BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of Rulemaking to consider amending and adopting rules in WAC 480-120, telephone companies, and WAC 480-123, universal service, to implement legislation establishing a state universal communications service program.	Docket No. UT-131239

COMMENTS OF THE WASHINGTON INDEPENDENT TELECOMMUNICATIONS ASSOCIATION ON DRAFT USF PROGRAM RULES

October 10, 2013

INTRODUCTION

The Washington Independent Telecommunications Association (WITA) welcomes the opportunity to submit comments on the draft Universal Communications Services Program Rules as set out in the Commission's Notice of Opportunity to File Written Comments in Docket UT-131239. WITA appreciates the hard work that the Commission has put into developing these draft rules in a relatively short period of time. The draft rules represent a significant effort and a major step forward in implementation of the new Washington Universal Service Fund.

The format for these Comments will be to address a few of the basic concepts in the draft rules and then provide suggested language modifications in a mark-up (redline) of the draft rules. However, as a preface, WITA will express its understanding of the intent of the universal service fund legislation and its effect on WITA's approach in these Comments.

Under ESSHB 1971 (the "Legislation"), the Legislature focused on benefits that the new fund could provide to consumers served by rural incumbent local exchange carriers. For example, in Section 201(1)(a), the Legislature made the finding that:

> "The benefit that all consumers and communications providers derive from connection to the legacy public telephone network is enhanced by a universal service program that enables as many consumers to be connected to the public network as possible. . . ." (emphasis supplied).

The Legislature went on to find in Section 201(1)(b) that "Consumers in all areas of the state should continue to have access to communications services at reasonable rates." Thus, the clear focus of the Legislation is on using the new universal service fund to keep local rates reasonable for consumers. That is, to reduce the upward pressure on local service rates.

In Section 201(2) of the Legislation, the Legislature described changes that are occurring in the communications field, including changes in federal regulations governing intercarrier compensation and federal universal service support. With that backdrop, the Legislature found that:

> "These changes are adversely affecting the ability of some communications providers to continue to offer communications services in rural areas of the state of Washington at rates that are comparable to those prevailing in urban areas. These changes, absent explicit federal and state universal service support for such communications providers, may lead, in the short term, to unreasonable telephone service rate increases or cessation of service for some Washington consumers."

The Legislature concluded as follows: "Therefore, it is in the best interest of the state to ensure that incumbent local exchange carriers are able to continue to provide services as the carrier of last resort." It is this legislative direction that will guide WITA's comments.

COMMENTS

1. Section III related to eligibility and distributions from the program should not use 2011 or later for a base year for calculating lost access charge revenues.

WITA strongly urges that the Commission not use 2011 or any later year as a base year to calculate lost access revenues. The reason for this is that under the Connect America Fund (CAF), as administered by the Federal Communications Commission (FCC), any state USF support that could be said to be related to intrastate terminating access revenues that the FCC has addressed in its Order No. 11-161 or under its revenue recovery rules in 47 CFR 51.917 will lead to a reduction in federal support. See 47 CFR 51.917(d)(vii). In other words, if a state fund is replacing revenues that the FCC is funding through the CAF, the CAF funding will be reduced.

The result is that there is no new revenue available to the recipient companies. Obviously, that result would not comport with the intent of the Legislation to reduce upward pressure on residential rates.

The reason the CAF support reduction related to access replacement in a state USF fund based on 2011 or later access loss occurs is that the FCC starts the CAF support calculation with a "2011 Rate-of-Return Carrier Base Period Revenue" (Baseline Revenue) as defined in the FCC's rules.[1] The Baseline Revenues consist of three categories of revenues: (1) the interstate access revenue requirement; (2) the revenues received by the carrier from intrastate terminating access rates in the 2011 federal fiscal year (October 1, 2010 through September 30, 2011) and; (3) the net reciprocal compensation for that same fiscal year. For each year of the CAF program, CAF support for a carrier is calculated using a comparison of (1) the revenue projected to be received from the three categories of revenues described above in that year with (2) the Baseline Revenues, subject to mandatory reductions which are discussed below.[2] Using a 2011 or later year as the baseline for the new state fund calculation will overlap the CAF calculation and result in a reduction of federal CAF support.

