the use of the local loop in connection with the origination of intrastate LD calls.

3) Eligible Telecommunications Carrier (ETC): A LEC or wireless carrier that is eligible to receive support from the Federal Universal Service Fund. The Federal USF is projected to be $8.7B (FY 2010) and is funded via an assessment on end-users' interstate charges and appears as a line-item on end user bills. The assessment is determined by the FCC, is currently 15.3% and is adjusted on a quarterly basis.

4) Federal Universal Service Fund (FUSF): The FUSF is a system of support programs under the direction of the FCC that has four main programs: The High Cost Fund; Low Income program; Schools and Libraries program; and Rural Health Care program. The FUSF is funded by a surcharge assessed on interstate telecommunications revenues. The surcharge is adjusted quarterly and is currently 15.3% . In FY 2010 the size of the fund is projected to be $8.7B.

5) High Cost Fund (HCF): HCF, currently estimated to be $4.6B for 2010 and is a component of the Federal Universal Service Fund which is estimated to be $8.7B in 2010. The High cost fund has been established support companies serving high cost areas with the goal of maintaining universal service. HCF support is available to qualifying ETCs such as incumbent LECs (ILECs), qualifying competitive LECs (CLECs) and qualifying wireless carriers. The HCF consists of the following support elements:

DEFINITIONS and ACRONYMS 'cont.

a) High Cost Loop (HCL) Support: Support s rural companies for their non-traffic sensitive local loop cost s in service areas where the cost to provide service exceeds 115% of the national average cost per line. On a national basis, HCL is estimated to be $1.5B of the $4.6B High Cost Fund.

b) High Cost Model (HCM) Support: Supports non-rural carriers for their interstate loop costs that exceed a national benchmark based on a forward-looking economic cost model. The benchmark is two standard deviations above the national average cost per line, which is capped at $240 per line and indexed to the rate of growth in the national total of working loops. Nationally, HCM is estimated to be in 2010, $ .355B of the $4.6B High Costs Fund.

c) Interstate Access Support (IAS): IAS was implemented in 2000 as a result of FCC interstate access charge reform in the Coalition of Affordable Local and Long Distance Service (CALLS) proceedings. It helps offset price cap companies' (i.e. typically, large non-rural LECS) revenue losses associated with reduction in access charges that cannot be recovered from increases in SLC revenue. Nationally, in 2010 IAS will account for approximately $ .641B of the $4.6B High Cost Fund.

d) Interstate Common Line Support (ICLS): ICLS was implemented in 2002 as a result of the FCC interstate access charge reform in the Multi-Association Group (MAG) proceedings. It helps offset rate-of-return companies' (typically rural LECs) revenue loss that cannot be recovered from the SLC revenue when they reduce their interstate access charges. For 2010, ICLS is estimated to be approximately $1.5B of the $4.6B High Cost Fund.

e) Local Switching Support (LSS): LSS subsidizes local switching costs for small ILECs serving 50,000 lines or fewer. For 2010, LSS is estimated to be $.5B of the $4.6B High Cost Fund.

DEFINITIONS and ACRONYMS 'cont.

f) Safety Net Additive (SNA): SNA supports rural carriers that make significant investment in years in which the high cost loop fund is capped. In 2010, SNA is estimated to be $52 Million of the $4.6B High Cost Fund.

g) Safety Valve Support (SVS): SVS provides additional support to rural carriers that acquire high-cost exchanges and make substantial post-transaction investment. For 2010, SVS is estimated to be about $2.3 Million of the $4.6B High Cost Fund.

6) Interim Terminating Access Charge (ITAC): A set of two intrastate access charge elements (Traffic Sensitive and Non-Traffic Sensitive) that LECs may levy on LD carriers ' calls that terminate over a LEC's facilities. These two terminating charges were authorized as a mechanism by which LEC's can recover any costs for support of universal access to basic telecommunications service (i.e. universal service).

