LAWYERS

Davis Wright Tremaine LLP

ANCHORAGE BELLEVUE LOS ANGELES NEW YORK PORTLAND SAN FRANCISCO SEATTLE SHANGHAI WASHINGTON, D.C.

MARK P. TRINCHERO
Direct (503) 778-5318
marktrinchero@dwt.com

SUITE 2300
1300 SW FIFTH AVENUE
PORTLAND, OR 97201-5630

TEL (503) 241-2300
FAX (503) 778-5299
www.dwt.com

February 8, 2006

Public Utility Commission of Oregon
Attention: Filing Center
550 Capitol Street N.E., Suite 215
Salem, OR 97301-2551

Re: UM 1217

Dear Filing Center:

Enclosed, for filing, are an original and five copies of the Rebuttal Testimony of Don J. Wood on behalf of RCC Minnesota, Inc. and United States Cellular Corporation, in the above referenced docket.

Very truly yours,

Davis Wright Tremaine LLP

Mark P. Trinchero

MPT:bl

Enclosures

cc: Service List

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

RCC MINNESOTA, INC. ("RCC")
AND
UNITED STATES CELLULAR CORPORATION ("USCC")

Rebuttal Testimony
Of Don J. Wood

February 2006

Purpose of Testimony

Q. **PLEASE STATE YOU NAME AND BUSINESS ADDRESS.**

A. My name is Don J. Wood. My business address is 30,000 Mill Creek Avenue, Suite 395, Alpharetta, Georgia 30022.

Q. **ARE YOU THE SAME DON J. WOOD WHO PREFILED DIRECT TESTIMONY ON BEHALF OF RCC MINNESOTA, INC. ("RCC") AND UNITED STATES CELLULAR CORPORATION ("USCC") ON DECEMBER 13, 2005?**

A. Yes.

Q. **WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

A. The purpose of my testimony is to respond to the direct testimony of Mr. Brant Wolf on behalf of the Oregon Telecommunications Association ("OTA"), Mr. Orville D. Fulp on behalf of Verizon Northwest, Inc. ("Verizon"), Mr. Dennis Pappas on behalf of Qwest Corporation and Malheur Home Telephone Company ("Qwest" and "Malheur"), and Ms. Kay Marinos on behalf of Commission Staff ("Staff").

Q. **DO YOU HAVE ANY OVERALL OBSERVATIONS REGARDING THE DIRECT TESTIMONY?**

A. Yes. It appears that on several issues, there is little difference in the stated positions of the parties. On other issues, particularly with regard to the reporting requirements of competitive ETCs ("CETCs")and ILECs, and regarding the best means of ensuring that so-called "creamskimming" will not occur (assuming that any action is needed to minimize the potential for this already highly unlikely

event), important distinctions do exist. I will address each of the identified issues in turn.

I. Public Policy Objectives

What policy objectives should the Commission attempt to achieve through this docket? (Issue I(A))

Q. **IN YOUR DIRECT TESTIMONY, YOU STATE (P. 4) THAT "THE OBJECTIVE OF THIS PROCEEDING SHOULD BE TO ENSURE THAT THE PROPER FRAMEWORK IS IN PLACE TO PERMIT THE FEDERAL USF PROGRAM TO OPERATE IN OREGON AS IT IS INTENDED TO OPERATE: IN A WAY THAT BRINGS BENEFITS TO CONSUMERS IN HIGH-COST, RURAL, OR INSULAR AREAS." DO THE OTHER PARTIES AGREE WITH YOUR STATEMENT OF POLICY?**

A. Generally yes, although as I will explain below the ILEC witnesses then go on to propose policy that focuses on providing benefits and protection for ILECs rather than for consumers.

At pp. 4-5 of her testimony (and explained further at pp. 13-21), Staff witness Marinos provides a list of eight policy objectives that represents a clear articulation of a sound public policy that should be adopted by the Commission:

> 1. Consistency with the universal service principles in the Telecommunications Act of 1996 that consumers in all regions of the state, including low-income consumers and those in rural, insular, and high cost areas, should have access to quality telecommunications services, including advanced and information services, that are reasonably comparable to those services provided in urban areas, and that are available at just, reasonable, and affordable rates comparable to those charged for similar services in urban areas;

2. Consistency with the principles of competitive and technological neutrality;

3. Adherence to the mandatory requirements and constraints imposed by the Act and the FCC rules;

4. Achievement of the most cost-effective and efficient use of support funds possible under the current federal system;

5. Direction of support into areas with the greatest need based on local characteristics and not whether the ILEC in the area is classified as "rural" or "non-rural".

6. Encouragement of the growth and expansion of telecommunications platforms capable of providing broadband and advanced services into areas where the market economics would not justify deployment without support;

7. Provision of support only to carriers that are able to provide the required services and are committed to shouldering the responsibilities that accompany support; and

8. Clear communication to current and prospective ETCs of the Commission's expectations regarding their responsibilities associated with the receipt and use of support funding.