This is why in its September 4, 2013 Reply Comments: Data Presentation and Recommendation, WITA recommended as the third step of the new universal service fund that the lost access revenue from between 2007 and 2010 be used. This approach avoids the overlap with the FCC's CAF recovery calculation.[3] WITA's Reply Comments demonstrated that during

[1] 47 CFR 51.917(b)(7)
[2] See, e.g., 47 CFR 51.917(d)(ii)
[3] See WITA's Reply Comments: Date Presentation and Recommendation at pages 7-11 (September 4, 2013).

this period of time, a reasonable approximation of the lost access revenue due to access bypass and call termination problems for its eligible incumbent local exchange carrier members is in the neighborhood of 5.4 million dollars. This was based on an examination of data from the Washington Exchange Carrier Association (WECA). It should be noted that WECA has filed data with the Commission on an annual basis. Therefore, the Commission has the means to confirm WITA's estimates by reference to the WECA annual reports that have been filed with the Commission each year.[4]

Given that the fund is capped at 5 million dollars in distributions on an annual basis and that in the neighborhood of 1 to 1.2 million dollars will be used to replace the traditional universal service fund rate element revenue, the loss of access revenue far exceeds the availability of funds from the new universal service fund.

An important factor is that in addition to the foregoing, the FCC is reducing CAF support by five percent per year.[5] This, in itself, represents a significant upward pressure placed on residential rates. This is a product that results from the way that the FCC has designed the CAF. The FCC assumes that carriers can become "more productive" at the rate of five percent a year without anything other than the reduction of funding.

Whatever one thinks of the wisdom of this decision, the practical effect of the reduction in CAF support is to put upward pressure on residential rates. The amount of the CAF reduction

[4] Please keep in mind that WECA administers non-traffic sensitive access rates and the traditional universal service fund rate element. Traffic sensitive access rates are administered by each company on its own. Generally, traffic sensitive access rates have exceeded non-traffic sensitive rates in financial scope. This can be confirmed by reference to company tariffs on file with the Commission.
[5] 47 CFR 51.917(b)(3) and, for example, 47 CFR 51.917(d)(i).

is set out on Exhibit 1. The CAF reduction for 2012 and 2013 is $1,418,423. This figure is calculated by the National Exchange Carrier Association using the information from the FCC's Baseline Revenue calculation. It is estimated that in 2014, another reduction of $650,993 will take place, putting the loss in CAF support for WITA's eligible carriers at over $2,000,000 by the time the Washington USF program is implemented.

So what should happen with all these events and possible adverse consequences? WITA recommends that the state universal service fund support be used first to replace the traditional universal service fund element of approximately 1.2 million dollars.[6] Then, as a second step, the universal service fund support be used to offset CAF reductions of approximately 2 million dollars in 2014, and growing each year. The third piece is to use the residual universal service revenues to replace lost access revenue for the period preceding the CAF.

The traditional universal support rate element revenues are known and easily verified through WECA. CAF reductions are calculated by the National Exchange Carrier Association and again are a readily known and available basis to determine the amount of needed support. The attached Exhibit 1 sets out not only the CAF reductions, but also shows the loss of traditional universal service support. When these amounts are taken into account, for the first year that the universal service fund will be in effect, there is only 1.7 million dollars of revenue that could be used to replace lost access revenue. The estimated 5.4 million dollars in lost access revenue certainly dwarfs that amount. WITA recognizes that the use of calendar year 2010 in

[6] As pointed out in WITA's Comments on the Commission's Specific Questions filed of even date herewith, the recovery of the traditional universal service fund element revenues should be without reference to a rate of return entry threshold.

the estimate has a three month overlap with the 2011 fiscal year used by the Federal Communications Commission. However, when the lost access revenue is compared to the amount of support available (5.4 million dollars compared to 1.7 million dollars), it is very easy to be able to make the case that support from the state fund is not duplicative of the support from the CAF.