7) Local Exchange Carrier (LEC): Provides local facilities to support traditional local service to subscribers as well as access services to LD carriers, wireless carriers and broadband services. LECs include both incumbent local exchange carriers (ILECs) as well as competitive local exchange carriers (CLECs).

8) Local Loop: The physical wire that connects the subscriber's premises to the LEC's local switch.

9) Local Switching Charge (LS or EO): Often called End Office Switching Charge, is the access charge rate element levied by the LECs to the LD carriers for use of local switching equipment in connection with the origination and termination of long distance calls. In Washington, Local Switching is applied on both originating and terminating intrastate minutes associated with LD calls.

DEFINITIONS and ACRONYMS 'cont.

10) Non-Traffic Sensitive (NTS): LEC telephone facilities which are unaffected by changes in the amount of telephone traffic. Typically, Local Loops have been thought of as a non-traffic component of LEC facilities.

11) Subscriber Line Charge (SLC): A flat rate, non-usage sensitive, monthly charge placed on end users billed by LECs and created by the FCC to assist LECs in the recovery of costs associated with local loops. This charge is also know as the Customer Access Line Charge (CALC) or End User Line Charge (EUCL) and is subject to adjustment and review by the FCC, differs for residential and business lines and appears as a separate line item on end user bills. For residential and single line business subscribers the SLC is capped at $6.50 per line per month.

12) Traffic Sensitive (TS): LEC telephone facilities which are affected by changes in the amount of telephone traffic. Typically, End Office switches and transport facilities from the LEC switch to the LD carriers switch have been thought of as traffic-sensitive parts of LEC telephone facilities.

13) Transport facilities: In its simplest form, LEC facilities that connect the LEC end office switch to the a designated LD switch over which long distance traffic is passed between the LEC local switch and the LD carrier.

14) "Traditional" USF : Authorized by the UTC in U-85-23, "Traditional" USF is an access charge element identified to support LEC's whose loop costs exceed 115% of the statewide average. This element is billed by all LEC's to LD carriers on every originating and terminating intrastate LD minute. It is currently $.00152 per originating and terminating minute.

DEFINITIONS and ACRONYMS 'cont.

15) Universal Service: Policy of Federal government contained in Section 1 of the Telecommunications Act of 1934. Sec. 1 states that the purpose of Universal Service is "...to make available, so far as possible, to all the people of the United States a rapid, efficient, nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges..."

In 1985, Washington's legislature also embraced universal service as a policy goal that is found in RCW 80.36.300 where it states:

" The legislature declares it is the policy of the state to: 1) Preserve affordable universal telecommunications service; (2) Maintain and advance the efficiency and availability of telecommunications service; (3) Ensure that customers pay only reasonable charges; (4) Ensure that rates for noncompetitive telecommunications service do not subsidize the competitive ventures of regulated telecommunications companies; (5) Promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state; and (6) Permit flexible regulation of competitive telecommunications and services. "

16) Washington Carrier Access Plan (WCAP): Provides guidance for the administration of the revenue pooling performed by WECA. The plan is a result of a settlement adopted in Docket UT-971140. The Traditional USF access charge rate element as well as the NTS ITAC and the CCLC elements are pooled in WCAP and the proceeds are distributed to the WECA member companies to support their loop costs.

DEFINITIONS and ACRONYMS 'cont.

17) **Washington Exchange Carriers Association (WECA):** A non-profit corporation that administers the WCAP pool for 24 member LECs. WECA also functions as the administrator of the Data Distribution Center (DDC) and as a tariff bureau. The member companies are:

Asotin - TDS	Hood Canal	Pioneer
Beaver Creek	Inland Telephone	St. John
CenturyLink of Cowiche	Kalama	Tenino
Century Link of Inter-Island	Lewis River-TDS	Toledo
CenturyLink of WA	M&L Enterprises	Western Wahkiakum
Computers 5 – Local Tel	Mashell Telecom	WeavTel
Ellensburg - Fairpoint	McDaniel - TDS	Whidbey
Hat Island	Pend Oreille	YCOM Networks - Fairpoint

APPENDIX 4

Attachment A

Questions Concerning Appropriate Universal Service Policies in Washington

Docket UT–100562

1. What is the role of the public switched telecommunications network operated by incumbent local exchange carriers (ILECs) in providing universal service in the state of Washington?

