Summary and State Implications
FCC Report and Order and Further Notice of Proposed Rulemaking

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Introduction

- We welcome the opportunity to provide Commission staff with an overview of the order and of the state role under the FCC-ordered changes. With such a lengthy and significant order, we continue the process of review and may have additional insight and reaction in the future.
- Much of the regulatory and implementation activity associated with the changes falls to the states and we look forward to working closely with Commission staff to interpret and implement the order.
- This overview generally addresses the FCC order as it applies to us and other companies that are price cap regulated at the federal level.

Federal Universal Service Principles Expanded to Explicitly Support Broadband

- The FCC created a new Universal Service Principle under Section 254(b): “Support for Advanced Services – Universal Service support should be directed where possible to networks that provide advance services, as well as voice services.”
- The FCC did not add broadband service to the list of supported services but instead required that the supported network be broadband capable and that all recipients offer voice and broadband services as a condition of receipt of Federal USF.
- The FCC did not alter state obligations regarding voice service, including COLR obligations, while noting the need to harmonize purpose and effect.
- The Supported Service definition was renamed “Voice Telephony Service” to be technology neutral; allowing VoIP to qualify. Access to operator services and directory assistance was dropped from the definition.

Federal Universal Service Reform: Phase I

The FCC order will transition present high cost USF support in price-cap areas to a larger Connect America Fund (CAF) program supporting broadband networks in targeted high cost areas.

<u>CAF: Phase I</u>

- Existing High Cost Support Mechanism: Legacy support levels are frozen at 2011 levels and were announced in February 2012. These amounts will be distributed on a monthly basis effective January 2012 until Phase II has been implemented.
- Phase I Incremental Support: Up to $300M additional funding will be made available to price cap carriers for the deployment of broadband.
- Incremental Support is calculated at the holding company level nationally based on the model currently used to determine high cost funding for non-rural carriers.
- Available funding amounts will be announced by the FCC 2Q; carriers can accept all, some, or none.

Federal Universal Service Reform: Phase I

CAF Phase I Obligations

- Within 90 days, the carrier must provide notice to the states of the amount of support it accepts and identify the areas by wire center and census block that it intends to deploy broadband.
- Frozen high-cost support must be used in a manner consistent with achieving universal availability of voice and broadband. If Phase I support is extended beyond 2012, the requirement to use frozen support for expanding broadband into currently unserved locations will phase in.
- Recipients of incremental CAF Phase I support must deploy broadband of at least 4/1 Mbps to at least one unserved location for each $775 in support it receives.
- Deployment of must occur in areas shown on the National Broadband Map as unserved at 768/200 Kbps. [pending PFR]
- 2/3 of locations must be built within 2 years; 100% within 3 years.

Federal Universal Service Reform: Phase II

CAF Phase II

- During 2012, the FCC will develop a forward looking cost model to estimate the cost of deploying broadband capable networks in high cost areas and to identify at a granular level where support will be available. Currently targeted for introduction in 2013.
  - ABC Plan proponents have submitted their model to the FCC for consideration.
- Supported locations will be in areas not served by an unsubsidized wireline competitor.
- Total available support for price cap carriers will be limited to the $1.8B annual budget.
- Annual support, as determined by the cost model, for a period of five years will be offered to each price cap carrier on a state by state basis in exchange for a commitment to offer voice service throughout its service area and broadband service to supported locations.
- Support will be awarded through a competitive bid auction for all areas where a price cap LEC declines the Phase II support.

Federal Universal Service Reform: Phase II

CAF Phase II Obligations

- By the end of the 3rd year, carriers must offer at least 4/1 Mbps broadband service to at least 85% of the high cost locations
- By the end of the 5th year, carriers must offer at least 4/1 Mbps broadband service to 100% of the high cost locations and 6/1.5 Mbps to a portion of the locations (to be identified by the CAF Model)
- Waivers can be sought for the 1 Mbps upstream requirement to the extent a carrier can demonstrate that the support is insufficient

Federal Universal Service Reform: State Roles

Eligible Telecommunications Carrier (ETC) Certification

- States maintain an ongoing role in annual ETC certifications.
- States now must certify all high-cost support was used in the preceding year and will be used in the coming calendar year consistent with purposes for which the support is intended.
- Annual certifications by the state must be filed by October 1 of each year in order for carriers to receive full support in the succeeding year.