In addition, as CAF reductions increase, the amount from the state program available for access revenue loss replacement decreases. Attached as Exhibit 2 is a table that shows the amount of the Washington program support for CAF reductions increasing over the five years and the amount of lost access revenue support decreasing and ultimately disappearing altogether.

Once it is recognized that there is some lost access revenue recovery, then it must be decided how to distribute that amount among the companies. WITA looked at several possible alternatives. What WITA has ultimately recommended to the Commission is use of the WECA distribution ratios.[7] There is a direct link between these distribution ratios and access revenue since that is how the money in the WECA pools are currently distributed. Further, the WECA distribution ratios have received Commission approval in Docket UT-971140 and subsequent docket filings. Thus, this approach would use a Commission approved ratio which is directly related to access pooling. Employing these distribution ratios would reflect some level of recovery of lost access revenues not associated with CAF recovery through the residual amounts available under the new universal service fund.

[7] See WITA's Reply Comments: Data Presentation and Recommendation at pages 11-14 (September 4, 2013). WITA recommends adjusting the distribution ratios using strata related to how well or poorly a company is earning.

WITA provides suggested language for Section III(2) addressing this issue in the redline of the draft rules that accompanies these Comments.

2. The use of rates above the urban rate floor is not appropriate.

In Section I(1)(d), the draft rules propose as a prerequisite for eligibility that the residential rates of a carrier be x% above the urban rate floor. As noted by the Commission's draft rules, the urban rate floor consists (at least in Washington) of the rate for residential local exchange service plus mandatory extended area service.[8] The actual rates paid by residential customers are actually much higher than the residential urban rate floor as used by the Federal Communications Commission. The rate that residential customers pay includes the subscriber line charge, the access recovery charge, the assessment for E-911 service and state sales tax. Exhibit 3 sets out the rates that customers actually pay for service. As the Exhibit shows, the actual out-of-pocket charge for residential service ranges from $24.66 per month to $35.33 per month.[9] It would not be appropriate to require rates to be higher than these levels to participate in the fund. That requirement by itself would put upward pressure on residential rates for many companies. The result appears to be contrary to the intent of the Legislation.

If the Commission were to adopt any percentage above the urban rate floor, at least twelve of the potential eligible companies would need to raise rates in order to draw from the fund in order to be able to further reduce the upward pressure on residential rates. It would be an ironic situation that customers would have to endure Commission initiated rate increases to be

[8] The rule used "mandatory exchange area service charges" but WITA believes that is a typographical error.
[9] It is expected that the urban rate floor will increase in 2014. Thus, these rates most likely will be even higher.

sure that further rate increases are not imposed because the company cannot draw from the state universal service fund without raising residential rates.

In its initial Comments in this docket, WITA pointed out that there may be competitive reasons why a company may not raise its rates to the urban rate floor. In summary, the act of raising rates to the urban rate floor may cause a migration of customers which would put increasing upward pressure on residential rates. This could potentially lead to an unsustainable cycle. In recognition of that possibility, WITA's recommendation is that the urban rate floor not be used as a bar to participation, but as a test of the level of where rates should be. This means that if a company has residential rates below the level of the urban rate floor, it would face an imputation of revenue that would assume that the rates were at the urban rate floor level and this difference would be subtracted from what it otherwise would be able to draw from the fund. This is how the Federal Communications Commission applies the urban rate floor. Thus, use of the benchmark for imputation, not as a bar, remains WITA's recommendation.

3. The Commission should not require audited financial statements.

Under Section II(1)(e), the Commission is requiring audited financial reports. Under Section II(1)(f), the Commission is requiring that FCC Form 481 be filed with it as part of the petition. For privately-held rate of return companies, the two items contain the same financial information. FCC Form 481 is extremely detailed and requires privately-held rate of return carriers that receive loans from the Rural Utility Service (RUS) file electronic copies of their annual RUS reports. For those privately-held companies that are not RUS borrowers and have

financial statements that are audited in the course of business, they must provide either a copy of their audited financial statement or a financial report in a format comparable to the RUS Operating Report, accompanied by a management letter issued by an independent certified public accountant that performed the company's financial audit. See 47 CFR 54.313(f)(2). If audited financials are not available, then reviewed financials are acceptable. The FCC found use of the RUS Form 479 as part of FCC Form 481 appropriate.[10] As a result, in the draft rules the Commission is, in essence, requiring the same information to be submitted twice by privately-held companies.