2. Does the UTC need to address intrastate switched access rates to ensure universal service and the widespread availability of telecommunications services at reasonable rates in Washington? What statutory or rule changes are needed in order to do so?

3. Should there be a Washington Universal Service Fund (WUSF)? If so, what factors should the State of Washington consider in weighing the need for establishing a WUSF? Commenting parties are encouraged to address the following factors:
   a. trending reductions to incumbent carrier's intrastate access charge revenues,
   b. the need for comprehensive or streamlined earnings review including determination of the effective intrastate or overall rates of return of recipients of WUSF funding,
   c. revenues from regulated services,
   d. revenues from both regulated and unregulated services,
   e. carrier of last resort obligations of potential WUSF recipients,
   f. any other factors that should be used in determining the need for establishing a WUSF.

4. What is the role of the National Broadband Plan in evaluating the need for a WUSF? If Congress and the Federal Communications Commission (FCC) implement the recommendations in the National Broadband Plan, what would be the role of a state USF? What are the possible effects on Washington consumers of the changes to federal rules contemplated in the National Broadband Plan if there is no state universal service fund? Does the National Broadband Plan alleviate or intensify the need for Washington to address intrastate access charge reform and universal service issues at this time?

5. If the UTC addresses intrastate access charge reform, to what extent is there a need for a WUSF to replace some or all intrastate access charge revenues of ILECs in order to preserve and advance the telecommunications network in the State of Washington? Are statutory changes necessary in order to do so?

6. What direct benefits, if any, will there be to consumers in Washington by addressing intrastate switched access and universal service reform? If intrastate access charge reform is implemented, how will access charge cost reductions realized by current interexchange carriers in Washington be flowed through to Washington consumers?

7. Should intrastate switched access reform apply to all providers of intrastate switched access in Washington? What statutory or rule changes would be necessary?

8. Assuming implementation of the National Broadband Plan, is there a need for a state WUSF during the period in which federal universal service support transitions to support for broadband?

9. If a WUSF is established, what should be the criteria for eligibility to draw from the fund? How should the size of the fund be determined? What should be the basis of the amount of support to be received?

10. What, if any, is an appropriate contribution basis for a WUSF? To what extent should other telecommunications providers, including wireless and VoIP service providers (nomadic and fixed) contribute to a WUSF? If so, on what basis should they contribute?

11. What is the role of carrier of last resort in a state universal service fund? Should any carrier that receives support from the universal service fund be required to assume the obligations of carrier of last resort with respect to traditional voice services, with respect to broadband service, or both? Should the fund support more than one provider per geographic area? How should "area" be defined?

12. Should a state universal service fund include a local rate benchmark? If so, for what purpose and how should it be determined?

13. Should there be a transition period from the current state universal service mechanism to a new WUSF? If so, how long should the transition period be?

14. Currently intrastate universal service support consists of at least two elements that are incorporated into intrastate access charges billed to intrastate interexchange carriers (the Universal Service rate element that is billed by all LECs on both originating and terminating intrastate interexchange usage and the Interim Terminating Access Charge (ITAC) that is billed only on terminating minutes by some carriers but not all). The administration of the traditional USF is currently performed by the Washington Exchange

Carrier Association (WECA); but the LECs each administer their own ITACs. Should WECA continue to administer all of the ITACs in conjunction with the Traditional USF? Should WECA continue to administer any USF (traditional or otherwise)? Should the WECA Board be expanded to include the interests of contributors?

15. In designating entities to be eligible for WUSF funding, should there be an eligible telecom carrier (ETC) designation process that is distinct from the existing federal ETC designation process, or should they be combined?