Q. **WOULD YOU ADD ANY POLICY STATEMENTS TO MS. MARINOS' LIST?**

A. While I believe that each objective on her list represents sound public policy, I would add two additional principles:

9. Complete and thorough accountability of the use of all USF support received by both competitive ETCs and ILEC ETCs, based on information collected during the annual recertification process; and

10. Efficient monitoring of an ETC through reporting requirements that reflect the market power and position of each competitive ETC or ILEC ETC.

Q. **DO THE ILEC WITNESSES AGREE WITH YOUR STATEMENT OF POLICY?**

A. At a high level, yes. Mr. Wolf states (pp. 3-4) that the policy objective of the Commission when considering the designation of an ETC should be to ensure "the accomplishment of the policy objectives contained in section 254," and that the Commission should adopt an annual recertification process that "is cost efficient, yet provides accountability in the use of federal high-cost funds." I agree with both of these statements.

Mr. Wolf goes on (p. 4) to list several principles "that Congress established for universal service set forth in section 254": (1) quality services should be made available at just, reasonable, and affordable rates; (2) there should be access to advanced telecommunications and information services in all regions of the nation; (3) consumers, including low income consumers and those in rural, insular, and high cost areas should have access to telecommunications and information services, including interexchange services and advanced telecommunications services that are reasonably comparable to those provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas. Again, so far so good.

Mr. Wolf then ignores the principles that he has just listed and declares (p. 4) that "*the* principle of Universal Service is straight-forward – to ensure that 'all Americans have access to affordable, quality telecommunications services'" (emphasis added). While this is certainly *a* principle of universal service, and prior to the Congressional statements of policy in the 1996 Act (quoted and then

ignored by Mr. Wolf) may have been a principal policy, it is clearly not the only federal policy in effect today. In fact, what Mr. Wolf asserts to be "*the* principle of universal service" does not actually appear in the 1996 Act at all.

Q. **MR. WOLF SUGGESTS (P. 5) THAT PUBLIC POLICY SHOULD REFLECT THE FACT THAT RURAL ILECS "FACE SUBSTANTIAL ECONOMIC CHALLENGES." DO YOU AGREE?**

A. No, for two reasons. First, what Mr. Wolf actually describes in his testimony are the challenges of providing service in an area of low population density,[1] but the concepts are not interchangeable: not all areas served by "rural" ILECs are of especially low density, and not all areas of low density are served only by "rural" ILECs (many low density, high cost areas are served by non-rural ILECs and by other, non-ILEC carriers). What is important to consider is not the identity of the provider, but the cost to provide service in a given area compared to the cost to provide service in other areas. The existing federal USF mechanism includes the requirement that non-rural ILECs disaggregate support in a way that reflects cost differences and provides the opportunity for rural ILECs to do so. This disaggregation permits support to be targeted to areas of the greatest cost and need. The essential point of clarification is that it is the needs of consumers and the characteristics of the area that are important to the development of sound public policy and the accomplishment of the stated objectives of section 254. In

[1] As I explained in my direct testimony (pp. 32-34), the correlation between a simple measure of population density over a broad geographic area and the per-line costs to provide telephone service to customers in that area is actually quite low. Any quantitative analysis based on such a measure should only be treated as a rough approximation.

contrast, the classification of a given carrier as "rural" or "non-rural," or even as an ILEC or non-ILEC, is not.

Second, it is not at all clear that rural ILECs in Oregon have been unable to effectively meet these "substantial economic challenges" and to enjoy a significant level of earnings. According to the *2004 Oregon Utility Statistics* (p. 76) small telecommunications utilities realized a return (net operating income divided by average rate base, on an unseparated basis) of between 9.3% and 29.8%, with three companies enjoying returns of over 20%. Such returns are not indicative of fragile companies with substantial challenges that they are poorly positioned to face.

Q. **VERIZON WITNESS FULP MAKES (P. 3) A SIMILAR ASSERTION THAT THE COMMISSION SHOULD "RECOGNIZE THE UNIQUE POSITION OF ETC DESIGNEES THAT ARE ALSO LOCAL EXCHANGE CARRIERS." DOES HE PROVIDE ANY LEGITIMATE BASIS FOR THE SPECIAL TREATMENT OF ILECS?**

A. No. Any challenges of serving a high cost area apply equally to both ILEC ETCs and CETCs.

Mr. Fulp also argues that ILEC ETCs "should not be subject to the same disclosures or be subject to the same regulations as non-ILEC ETCs." The basis for this assertion is that "it would serve no good purpose" to require ILEC ETCs to produce the information required of CETCs because such reports "were intended in the first instance to only be a substitute for the extensive information the Commission already receives from and about ILECs." While I will address

this issue in more detail in response to Issue III, it is important to note that Mr. Fulp is juxtaposing the regulation of ILECs as monopoly (or former monopoly) utilities with the regulation of ILECs because they are ETCs. The purpose of each set of regulatory constraints is different, and the information needed to ensure compliance is different. The information that the Commission needs when conducting an annual recertification analysis to ensure that all ETCs (ILEC ETCs and CETCs) are meeting all of the applicable requirements requires a specific set of information. This information includes (but is not limited to) a demonstration of how the previous year's support was used to advance the stated goals of universal service. The ILEC ETCs could file any number of reports with the Commission as a part of their general regulation as ILECs, but if those reports do not include this essential information their existence is irrelevant to this proceeding. The question here is how to ensure that the Commission receives the information necessary for its oversight of the ILECs *as ETCs*.