In addition to the foregoing, there are three WITA members that are privately-held rate of return companies that would otherwise be eligible to receive support that do not have audited financial statements. It would be inappropriate to exclude those companies solely on the basis of a lack of audited financial statements or, alternatively, forcing those three companies to pay for an outside auditor to prepare the three last years of audited statements.

Those three companies do, however, have reviewed financial statements. This means that there is a third party looking at the company's financial statements and making some conclusions about their appropriateness. Use of either audited or reviewed financial statements, which are the basis for FCC Form 481 reporting, should give the Commission sufficient assurance that the financial statements that they are receiving in the Form 481 have passed

[10] See the discussion in the FCC's Transformation Order, FCC 11-161, at paragraphs 595-602 and the Fifth Order on Reconsideration, FCC 12-137, at paragraphs 7-12.

inspection from a third party and is not just a company preparing its own financial numbers.[11] Thus, the Commission reaches its objective through the requirement of filing Form 481.

It is important to consider that there are five WITA members that are operating company subsidiaries of one of two publicly-traded companies (FairPoint Communications and TDS Telecom), and these operating companies do not have operating company level audited financial statements. Nor do these companies have the requirement to file audited financial statements with their Form 481. The rules should allow these companies to either file operating company level audited financial statements or file a copy of their most recently completed consolidated audit report of the publicly-traded company along with unaudited financial statements for each operating company.

WITA questions why three years of financial statements are needed. That appears to be excessive. WITA suggests that one year of financial records be provided. However, please note that by requiring the use of FCC Form 481, the Commission will receive two years of balance sheets and income statements. Perhaps this level of reporting is an acceptable compromise.

4. Carriers should not have to apply for each of the five years of the existing life of the fund.

Under Section II(1), the draft rules provide that a carrier must petition each year to be eligible to receive support. That proposed requirement places a substantial financial burden on each company given the amount of information that has to be provided with each petition. The

[11] This is also what the FCC found to be acceptable. See the FCC's Fifth Order on Reconsideration, FCC 12-137, at paragraphs 9-10.

significant administrative costs do not seem to be warranted given that the Commission is asking for such detailed financial information. In addition, it is difficult without at least a modicum of certainty for companies to make investments and plan service improvements. For this reason, WITA suggests that, at a maximum, carriers need to apply every other year.

5. The greatest chance of protecting ratepayers is to make distributions as early as possible.

Under proposed Section III (5),[12] the Commission has set the date for making decisions on funding as January 1 of the program year. This leads to the conclusion that funds will not be distributed until after January 1. Given that the intent of the new universal service program is to reduce as much as possible the upward pressure on residential rates brought about by unprecedented changes in the telecommunications industry, it is logical that the earlier the distributions can be made, the greater the benefit to the customers. This is because the earlier the distribution is made, the greater chance that upward pressure on residential rates will be alleviated. This nexus between distribution and meeting the intent of the Legislation compels WITA to ask the question of whether the dates contemplated by the draft rules can be moved forward to accommodate earlier distribution.

6. Section II(1)(h) should focus on telecommunications services.

In Section II(1)(h), an affidavit is required by an officer of the provider to certify that the provider will continue to provide "communications services pursuant to its tariffs on file with the

[12] In WITA's redline of the draft rules, this becomes subsection (6).

Commission. . . ." There are two issues with this language. The first is the use of the term "communications services" which includes information services. The second is the reference to "tariffs".