16. What other kind of oversight, if any, should the UTC have over administration of the WUSF?

APPENDIX 5

WASHINGTON UNIVERSAL SERVICE/ACCESS REFORM PACKAGE

The public communications network is the communication link that supports economic development, broadband access and modern communications in rural Washington. The goal of universal service legislation is to promote and preserve a network which brings vitality into rural Washington. The concept is to create a fund that meets the economic and communication needs of rural Washington, will transition over time to a broadband fund and accomplishes access reform goals.

1) Washington Universal Service Reform - Contributions
   a. All carriers, defined broadly, who use the network pay to support the public communications network
   b. Contribution mechanism developed by Commission
   c. Universal Service Fund administered by the Commission through WECA or such other administrator as the Commission may designate
   d. Commission sets definitions and contribution amount. Commission has enforcement powers.

2) Access Reform Track
   a. Eligible providers – ILECs with less than 2% of state access lines.
   b. Support based on switched access revenue reduction, adjusted for local service benchmark rate which includes EAS
   c. One time calculation
   d. Simplified earnings review as threshold--uses total company regulated revenues and expenses with Part 64 adjustments explained
   e. ILEC may propose transition plan for reaching benchmark
   f. May elect to seek high cost support
      High cost support elements:
      i. High cost measured on wire center basis under cost standard set by Commission
      ii. COLR obligations established by Commission
      iii. One supported carrier per area for high cost purposes
      iv. All other service providers operating in the designated area are automatically relieved of COLR responsibilities, except to the extent of commitments for federal ETC status
      v. ILEC may opt for competitive status if no longer COLR

   g. Transition to Broadband
      i. Commission defines broadband goal
      ii. High cost areas for broadband operation, maintenance and deployment determined by Commission
      iii. Support for high cost areas is provided if needed to reach or maintain goal
      iv. Transitions old fund to new fund over ten years - begins after access reform goal is met

v. Standards established by Commission - not the same as High Cost Track, Phase 2

3) High Cost Track – applicable to areas traditionally served by ILECs with 2% or more of the state's access lines

Definitions:

Low cost areas – areas within the wire centers where the forward-looking cost per line is less than the high cost threshold.
High Cost areas – service areas where forward-looking cost per line is greater than $45 per month or in the alternative exceeds any national benchmark established through a federal USF/national broadband proceeding.

Phase 1 – support of existing multi-use networks

a. Eligible providers -
   i. Incumbent local exchange companies with 2% or more of state access lines.
   ii. Competitive local exchange companies

b. Funding of high cost (HC) areas - draws will be determined from forward looking cost model using the following criteria:
   i. Sub-wire center level granularity
   ii. HC sub-wire center level costs only
   iii. Offset draw using revenues from supported services within HC areas.
   iv. Each Carrier's support is capped at no more than it's existing support levels regardless of actual cost to serve it's existing HC footprint(shift from intrastate to interstate access rates, less additional revenues resulting from increases to local rate benchmark level).
   v. Each Carrier must, at a minimum, maintain existing broadband and voice deployment levels throughout its footprint, whether the entire HC area is funded (i.e. costs associated with serving HC areas exceed amount of phase 1 funding)
   vi. Carrier receiving support has COLR obligation

Regulatory treatment under Phase 1:

Low-cost areas with alternative providers with functionally equivalent services will be automatically classified as competitive. A facilities based provider or a designated CETC qualifies as a functionally equivalent service provider.

Phase 2 – State broadband plan – Triggered when "universal service" is redefined to include both voice and broadband services or if broadband speeds mandated[1]

Eligible providers -

- Incumbent local exchange companies with 2% or more of state access lines.
- Competitive local exchange companies
- All other facilities based service providers operating in High Cost Track areas

State plan must include the following:

- State sets out minimum deployment levels and targets required to be met to continue to receive funding.
- Competitively/technology neutral process
- A single "forward looking cost model" used by all applicants
- A process to designate a single COLR provider (either awarded or designated) per each high cost area
- Periodic reviews (five years minimum)
- Acknowledgement that awardees accept COLR obligations/responsibilities currently applied to ILECs for designated areas (not quasi-regulation as provided for in CETC model). All other applicants and/or providers relieved of state level COLR obligation.
- The same retail regulatory obligations will be applied to all awardee/designees without regard for technology type. ROR regulation will be eliminated and stream lined regulatory protection rules will identified and implemented.