Q. **MR. WOLF GOES ON TO SUGGEST THAT THE DESIGNATION OF WIRELESS CARRIERS AS ETCS HAS PUT UNIVERSAL SERVICE "AT RISK." DO YOU AGREE?**

A. Absolutely not. Mr. Wolf makes the unsubstantiated claim that "the continued availability of affordable, high-quality service to rural consumers is at risk because of the substantial and ever-increasing demands on the universal service fund from new carriers, particularly wireless carriers." Mr. Wolf's assertion is inaccurate for several reasons.

First, the designation of wireless carriers as ETCs is fully compliant with both the FCC's requirement of technical neutrality and the stated objectives of the Act. There is nothing pernicious about a wireless carrier seeking to be designated and to operate as an ETC. As described in my direct testimony (pp. 10-14), wireless service can provide consumer benefits that wireline carriers do not provide and will never be able to provide.

Second, even if Mr. Wolf's assertion was otherwise correct (and it is not, as I explain below) it is not the "continued availability of affordable, high-quality service to rural consumers" that is even potentially at risk, but rather the continued operation of the rural ILECs.[2] Rural ILECs are certainly not the only carriers capable of providing "affordable, high-quality service to rural consumers." As I explained in my direct testimony (pp. 9-10), Mr. Wolf's ILEC-protection policy is directly at odds with the conclusions of the FCC and Fifth Circuit Court, who have been clear that the purpose of the federal universal service mechanism is to provide benefits to rural consumers, not to protect incumbent LECs:

> The Act does *not* guarantee all local telephone service providers a sufficient return on investment; quite the contrary, it is intended to introduce competition into the market. Competition necessarily brings the risk that some telephone service providers will be unable to compete. The Act only promises universal service, and that is a goal that requires sufficient funding of *customers*, not *providers*. So long as there is sufficient and competitively neutral funding to enable all customers to receive basic telecommunications services, the FCC has satisfied the Act and is not

[2] The current earnings levels of the rural ILECs make it difficult to take a prediction of their imminent demise too seriously.

> further required to ensure sufficient funding of every local telephone provider as well (emphasis in original).[3]

Third, Mr. Wolf's assertion that the growth of the federal universal service fund is due primarily to the designation of wireless ETCs is just factually incorrect. The largest impact on the size of the fund has been caused by the transition from implicit to explicit subsidies required by the Act (access charges have been reduced, and explicit USF support has correspondingly increased). After this transition, the largest contributors to the size of the federal fund are the compromise elements that were included by the FCC for the benefit of rural ILECs. When seeking to paint wireless ETCs as the culprits, Mr. Wolf somehow neglects to mention in his testimony that the size of the high-cost fund is in large part a direct function of the FCC's decision to give the rural ILECs an extended transition period in which to improve their efficiency, reduce their costs, and better prepare themselves to operate in a competitive market. These elements of the mechanism, implemented at the request of and for the exclusive benefit of rural ILECs, represent a greater impact on the size of the fund than wireless carriers seeking designation as ETCs.

For the current interim mechanism, the FCC set aside its consistent (and economically valid) position that universal service funds should be sufficient to permit the recovery of a carrier's forward-looking economic costs, but not necessarily its embedded costs. In fact, the FCC did the rural ILECs one better,

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[3] *Alenco Communications, Inc. v. FCC*, 201 F.3d at 620, cited in *Fourteenth Report and Order*, paragraph 27.

and adopted at their request a modified embedded cost mechanism that was projected to increase the size of the high-cost fund by $1.26 billion dollars over the amount that would have been required by the existing embedded cost mechanism.[4] To my knowledge, no estimate has to date been published showing the actual impact on size of the federal fund that was caused by the decision to (1) permit rural ILECs to recover embedded, rather than economic, costs or (2) permit ILECs to recover the greater magnitude of costs pursuant to the modified embedded cost mechanism.

A second element of the interim federal universal service mechanism for rural areas, again included for the sole purpose of benefiting rural ILECs, is the modification of the concept of "portability." The FCC's decisions regarding the portability of these funds in rural areas are responsible for a portion of the increase in fund size. In its 2004 recommendation, the Joint Board set forth several options for limiting support to a customer's "primary line." Limiting support in this way would have reduced the size of the federal fund and would have enabled regulators to better manage the size of the fund in the future. Because the adoption of a "primary line" proposal could have resulted in a reduction in the USF support that they receive, the rural ILECs pushed for – and were able to get passed – a provision in the 2005 Consolidated Appropriations Act that, in the FCC's words, "prohibits the Commission from utilizing appropriated funds to 'modify, amend, or change its rules or regulations for Universal Service support payments to implement the February 27, 2004

[4] *Id.*, paragraph 28. It should be noted that this estimate was provided by the Joint Board and Rural Task Force, and not by some party opposing the adoption of the modified embedded cost mechanism.

recommendation of the Federal-State Joint Board on Universal Service regarding single connection or primary line restrictions on universal service payments."[5] By doing so, the rural ILECs obtained a legislative fix that prevented the FCC from adopting (or even considering) any of the Joint Board's recommendations to limit support to a primary line.