WITA recognizes that there is an internal conflict within the Legislation concerning the affidavit or certification that must be provided related to the continuation of services. In Section 203(2) of the Legislation, the obligation to provide assurance of continued operations reads that the provider must agree to "provide continued services under the rates, terms, and conditions established by the commission under this chapter for the period covered by the distribution." On the other hand, Section 203(4)(b) states that there must be an affirmative consent "to continue providing communications services to its customers under rates, terms, and conditions established by the commission pursuant to this chapter for the period covered by the distribution." Thus, Section 203(1) references the provision of "continued services" and Section 203(4)(b) references "communications services." Since the apparent intent of the Legislation is to reduce upward pressure on residential rates (please reference Section 201(2) of the Legislation) and to support the legacy public telephone network (see Section 201(3) of the Legislation) it is a reasonable conclusion that the services referenced in Section 203(2) refer to basic telecommunications services as that term is defined in Section 202(1)(b).

By contrast, communications services are defined in Section 202(1)(d) to include general telecommunications services and information services and any combination of the two. Since the Legislation contemplates that the affirmation of continued service is under the "rates, terms, and conditions established by the Commission under this chapter" and the Commission does not

regulate information services,[13] the necessary implication is that the affirmation relates to telecommunications services, not to "communications services" which include information services. This would appear to be the most logical and consistent interpretation of the apparently conflicting language.

The proposed rule language focuses on services under "tariff." However, the Legislation uses the terms "rates, terms, and conditions established by the Commission under this chapter." The distinction is that the Commission has the authority that goes beyond approving tariffs. For example, the Commission could approve an alternative form of regulation for an incumbent local exchange carrier. That alternative form of regulation could contain "rates, terms, and conditions established by the Commission under this chapter." Thus, the use of the more restrictive term "tariffs" might preclude a possible alternative form of regulation. WITA's suggestion is that use of the statutory language allows more flexibility.

WITA has suggested language in the attached redline of the draft rules which addresses these two issues.

7. The Commission should repeal its existing ETC reporting rules.

The draft rules do not contain any repealing language. Given what eligible telecommunications carriers (ETCs) will be required to report at the federal level, including but not limited to, the very extensive FCC Form 481, the Commission should give strong

[13] Indeed, it may well be that the Commission is preempted from regulating information services by actions of the Federal Communications Commission.

consideration for repealing its existing ETC reporting rules. The reports that are filed at the federal level are required by federal rule to also be filed at the state Commission.[14] Therefore, the Commission will be receiving extensive reporting about ETC activities. These reports include written explanations supporting required certifications of a carrier's ability to operate in emergency conditions and its compliance with quality of service and consumer protection standards. And, as discussed earlier, very extensive financial reporting information will be provided. As it now stands, ETCs will also be providing five year plans showing their construction and improvement programs. As a result, WITA urges the Commission to give strong consideration to repeal the existing ETC reporting rules in WAC 480-123-070 and 080.

8. The Commission should develop substantive wireless standards.

WITA understands and appreciates that the primary focus of these rules is to ensure that program operating rules are in place to implement the state universal service fund for wireline carriers. WITA also understands that, at this stage, it is speculative whether any wireless carrier will apply to receive funds out of the new program. However, that does not mean that the Commission should defer the consideration of wireless standards indefinitely.

Instead, WITA suggests that the Commission move forward with the rules in their present configuration, with the amendments WITA is recommending in these Comments, but immediately initiate additional rule making to address wireless standards once the current proposed rules are adopted and in place. The Commission and the industry should think through

[14] See, e.g., 47 CFR 54.313(i)

the standards that should apply to wireless carriers in advance and not be in a reactive mode and possibly be unprepared if a wireless carrier indicates a desire to make an application to participate in the program.

9. Rule language.

Attached is a redline markup of the Commission proposed draft rules with suggested language changes to address the issues set forth in these Comments and other matters. It is important to note that there are additional substantive matters addressed in the attached markup along with questions about why certain language is used or what is intended.

CONCLUSION

Thank you for your consideration of these comments. WITA is very supportive of the direction the Commission is moving and appreciates all of the very hard work the Commission has put in on this rulemaking to date.

Respectfully submitted this 10th day of October, 2013.

WASHINGTON INDEPENDENT
TELECOMMUNICATIONS ASSOCIATION

By: _____
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