Application process – Provider application must include the following:

1. Completed forward-looking cost data consistent with Commission approved high-cost model using its own costs.
2. Confirmation that provider willing and able to provide COLR responsibilities if awarded the HC area.
3. Broadband - Each applicant must submit a broadband plan consistent with the objectives and goals set out by the state, including a construction plan if needed to fulfill obligations under the plan.
4. Non-ILEC awardees acknowledge that within the awarded area the provider must submit to and comply with all current

[1] Is not triggered by commitments negotiated in settlement of adjudicated proceedings

Commission rules and regulations application to competitively classified companies.

5. Must agree to implement the Commission's prescribed local service benchmark (or impute to the benchmark).
6. Must file as part of its application file service extension plan consistent with WAC 480-120-071. Each plan will provide the following:
    a. Facilities based providers must apply distance based allowance consistent with ILEC treatment under the rule.
    b. Wireless/satellite providers must provide an auditable cost based allowance that replicates the distance sensitive allowance.
    c. Providers must track each customer request that involves a service extension, including the quote and the final resolution.
7. An applicant that must construct facilities to provision required service must do so within 12 months of being awarded the HC area Funding to begin once services are provided.

Evaluation and designation of COLR providers

- The State's evaluation process must balance the need to control the size of the fund with the long term sustainability of the applicants business plan and ability to provide quality services to high cost areas (i.e. Commission not bound to take lowest bidder).
- Should no non-ILEC providers apply to serve a HC area, the Commission may designation the ILEC as the COLR provider. USF support would be determined using an updated forward-looking cost model.

Regulatory treatment under this phase:

Low-cost areas with alternative providers with functionally equivalent services will be competitively classified. A facilities based provider or a designated CETC qualifies as a functionally equivalent service provider.

Unsupported service providers within a wire center are relieved of COLR responsibilities (except to the extent of commitments for federal ETC status) and are treated as competitively classified.[2]

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[2] Applies only to companies under the UTC's jurisdiction

4. Access reform all participating providers
    a. Reduce intrastate switched minute of use access charge rates to at least that company's composite interstate switched minute of use access rate levels or lower Commission prescribed level, maximum of over four years
    b. CLEC rates capped at ILEC rate for same serving area
    c. Commission set a single "benchmark" local service rate that includes EAS (not SLC) – move to the benchmark or impute the benchmark rate in order to be eligible to draw from WUSF Movement to benchmark not considered a general rate case.

APPENDIX 6

Overview of WITA Concept Paper

On September 1, 2010, WITA filed a "Concept Paper" in our proceeding, reflecting the organization's view of an appropriate state mechanism that it contends is a reasonable approach to protect and preserve universal service in Washington. Below we provide a summary of the major elements of the Concept Paper, subject to our understanding and interpretation of various provisions arising from discussions at our workshops and supplementary information submitted in our proceeding.

As a means to firm up their declining intrastate access charge revenue stream, and to preserve what WITA contends is a common "public switched telecommunications network" that is used extensively by other telecommunications companies that should be supported by such carriers, WITA proposes an intrastate access charge restructure mechanism that would shift a major portion of that revenue stream to a state universal service fund that would be broadly supported by contributions from all types of telecommunications carriers. The WITA Concept Paper envisions two state universal service funding approaches that differ materially depending on the size of the carrier to which funding may be directed: (1) smaller carriers that individually serve fewer than 2 percent of the telephone lines in the state, and (2) larger carriers serving greater than 2 percent of the telephone lines in the state. Each approach is discussed below.