In this light, Mr. Wolf's suggestion that the Commission should base its policy on the fact that – at least according to Mr. Wolf – wireless carriers have been "aggressive in seeking ETC status" is disingenuous at best. In the simplest terms, the facts are as follows: (1) rural ILECs have asked for and received various protections from the impact of competition as a part of the interim mechanism, (2) these protections have caused the size of the high-cost fund to significantly increase, and (3) the rural ILECs are now using the fact that the fund is growing to support an argument that actual competitive entry should be limited as a matter of public policy.

Q. **MR. WOLF GOES ON TO SUGGEST (P. 5) THAT PUBLIC POLICY SHOULD REFLECT THE FACT THAT "THIS COMMISSION GENERALLY DOES NOT REGULATE WIRELESS CARRIERS." IS HE RIGHT?**

A. No. As an initial matter, while the rural ILECs are subject to consumer protection regulations (as former monopoly providers with significant market power, such regulation is appropriate), in some important ways "this Commission generally does not regulate" rural ILECs. Pursuant to ORS 759.040, unaffiliated

[5] *2005 USF Order*, ¶11.

telecommunications utilities serving fewer than 50,000 access lines in Oregon are exempt from ORS 759.180 through 759.190 (the provisions requiring Commission review of rate changes).

Second, while I agree that any carrier's service quality is important, I disagree that it is necessary or even desirable for the Commission to attempt to regulate the service quality of a CETC. Such an imposition would add requirements for ETC designation that the FCC has consistently elected not to impose. More importantly, the regulation of the service quality of a carrier that does not have market power is unnecessary – not because service quality isn't important to end user customers, but because it is. Assuming an alternative is available, customers will not subscribe to a carrier's service if they find the quality of the service, or a carrier's customer service operation, to be substandard. Ultimately, a CETC that fails to meet customers' expectations regarding service quality will pay a significant price: it will not receive federal high cost support for that customer.

By basing support on a per-line basis and making it available (at least to CETCs) only when a customer is actually served, the FCC created a dynamic in which the marketplace can sort out these issues. The designation of carrier as a CETC will provide it with an even greater incentive to ensure that customers see its services to be of high quality because, in addition to customer revenues, federal support dollars will be at stake.

Q. **MR. FULP ARGUES (P. 3) THAT IN ADDITION TO MEETING THE PUBLIC INTEREST STANDARD AS DESCRIBED BY THE FCC IN THE**

2005 USF ORDER, AN ETC APPLICANT MUST DEMONSTRATE THAT IT HAS ADEQUATE FINANCIAL RESOURCES. DOES SUCH A REQUIREMENT EXIST?

A. No. Mr. Fulp asserts that his proposed requirement is "called for by the Telecommunications Act," but he provides no citation to support this claim. In reality, the FCC has consistently rejected requests by the ILECs that such a requirement be imposed.

Most recently, in its *2005 USF Order* the FCC declined (¶37) to adopt a recommendation "that an ETC applicant demonstrate that it has the financial resources and ability to provide quality services throughout the designated service area." Instead, the FCC concluded that an ETC applicant "must demonstrate the ability to offer the supported services in the designated area by submitting detailed commitments to build-out facilities." Put directly, the FCC is interested in what a carrier will do, not in how it will pay for it.

The FCC's conclusion that an up-front demonstration of how investments will be financed is unnecessary is based on two stated factors. First, the FCC noted (¶37) that in the case of a wireless ETC applicant this capability must already exist: "after obtaining a license, whether by auction or other means, wireless carriers must further comply with the Commission's rules by meeting build-out or substantial service requirements for the particular service. Therefore, we find additional financial requirements are unwarranted to demonstrate that an ETC applicant is capable of sustaining operations and supported services." Of course, a wireless ETC must have the ability – including but not necessarily

limited to the required capital – to begin to build facilities in an area because, unlike ILEC ETCs, CETCs only receive support if they are actually providing service to customers. For CETCs, the key events of the timeline are (1) build facilities where feasible without USF support, (2) serve customers in that area, (3) receive support based on customers served, and (4) use that support to extend, enhance, or operate network facilities in high cost areas. In reality, a CETC will have demonstrated that it has some financial capability before it receives the first dollar of USF support.

Second, the FCC noted that "in its annual certification and reporting requirements, an ETC must demonstrate that it has used universal service support to provide quality service throughout the designated area." This demonstration of how the previous year's plan has been met, and how USF support funds have been used, represents a much more meaningful exercise.

II. Initial Designation of ETCs

Q. **MR. WOLF RECOMMENDS (P. 7) WHAT HE CALLS A STANDARD OF "EQUIVALENCY" FOR THE DESIGNATION OF ETCS. DO YOU AGREE WITH THIS PRINCIPLE?**

A. I agree with the principles of competitive and technological neutrality that have been adopted by the FCC. Mr. Wolf states (p. 7) that "incumbent and competitive ETCs alike should be accountable in the ETC process and the use of Federal USF monies." I certainly agree with that statement. What I do not agree with, however, is Mr. Wolf's approach to achieving "equivalency" by applying

fundamentally different standards when designating or recertifying ILEC and non-ILEC ETCs.

