BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 1481

In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Investigation Into The Oregon Universal Service Fund	STAFF'S CLOSING COMMENTS

The following comments are structured to address a number of key points that were brought up during the workshops and in the initial round of comments. These comments will focus strictly on the current Oregon Universal Service Fund (OUSF or Fund) and will not address broadband except as it relates to the broader issues of the wireline network. The six main issues that are addressed are the following:

- Is there a continuing need for the OUSF?
- Has the OUSF money been spent as intended?
- What changes should be made to the fund to make it more efficient?
- Which companies should be allowed to receive money from the Fund and on what basis?
- Should all revenues derived from the network be considered in calculating support?
- Should the support base of the Fund be expanded?

1. Is there a continuing need for the OUSF?

Yes. The OUSF was brought into existence by ORS 759.425 to help meet the needs of Oregon residents for affordable, basic telecommunication service. The underpinning of ORS 759.425 was the principle laid out in Section 254 of the Telecommunications Act of 1996. Since 1996, the need to have affordable and reasonably comparable service has not changed. As explained below, the same conditions that produced the policy statement still exist: low income consumers and pockets of high cost service produced by low densities, difficult terrain, or a combination of both.

Service Being Provided by Unsupported Competition
Some commenters have argued that affordable basic local telephone service is already available to all citizens of Oregon and that this availability is due at least in part to unsubsidized competition that has sprung up over the past years. Based upon this allegation, these commenters then conclude there is no future need for OUSF support.

Although unsupported Competitive Local Exchange Carriers (CLECs) and wireless companies account for a significant portion of the market, the wireline companies still account for over one million lines and the non-rural companies account for over 150,000 of the one million lines. Clearly, Oregon is not at the point where there are just a few wireline customers left. Indeed, there are 350,000 customers in high cost areas that are currently receiving support.

The point made by the Oregon Telecommunication Association regarding unsupported competition is a good one: even in a high cost area there are relatively high density pockets where the cost of providing service is relatively low. By targeting these relatively low cost areas, competitors are able to provide service without support, but leave the average cost of the remainder of the area at a higher level. In other words, there is no longer a lower cost area to average with the high cost one. The remaining area typically is not attractive because the cost of providing service there generally makes it unprofitable to do so.

A State-Level Universal Service Fund (USF) Allows More Control
Even though there is both a state and a federal USF, the small companies have been relying on both funds. When state USF support is calculated for one of the rural companies, the federal USF that the company receives is used to reduce the state USF support dollar-for-dollar.

One of the real values of a state-level USF is that it reduces the reliance of the companies based in Oregon on the federal USF and allows the state to have more control over how the funds are used and the rate Oregon customers pay.

2. Has the OUSF money been spent as intended?

Yes, as explained below, both the rural and non-rural companies have followed the directions of the Commission and the statutes in the way that they used the OUSF funds. The rural companies used the Fund to reduce the Carrier Common Line (CCL) element of their access charges and the non-rural companies used it to reduce a set of rates that they found at the time to be above their economic cost.

The Present Structure of the OUSF
There are presently two distinct funds, based on how the money is used, that make up the OUSF: one fund is primarily directed toward the non-rural companies and the other is directed toward the rural companies. The level of support for non-rural companies, and how it is to be used, was established in Phase IV of Docket UM 731. The level of support for the rural companies and how it is to be used was established in Docket No. UM 1017.

The non-rural companies were directed to reduce certain business and non-basic service prices to the point where the reduction in revenues generated by those products and service would equal the OUSF support that they would be receiving. The rural companies were directed to use the OUSF support to reduce access rates by using it to offset the revenue requirement for the CCL component of those rates.

Requirements Imposed on the Non-Rural Companies
Shortly after the order was issued to reduce certain business and non-basic service prices, both non-rural companies filed proposed rates with the Commission along with supporting work papers. The work papers illustrated how the increase in revenues from the OUSF was offset by a reduction in revenues from the designated services. Aside from the reduction in the above mentioned rates, no other actions were required by the two companies.

Requirements Imposed on the Rural Companies
Every year the Oregon Exchange Carrier Association (OECA) files intrastate tariffs with the Commission along with supporting documentation for the Commission to review. This documentation consists of financial statements (Form-O and a budget for the upcoming year) and separation statements (Form-I, Part 36 and Part 69 separation reports). As part of the process of developing these rates, the revenue requirement for the CCL element is reduced by the amount of OUSF support that a company receives. This is done on a company-by-company basis. With the exception of some residual amounts, where the OUSF support for a company exceeds the CCL revenue requirement, the support the companies receive is used to reduce access rates.

3. What changes should be made to the Fund to make it more efficient?

Although this docket is not the proper forum for making changes to the OUSF, it is the proper forum for suggesting changes that should be discussed in a future, more focused docket covering how the Fund should be modified to make it more efficient and more in line with present universal service objectives.