A. Proposed support mechanism for small ILECs.

For those ILECs serving fewer than 2 percent of the access lines in Washington, state funding would be available to them for the direct financial effect of reducing their existing intrastate access charge rates to interstate rate levels offset by the calculated difference between their existing local rates and a statewide benchmark local rate the Commission would be authorized to establish prior to funding. The financial effect of reducing their intrastate access charges would be a onetime calculation that would establish a potential amount each small carrier would be eligible to receive from the fund subject to the following limitations and adjustments.

First, each carrier would be able to seek compensation from the state fund after subjecting itself to a "simplified earnings review" pursuant to which a carrier would be required to show that its existing overall rate of return does not exceed a reasonable level that would be

determined by the Commission.[1] Smaller carriers would be eligible for state funding only after application of a simplified earnings review and the Commission had been satisfied that support was warranted.

Second, for carriers passing the earnings review process, the amount of state funding they could be eligible for, determined as a consequence of reducing their intrastate access charges to interstate levels, would be further reduced by the difference between their existing local telephone rate levels and a statewide benchmark rate determined by the Commission.[2] WITA's access charge reduction proposal and the related offset associated with a local rate benchmark would be optional for each company. Additionally, the proposal would allow each company to propose a transition plan for local exchange rates that are lower than the Commission's benchmark rate as a means to mitigate adverse effects on consumers in their service area. Finally, the proposal for small carriers includes an option to seek additional state funding upon a showing of need and pursuant to some sort of determination of high cost by the Commission.

B. Proposed support mechanism for companies serving ILEC study areas with greater than 2 Percent of the telephone lines in Washington.

For local telephone companies serving more than 2 percent of the telephone lines in the state, the WITA Concept Paper contains a universal service proposal that would direct state support to carriers serving certain designated high-cost service areas. Under this aspect of WITA's proposal the Commission would be required to conduct a proceeding, or proceedings, to identify specific areas of the state where the costs of providing local telephone service exceed some predetermined measure of the standard or average cost of providing service, and the cost model would reflect detailed costing information on a "sub-wire center" basis.

High-cost areas would only include those areas where a second wireline-based carrier, such as a cable company, is not providing competing local telephone service. In essence, the

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[1] We note here that the Commission Staff and WITA representatives participated in several meetings to discuss an appropriate earnings review process should there be agreement on a new state universal service mechanism. Although agreement was not reached on an acceptable earnings review process, WITA represented, and the Commission understands, that the term "overall rate of return" would include a determination of each company's earnings using all of the revenues received by each carrier, regardless of whether the revenues are attributable to services that are regulated or unregulated.

[2] The benchmark is proposed as a way to avoid a continued subsidy to carriers that currently have exceedingly low local exchange rates relative to the prevailing local exchange rates in other areas of the state served by the larger ILECs.

existing local exchanges (i.e., individual service areas such as a town surrounded by suburban and rural areas) would be subdivided into areas where competition exists and where it does not exist. Areas where competition exists would not be eligible for high cost support and services provided by all telecommunications carriers in such areas would be classified as competitive telecommunications services pursuant to state law.[3]

In areas where competition from a wireline-based alternative carrier does not exist, a carrier serving that area would be eligible for state high cost funding according to a competitively neutral provider selection process that the Commission would be required to establish; a process that would occur approximately every five years. We understand that, under this aspect of the WITA Concept Paper, the Commission would be required to develop and implement some form of a forward-looking cost model to identify and determine costs of serving high cost areas of the state where state universal service support would be directed prospectively. Once modeled, the high costs identified for a particular area would be offset by the revenues received from "supported services"[4] derived in that area and by an amount determined as the difference between their current local rates and the statewide local service benchmark established by the Commission. Any remaining difference would be the amount that may be funded prospectively from a state universal service fund and any carrier receiving such support would be subject to specific carrier of last resort responsibilities.

C. Transition to Broadband

Although not a central component of the organization's proposal, the WITA Concept Paper does leave open the possibility of transitioning any state universal service fund to support broadband service at some point in the future should state policymakers wish to harmonize such funding with any prospective changes at the federal level involving subsidization of broadband services.