Q. **WHAT IS MR. WOLF'S STATED BASIS FOR ACHIEVING "EQUIVALENCY" BY APPLYING DIFFERENT STANDARDS?**

A. Mr. Wolf argues that differences in "funding rules" and in technology dictate that "different approaches are needed."

The "funding rules" difference noted by Mr. Wolf is that "the process for rural companies, of first having [to] put the facilities in the ground … contrasts with how CETCs (CETCs) receive support. A CETC receives support based upon the incumbent ETC's costs. The CTEC does not have to prove that the supported facilities have already been constructed."

Mr. Wolf is apparently attempting to draw two distinctions here; one related to the timing of investments and support and one related to the cost basis for support. His first distinction is based on a demonstrably false assumption, and his second, while factually correct, in no way provides a justification for a disparity in the treatment of ILEC ETCs and CETCs.

Q. **IS MR. WOLF CORRECT THAT CETCS DO NOT HAVE TO FIRST "PROVE THAT THE SUPPORTED FACILITIES HAVE ALREADY BEEN CONSTRUCTED"?**

A. No. He is right that CETCs do not have to file cost studies to prove the existence of these facilities, but he fails to take note of a much more fundamental requirement: a CETC must have facilities in its ETC service area – and must be serving customers with those facilities – in order to receive any support. Proving

the existence of the facilities with a cost study is not necessary because a CETC with no facilities receives no support. Once a CETC constructs facilities within its ETC service area, any support than is received for customers served can then only be used for the "provision, maintenance, and upgrading" of facilities to serve that area.

Q. **DOES MR. WOLF PROVIDE ANY BASIS FOR HIS ASSERTION THAT "THE CETC DOES NOT HAVE TO PROVE THAT THE SUPPORTED FACILITIES HAVE ALREADY BEEN CONSTRUCTED"?**

A. No. Since no foundation for this statement is provided in his testimony, the information was sought in a data request to OTA. Specifically, OTA was asked if it contends that "CETCs can receive high cost support without first investing in facilities," and if yes, to explain and provide any documents or data supporting such a contention. In response, OTA provided no response and no supporting documentation of any kind, but instead stated that "OTA objects to this data request as a misstatement of OTA's position." I am not an attorney, but I can note that in my review of thousands of data request responses over the past twenty years I have never before seen the "that's not what we said" objection. If OTA does *not* contend that "CETCs can receive high cost support without first investing in facilities," it's not clear why it could not have simply responded "no" rather than objecting to the request (that appears to be the substance of the response). Either way, Mr. Wolf's claim that there is a significant "contrast" in how ILEC ETCs and CETCs receive support remains undocumented.

In reality, of course, both ILEC ETCs and CETCs must construct network facilities before receiving USF support.

Q. **MR. WOLF ALSO SUGGESTS (P. 6) THAT THE FACT THAT "A CETC RECEIVES SUPPORT BASED UPON THE INCUMBENT ETC'S COSTS" IS SIGNIFICANT. DO YOU AGREE?**

A. No. Mr. Wolf suggests that this "contrast" is also important, but he ultimately makes no recommendation based on his observation that the per-line support received by CETCs is based on the ILEC ETC's costs.

The current mechanism of basing support for all ETCs in the ILEC ETC's cost is administratively efficient and is in no way at odds with sound public policy and in no way supports a recommendation to treat ILEC ETCs and CETCs differently in either their initial designation or in their annual recertification.

Q. **PLEASE EXPLAIN WHY USING ILEC COSTS AS THE BASIS FOR CETC PER-LINE SUPPORT MAKES SENSE.**

A. There are three possible scenarios: (1) The CETC's costs and the ILEC's costs are identical, (2) the CETC's costs are higher than the ILEC ETC's costs, and (3) the CETC's costs are lower than the ILEC ETC's costs.

Scenario 1 (CETC's and ILEC ETC's cost is the same) clearly does not create an issue; each carrier will be supported based on the cost that it incurs.

Scenario 2 (CETC's cost higher than ILEC ETC's cost) does not create an issue; in this case the CETC would not be able to compete with the ILEC ETC on price. Unless the CETC has a superior product that it believes customers will be

willing to pay for, it would not rationally enter the market and would not seek designation as an ETC.

Scenario 3 (CETC's cost lower than ILEC ETC's cost) also does not create an issue. While Mr. Wolf leaves his statement hanging with no subsequent recommendation, ILEC witnesses often argue that wireless providers, due to differences in network design and operations, have a lower per-line cost to serve customers in rural areas. Basing the wireless CETC's support on the higher ILEC costs, the ILECs typically argue, provides a "windfall" to the wireless CETCs.[6] This argument doesn't hold up under scrutiny. Even if the CETC's per-line costs prove to be lower than those of the ILEC ETC, no "windfall" can occur because the rules specifically limit the CETC's use of USF support to the investment in, and operation of, network facilities in the high-cost area. On the other hand, if one assumes the possibility of a "windfall" and then realizes that such a "windfall" will occur only if CETC's per-line costs are indeed lower, the worst outcome that can be realized is that the carrier that all parties agree is a more efficient provider will be encouraged to build out its network on an accelerated basis. Once this buildout is complete, support can be based on this more efficient network (and ultimately limited to this single efficient carrier) thereby minimizing the size of the fund over the long run.