Federal Universal Service Reform: State Roles

- States should take an active role in monitoring the FCC's development of the cost model for Phase II CAF funding and that broadband build out requirements and timelines are achievable.
- Broadband expansion into high cost areas will be jeopardized if unrealistically low amounts of support are available or build out requirements are not reasonable.
- With continued universal voice obligations and Federal high cost support increasingly focused only on broadband expansion in unserved areas, state high cost support remains a critical component to the maintenance of universal service at affordable rates.
- States should ensure that any state obligations, such as carrier of last resort, are consistent with and do not conflict with the new federal policies.

Intercarrier Compensation Reform: Summary

The FCC order sets forth several Intercarrier Compensation (ICC) reforms:

- The FCC adopted rules to address phantom traffic and access stimulation to address longstanding arbitrage issues.
- The order also determines that IP non-local traffic is subject to interstate access charges beginning January 1, 2012. It made no determination regarding the traffic prior to that date.
- The FCC issues a reconsideration order establishing bill and keep as the default rate for all intra-MTA traffic exchange with CMRS providers starting July 1, 2012.
- Interstate and intrastate switched access charges are defined as reciprocal compensation subject to the FCC authority under the Telecom Act and a default rate transition is set in motion.
- Default access charges remain tariffed but negotiated agreements are acceptable.
- NOTE: AT&T and CenturyLink have both filed limited appeals of the order and will participate in the case at the 10th circuit in Denver, CO.

ICC Reform: Switched Access Charge Transition

- All interstate and intrastate switched access charged are capped as of the effective date of the FCC rules; December 29, 2011.
- Default Intrastate terminating switched access charges are transitioned to parity with interstate in two steps; July 1, 2012 and July 1, 2013.
- Once parity is reached, Interstate and intrastate terminating switched access default charges for the majority of the elements are subsequently transitioned to bill and keep over the following four years.
- Disposition of the remaining access elements is the subject of a FNPRM at the FCC.

ICC Reform: State Roles

- Default intrastate switched access rates remain in intrastate tariffs throughout the transition.
- States should review intrastate switched access reductions through the transition to ensure compliance with the FCC rules for default intrastate switched access charges.
- Initial intrastate tariffs will be filed pursuant to state rules to be effective July 1, 2012.
- Intrastate tariffs will be updated to address the applicability of interstate access charges to IP-traffic.
- Incumbent providers will need maximum flexibility to adjust to significant switched access reductions to ensure there is no consumer or investment harm.

Retail Customer Impacts

- The FCC has placed a strict overall budget on the CAF support program to limit increases in the Federal USF contributions.
- Beginning July 1, 2012 carriers will be allowed to recover a portion of the lost ICC revenues through a transitional end user charge and, in some cases, additional USF support.
- The Access Recover Charge (ARC) will be calculated separately and likely combined with the SLC for billing purposes.
- For residential and single line businesses the ARC can increase no more than $0.50 per year up to $2.50.
- A residential rate cap of $30, inclusive of basic service and mandatory fees, also constrains the level of the ARC [pending PFR].
- The multi-line business ARC can increase no more than $1 per year, up to a maximum of $5, with the SLC+ARC no greater than $12.20.
- Additional PFR item seeks reconsideration of “collected revenues” instead of “billed revenues.”

Conclusion

- The FCC order is highly detailed and touches on many policy issues that are important to state policymakers.
- States have a key role in the reform process.
- The intent of the order is to simplify the existing intercarrier compensation system while advancing the goals of the National Broadband Plan by making broadband service available in unserved and underserved high-cost markets.
- State voice service requirements, including COLR, are not preempted so states must carefully examine their high cost support mechanisms, regulatory requirements, and competitive policies to ensure that any mandates are properly supported and that there is competitive equity among providers.
- We commit to working with Commission staff on how the order impacts individual states.