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[3] We understand that as an alternative to receiving high cost support, if such an approach is deemed unacceptable, all telecommunications services offered by a large carrier throughout their service territory in Washington would automatically be treated as competitive pursuant to state law.

[4] It is unclear what the scope is of the term "supported services." The Commission assumes it includes all telecommunications services including basic and enhanced services. We understand the term does not include a carrier's broadband service revenues unless or until a state fund was transitioned or redirected towards broadband service.

APPENDIX 7

Responses of Interested Parties to WITA Concept Paper

In response to a Commission Notice, seven interested parties filed comments on various aspects of the WITA Concept Paper. As would be expected, parties were generally divided on the merits of the proposal according to their own economic interests, with potential recipients supportive of WITA's proposal and potential contributors or competitors of the ILECs opposed to the proposal. This section summarizes the comments from the various stakeholders.

A. Supporters of Elements of the WITA Concept Paper

1. WITA

WITA points out that universal service has been the social policy of our state and nation for more than over seventy years and that the state reaffirmed this policy when the Legislature adopted the Regulatory Flexibility Act in 1985 and again in 1998 when it established RCW 80.36.300. WITA also contends that the 1996 Act affirms this policy at the federal level.

As a result of state law, WITA argues that the need to move from an implicit to an explicit funding mechanism has been on the books for several years and that the need to stabilize universal service has become much more acute because WITA's members are challenged to obtain the capital to build and operate the public switched network and fulfill their carrier of last resort (COLR) responsibilities. WITA points to significant changes in the telecommunications industry which it contends must be taken into consideration when drafting a state universal service mechanism. One such change is the introduction of nearly ubiquitous wireless services which means that rural carriers are no longer monopolies, though they continue to carry the legacy carrier of last resort obligations. Another is that access to broadband is now considered as important to our quality of life and commerce as telephones and electricity have been to previous generations.

2. Frontier Communications Northwest, Inc.

Frontier supports WITA's efforts to enable access charge reform and to create a state universal service fund. The company agrees with WITA that both are needed to insure the continued availability of affordable voice services and to support broadband deployment in high-cost areas of Washington. Specifically, Frontier believes that access reform, if not addressed in a separate proceeding prior to establishment of a state universal service fund,

should not be mandated but instead be a condition to be eligible for receipt of state universal service support. Frontier also believes that carrier of last resort responsibilities should be a condition to be eligible for receipt of state universal service support. The company also supports requiring all voice services; including wireless, VoIP and cable to establish a reasonable surcharge level and maintain competitive neutrality among all forms of voice communications service providers.

3. AT&T Communications of the Pacific Northwest, Inc.

AT&T does not support all aspects of WITA's proposal, but it does support a number of overarching principles: (1) reducing ILEC intrastate switched access rates to mirror interstate rates; (2) setting a single statewide local retail rate benchmark to which ILECs must raise local rates or to which local revenues will be imputed before any money can be taken from a state USF; (3) limiting support from a state universal service fund to a single provider per geographic area; (4) recognizing COLR obligations and universal service support are inextricably linked and limiting receipt of state USF support to the provider with COLR obligations; and (5) recognizing that plain old telephone service (POTS) will become obsolete at some point and the state universal service fund will need to change.

AT&T is expressly concerned with one element of the WITA Concept Paper: the notion that a LEC with fewer than 2 percnt of the access lines in the state may also be able to receive high cost support from a state universal service fund that would be in addition to any funds that the LEC would receive from the fund after rebalancing its local retail rates. AT&T believes that, at a minimum, any fund support above that which is necessary to rebalance access rates should be subject to a complete earnings review.

B. Opponents of Elements of the WITA Concept Paper

1. Verizon

Verizon does not support establishing a state USF and, therefore, does not support the proposals contained in WITA's USF Concept Paper contending they are both unnecessary and inappropriate. Verizon contends that intrastate access charge reform in Washington does not warrant the creation of a universal service fund because the use of such a fund would allow companies to continue recovering a disproportionate amount of their costs from other providers and their customers – and it will be Washington consumers that will be burdened with paying a state USF the surcharge on top of the current federal USF assessment.