If a wireless carrier has a cost advantage over a wireline carrier, that advantage is not created – and is not changed – by the designation of the wireless

[6] If Mr. Wolf is not suggesting that CETC's have a lower cost to serve the area than the ILEC ETC, then there would really be no point to his attempt to bring attention to the "contrast" in the basis of per-line support for CETCs and ILEC ETCs.

carrier as an ETC; it simply means that the wireless carrier is utilizing a more efficient technology to serve the area or is operating more efficiently than the wireline carrier. As explained above, if wireless carriers do have an efficiency/cost advantage, the existing per-line support mechanism will encourage accelerated deployment of network facilities by the more efficient provider (as there is no other permissible use for these funds). While he suggests that the "contrast" in the basis for per-line support is significant, Mr. Wolf offers no explanation of why the public interest would be served by adopting a policy of discouraging investment by a more efficient provider while encouraging investment by a less efficient provider.

Should the Commission adopt any, or all, of the requirements proposed by the FCC (Issue II(A)(1))?

Q. **AT PP. 15-25 OF YOUR DIRECT TESTIMONY, YOU RECOMMENDED THAT THE COMMISSION ADOPT, WITH SOME CAVEATS AND MODIFICATIONS, THE ETC DESIGNATION REQUIREMENTS PROPOSED BY THE FCC. DO THE OTHER PARTIES SIMILARLY RECOMMEND THE ADOPTION OF THESE REQUIREMENTS?**

A. In most cases yes,[7] although there are some important differences in how these requirements should be interpreted and applied. I will address each of the FCC's recommendations, and the parties' position on each recommendation, in turn below.

[7] Verizon witness Fulp argues (p.4) that the Commission should not adopt the FCC requirements because these requirements either "do not fit well in Oregon" or "are redundant of obligations that Verizon satisfies routinely as an ILEC." As I will explain in detail when addressing Issue III, I disagree that the current ILEC filings with the Commission provide the information necessary for the ILEC to meet its obligation to demonstrate that the funds received have been used only for the intended use.

Q. **SHOULD THE COMMISSION ADOPT THE FCC'S RECOMMENDATION REGARDING A CARRIER'S "COMMITMENT AND ABILITY TO PROVIDE THE SUPPORTED SERVICES"?**

A. Yes, with one change. Staff witness Marinos recommends a reasonable change to the reporting provision: "the Commission should not require that unfulfilled service requests be reported within 30 days, but rather reporting should be done as part of the annual recertification process," and this change should be adopted. A consideration of a carrier's performance as a part of the annual recertification process means that the Commission and Staff will have a much more complete and useful fact set upon which to reach a conclusion.

Mr. Wolf generally supports the adoption of the FCC requirements, but then seeks (p. 9) to add a provision regarding unfulfilled requests for service. He argues that his principle of "equivalency" can be applied by requiring "the ETC applicant to meet the same held order and service installation standards as rural companies." While Mr. Wolf did not specify which specific rules should be applied, in response to a data request OTA responded that OAR 860-034-0390(4), OAR 860-032-0012(5), OAR 860-032-0012(6), OAR 860-032-0012(7), OAR 860-032-0012(8), and OAR 860-032-0012(11) should apply to wireless ETCs.[8]

As RCC witness Otto explains in his rebuttal testimony (Exhibit RCC/3), the application of these rules to wireless carriers makes little practical sense. Wireless carriers and wireline carriers provision service in different ways and track performance in different ways. These differences are due in part to technological differences and in part to customer expectations. For example, in

[8] OTA Response to Joint Data Request Nos. 1 and 2.

most cases a wireless carrier can provide service to a customer immediately (before the customer leaves the store), while a request for service made to a wireline carrier almost always involves some delay. It would not make sense to require the ILECs to meet the wireless "instant activation" interval, nor would it make sense to require ILECs to track the number of minutes that elapse between the receipt of the customer's order and the activation of the local loop to the customer's premises.

As I explained in my direct testimony, the FCC explicitly rejected the notion that a CETC should be subject to the same consumer protection requirements as the ILECs.[9] Instead, the FCC urged states to adopt only those requirements that are actually needed to protect consumers:

> In determining whether any additional consumer protection requirement should apply as a prerequisite for obtaining ETC designation from the state – i.e., where such a requirement would not otherwise apply to the ETC applicant – we encourage states to consider, among other things, the extent to which a particular regulation is necessary to protect consumers in the ETC context, as well as the extent to which it may disadvantage an ETC specifically because it is not the incumbent LEC. *We agree with the Joint Board's assertion that 'states should not require regulatory parity for parity's sake.' We therefore encourage states that impose requirements on an ETC to do so only to the extent necessary to further universal service goals* (emphasis added).[10]

Mr. Wolf and the OTA offer no rationale for their position that the application of OAR 860-034-0390(4), OAR 860-032-0012(5), OAR 860-032-0012(6), OAR 860-032-0012(7), OAR 860-032-0012(8), and OAR 860-032-0012(11) are "necessary to protect consumers," are "necessary to further universal

[9] The 1996 Act does not require CETCs to be ILECs or to be regulated as ILECs.
[10] *2005 USF Order*, ¶30.

service goals," and do not serve to "disadvantage an ETC specifically because it is not the incumbent LEC."