Non-Rural Companies
Frontier's acquisition of Verizon illustrated the disparity between the networks that are provisioned in the high-density, lower-cost areas and those that are provisioned in the high cost areas. Although a network capable of handling broadband service is outside the scope of the present Fund, the presence, or lack thereof, of such a network is a good indicator of the non-rural companies' willingness to invest in a given geographic area. Over the past 10 years, Verizon was provided approximately 150 million dollars from the Fund (Qwest was given approximately 200 million dollars) yet little of this flowed to improving the networks in the high cost areas. To address this issue, the Commission added a condition to the merger requiring Frontier to upgrade the networks in those areas so they were reasonably comparable to the higher density areas around Portland.

It is important to note that this is not to say that Verizon misused the funds these past years. The focus of the early orders and rules was on keeping specific rates down, not on producing reasonably comparable facilities at an affordable rate.

Rural Companies

The rural companies, since Order No. 03-082 (Docket No.UM 1017), have each year used the OUSF support to reduce the CCL component of the intrastate access changes. The intent of Order No. 03-082 was to reduce access rates while keeping the line rates at a level that was reasonably comparable with the rates of higher density areas. Over time, the intrastate minutes started to erode due to competition, and the CCL revenue requirement started to increase as the companies invested in modernizing their local loops.

Over the past several years, the volume of OECA Pool minutes[1] has dropped precipitously. Indeed, the current forecast is for an annual drop in excess of 15 percent, which is a slight acceleration from the prior year's erosion rate. This loss in minutes, along with dropping line counts which determine the amount of support a company receives, has resulted in a combined terminating access rate approximately five times greater than the average interstate rate. This will only get worse in the future as intrastate minutes drop.

One possible solution for discussion would be to go to a uniformly-priced minute for all classes of traffic handled by the switch. The cost of local calls would be assigned to the line charge and the other various classes of usage would be assigned on a per minute basis to the user. The OUSF would be used to keep the rates relatively comparable.

4. Which companies should be allowed to receive money from the Fund and on what basis?

Presently, the Fund allows any company that passes the hurdle of becoming an Eligible Telecommunications Company (ETC) for a given geographic area to receive support in that area based on the incumbent's local exchange carriers' cost for providing service to the entire franchised area. This allows CLECs to enter the higher density areas where the cost of providing service is generally lower than the average cost of service and receive support as if they were incurring the average cost.

This type of supported entry is undesirable for a number of reasons: the company entering the market takes more money from the Fund than it would be entitled to receive based on its own costs; it drives up the unit cost of the company serving the area; and it not a good use of OUSF money. The Fund should focus on ensuring that reasonably comparable networks at affordable rates are being developed. It should not be used for inefficient entry into the market.

There is an exception when a CLEC enters the market area using its own facilities and completely takes over a franchised area with superior service. Under these circumstances, the CLEC should be entitled to support based on its cost. If the

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[1] The rural companies in the pool use a single set of intrastate rates developed by dividing each rate element's revenue requirements, developed for all of the companies, by the element's projected total minutes, which is the sum of each company's minutes.

incumbent is not keeping the facilities reasonably comparable, the new entrant should be rewarded for its entry into the area.

5. Should all revenues derived from the network be considered in calculating support?

An important goal of the OUSF is to support the deployment and maintenance of networks that would otherwise not be deployed because it is uneconomical to do so. To make this determination regarding the economic viability of a network, it is necessary to take into account all of the revenues generated by the network, not just a subset of the revenues. If the local loop is supporting a range of broadband services (e.g. internet, video) as well as voice, the determination of the economic viability of the network has to take into account all of the revenues from these services, not just the revenues from the voice services.

6. Should the support base of the Fund be expanded?

Funds for the OUSF are presently collected from only a portion of the users of the public switched telecommunications network (PSTN). Users whose calls originate on a cell phone are exempt by statute [ORS 759.425(7)]) from contributing to the fund even though they use the PSTN, just like the customers that pay into the fund. This exclusion of classes of PSTN users results in a surcharge rate that is two to three times greater than what it would be if all users of the PSTN were contributing to the Fund.

This concludes Staff's Closing Comments.

Dated at Salem, Oregon, this 23rd day of November 2010.

Roger White
Program Manager
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CERTIFICATE OF SERVICE

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Closing Comments

I certify that I have this day served the foregoing document upon all parties of record in this proceeding by delivering a copy in person or by mailing a copy properly addressed with first class postage prepaid, or by electronic mail pursuant to OAR 860-13-0070, to the following parties or attorneys of parties.

Dated at Salem, Oregon, this 23th day of November, 2010.

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