2. T-Mobile Corporation

T-Mobile suggests that WITA's access reform proposal is conceptually unsound because it is premised upon the assumption that there should be dollar-for-dollar "universal service fund" recovery of revenues decreased as a result of intrastate access charge reform (net of revenues increases resulting from the benchmark rate), yet there is no requirement for any test showing that such an increase is necessary to actually preserve or advance universal service. T-Mobile also contends that the access reform proposal is contrary to federal law. Although 47 U.S.C. § 254(f) allows states to adopt programs to preserve and advance universal service in the state, and to assess providers of intrastate telecommunications services to fund such programs, it argues there is no authority to assess one provider in order to maintain the revenue levels of another provider.

T-Mobile also objects to the proposal for a "simplified earnings review," based only on total company regulated revenues and expenses. It argues that any state universal service funds would be used to support common plant providing regulated and unregulated services, and interstate and intrastate services. To the extent that revenue from those services in their totality is sufficient to avoid rates that would jeopardize universal service goals, there is no logical justification for universal service support for such common plant. Accordingly, the company argues that if access reform is adopted by the Commission, eligibility for such support must be tested against all revenues generated (in whole or in part) by facilities receiving universal service support, and not against a subset of those revenues.

Like AT&T, T-Mobile objects to the proposed high-cost support element of WITA's Concept Paper as discriminatory and anticompetitive because it would allow only one carrier in an area to receive high-cost support. It contends the likely effect of this is to prevent competition in these areas, since it is unlikely that any unsubsidized competitor would find it financially feasible to compete with another carrier that receives a subsidy.

Finally, T-Mobile suggests that any provisions related to the transition to broadband service should not be finalized until there is a decision on the specifics of how the recommendations of the NBP will be implemented. It argues that only after any federal broadband subsidy rules are implemented should the need for additional state broadband funds should be evaluated, and that any such funds should be made available through a process and in a manner consistent that decision.

3. Comcast

Comcast argues that because state USF contributions are paid ultimately by end users, it is necessary that those parties that advocate an industry-specific contribution explain whether the financial redistribution effected by such a proposal is desirable. The company asks whether it makes sense to effectively "tax" lower-income residents of Seattle in order to subsidize telephone service for all consumers in rural Washington. Comcast contends that the WITA Concept Paper is really a make-whole plan to offset access charge reductions and should not be adopted. It agrees with other opponents that the "simplified" earnings review is deficient because it excludes consideration of significant new revenues and profits from unregulated services.

Comcast agrees that intrastate switched access rates should be reduced at least to each company's interstate access rates and that existing ILEC local rates that are well-below a reasonable benchmark should not be maintained except for a very limited transition period. The company suggests that to the extent any subsidies are needed in order to keep local rates at below-cost levels, it is important that the benchmark not be set too low because it would lead to an unnecessary and inequitable subsidy from customers in one geographic area to another.

4. CLECs

The CLECs support the concept of an "earnings threshold" before a carrier can draw from a state universal service fund, but the CLECs believe that if a carrier is going to tax the end user customers of other carriers in the state of Washington through universal service fund contributions, then all ILEC revenues should be considered as part of the threshold test for eligibility to draw from the fund. Since non-regulated revenues, such as revenues from broadband offerings, have played some role in the reduction in access lines and access minutes, and these revenues are derived, in part, from the same network used to provide basic service to end user customers, the revenues generated from these services should be included. The CLECs suggest that the ability to "promote and preserve a rural telephone network is not dependent solely upon regulated revenues received as a result of that network, but all revenues generated from that network. Finally, the CLECs generally object to all of the proposals concerning the creating of state universal service funding of large ILEC local or broadband networks suggesting that it is not clear that a fund is necessary or that mandated reform at this time is even desirable.