Q. **SHOULD THE COMMISSION ADOPT THE FCC'S FIVE YEAR NETWORK IMPROVE PLAN REQUIREMENT?**

A. No. As set forth in my direct testimony, I support a requirement that a carrier seeking ETC designation must provide a plan for how it will "use universal service support to improve service" and believe that the Commission should adopt such a requirement. I disagree with the FCC's proposed five year plan because it provides little useful information (certainly the information beyond the first year or two is of questionable value), requires wireless carriers to report information at a geographic level (the ILEC's wire center) that has no meaning for a wireless network, and is costly to produce. A five year plan is not the most effective – and is certainly not the most efficient – means available for the Commission to ensure that a carrier maintains the "capability and commitment" to "respond to reasonable requests for service" and that federal USF support is being used for the intended purposes. It would be more effective and efficient for the Commission to require all ETCs (both CETCs and ILECs) to provide one-year plans and to carefully review the ETC's progress toward reaching these stated objectives in the context of the annual recertification process.

Q. **STAFF WITNESS MARINOS RECOMMENDS A MODIFIED NETWORK IMPROVEMENT PLAN. DOES HER PROPOSAL MAKE SENSE?**

A. Yes. Ms. Marinos notes (p. 33) that "the length of the plan, combined with the amount of wire-center detail required by the FCC, does raise issues regarding the

value and necessity of a plan that would meet FCC requirements." In lieu of the FCC's proposal, Ms. Marinos has developed an alternative plan that focuses on a description of the carrier's initial network facilities, detailed plans over a two- rather than five-year horizon, and more general planning information for years three through five. As Ms. Marinos explains, "the detailed 2-year plan would serve as the basis for review in the annual reporting process. It would be updated each year and shifted forward to add a new second year."

Ms. Marinos also notes that while a carrier's plan should demonstrate that improvements will be made throughout the carrier's ETC service area, "requiring such details for every wire center is a needlessly onerous way to achieve that objective." Ms. Marinos does state that a CETC should provide line/handset counts by ILEC wire center if the ILEC has disaggregated support (something that she recommends). This requirement makes sense, and corresponds to the information that the CETC must report to USAC in those circumstances.

Q. **DOES OTA SUPPORT REQUIRING ETCS TO FOLLOW THE FCC'S FIVE-YEAR PLAN?**

A. The answer appears to be yes, but Mr. Wolf's reasoning is hard to follow. He apparently supports the application of the requirement to new ETC applicants and to previously-designated CETCs, but seeks to exempt ILEC ETCs from the requirement.

Mr. Wolf first seeks (p. 10) to base his recommendation for disparate treatment on his belief that the fact that "incumbent ETCs (the rural companies) receive USF support, particularly high cost support, based upon past, actual

investment" is unique or can otherwise justify a difference in the treatment of ILEC ETCs and CETCs. As explained above, CETCs also receive USF support only after making "actual investments." Mr. Wolf then suggests that disparate treatment "makes sense" because the level of per-line support received by CETCs "is based upon the incumbent ETC's level of support per line." As explained above, this mechanism means that only efficient competitors will seek to be designated as ETCs, and in no way relieves a CETC of its obligation to use all USF support received for the "provision, maintenance, and upgrading" of network facilities to serve the area. Nothing in the timing of network investments and support, or in the underlying basis of the per-line support, justifies a closer scrutiny of a CETC's operations than should be undertaken of an ILEC ETC's operations (including a demonstration that funds received were used for the intended use and a projection showing how planned future investments will be consistent with the objectives of universal service).

After seeking to draw a distinction between the operation of CETCs and ILEC ETCs by claiming that ILECs must make "actual investment" before receiving support (the purported distinction, apparently, being that CETCs need not make "actual investment" before receiving support), Mr. Wolf then almost immediately takes a contradictory view. He states (p. 11) that "typically, a wireless carrier seeks ETC designation from the Commission *after it has already constructed its network* and begun providing serving" (emphasis added). Hold on a minute here. On the page before this statement, Mr. Wolf was claiming that CETCs require careful scrutiny because they allegedly receive USF support

before making "actual investments" (whereas ILECs require no such scrutiny because "actual investments are made before support is received). Now one page later, Mr. Wolf argues that CETCs require careful scrutiny because they are receiving support *after* making all of the necessary network investments to serve the area. Both of these assertions can't be true.[11]

Mr. Wolf then goes on to claim (p. 11) that because it has already constructed its network, "the wireless carrier is already providing service to the public without relying on universal service funding. If the wireless carrier subsequently attains ETC status from the Commission, it can boost its revenues without doing anything to further the goals of universal service." This, according to Mr. Wolf, will "result in an unearned windfall without any benefit to Oregon consumers."

While I disagree with his conclusion, Mr. Wolf raises a point worth considering further. His factual premise regarding a wireless ETC applicant is incorrect; a wireless carrier seeking designation as an ETC will have made network investments in the area, but will not, without USF support, have made all of the necessary investments to provide quality service throughout the entire service area. All of the support that it receives must be used for the provisioning, maintenance, and upgrading of network facilities in its ETC service area, and the Commission makes this assurance every year during the annual recertification process.

[11] In reality, neither assertion is right. A CETC must make investments in its own facilities, and serve customers with those facilities, before it receives any USF support. This support then makes it possible for the CETC to make additional investments to expand and improve coverage in the area.

ILEC ETCs, on the other hand, are a different story. According to Mr. Wolf (p. 6), "each of OTA's members have [sic] constructed telecommunications networks throughout their individual service areas that for the most part are ready to serve any customer that requests service." If Mr. Wolf's claim that wireless carriers can serve the ILEC service area "without relying on universal service funding" is correct, and if the ILECs are now receiving USF support after having fully built out their networks, only two possibilities exist: (1) a given ILEC can provide service throughout its service area as efficiently as a wireless CETC, and therefore can "boost its revenues without doing anything to further the goals of universal service," resulting in "an unearned windfall" to the ILEC "without any benefit to Oregon consumers," or (2) a given ILEC cannot provide service throughout its service area as efficiently as a wireless CETC. Either conclusion begs the questions of why it is in the public interest to use limited universal service funds to continue to support the ILECs. If the first possibility holds true (ILEC is equally as efficient as wireless CETC), then the ILECs are, in Mr. Wolf's words, receiving "an unearned windfall" that does nothing to "further the goals of universal service." If the second possibility holds true (ILEC is not as efficient as wireless CETC), then it is unclear why the less efficient carrier should be supported. If, as Mr. Wolf claims, a wireless carrier can provide service throughout an ILEC service area *without* relying on universal service funding, why is it in the public interest to continue to provide support to the less efficient carrier – the ILEC – that can only provide service in the area *with* universal service funding? Mr. Wolf offers no answer to this question.

Q. **DOES THERE APPEAR TO BE ANY DISPUTE REGARDING THE ADOPTION OF THE FCC'S REQUIREMENTS FOR AN ETC APPLICANT TO SHOW THAT IT WILL REMAIN FUNCTIONAL IN EMERGENCY SITUATIONS AND THAT IT ACKNOWLEDGE THAT IT MAY HAVE TO PROVIDE EQUAL ACCESS IF THE ILEC RELINQUISHES ITS ETC DESIGNATION?**

A. No. It appears that all parties are in agreement on these issues.

Q. **SHOULD THE COMMISSION ADOPT THE FCC'S REQUIREMENT REGARDING LOCAL USAGE?**

A. Yes, but there appear to be some differences of opinion regarding the meaning of this requirement. As I described in my direct testimony, the FCC's *2005 USF Order* includes two important conclusions: (1) the FCC rejected, as it has consistently done, suggestions that a "specific local usage threshold" be adopted, and (2) the FCC instead determined that CETC rate plans should be considered on a case-by-case basis, with due consideration given to the differences in geographic scope of the "local" callings areas offered by various carriers and to other fundamental differences in service offerings.

Ms. Marinos notes (pp. 43-44) the FCC's recommendation that the larger local calling plans of wireless carriers be considered when evaluating local usage offerings, but goes on to suggest that "this approach is not consistent with the basis for, or the calculation of costs underlying, per-line support. Federal universal service is not intended to support the costs of non-local calling." I must respectfully disagree with Ms. Marinos' reasoning here for two reasons. First, the

"local" calling area of the ILEC does not determine what is a "local" call for other carriers. Wireless carriers, whether or not designated as an ETC, can designate their own local calling areas, and these areas can be larger than those of the ILEC. Second, the federal universal service mechanism supports networks, not individual services. If USF support is used for the "provision, maintenance, and upgrading" of network facilities that provide the nine supported service functionalities, there is no reason that these facilities must be limited to only those nine functionalities. The FCC has specifically noted that the larger local calling areas often offered by wireless ETCs are an important consideration when evaluating the public interest.[12]

Ms. Marinos goes on to suggest (pp. 43-44) that because "flat rated, unlimited local calling is the standard for wireline local exchange service in Oregon," wireless ETC applicants "should be required to demonstrate that they offer a local calling plan that offers unlimited local minutes, or includes at least the average number of local calling minutes made by ILEC customers." I again must respectfully disagree with this conclusion. A requirement that CETCs offer unlimited local usage is not necessarily consistent with the best interest of consumers. Any suggestion that unlimited local usage means that local usage is being provided "for free" to customers is a mistaken one; in reality, a flat-rated service offering simply means that customers are buying – and paying for – a fixed bundle of usage that corresponds to average customer usage. Some customers will use fewer minutes but still pay for the average amount, while others will use more minutes and benefit by paying for only the average. In

[12] See *Virginia Cellular Order*, ¶29; *Highland Cellular Order*, ¶23; and *2005 USF Order*, ¶33.

contrast, the service plans of most wireless carriers allow the customer to make a choice regarding the amount of usage that he or she wishes to pay for. This choice can be based on a consideration of total calling volume and with the scope of the geographic area that the customer wishes to include.

Mr. Wolf similarly argues (pp. 13-14) that an ETC applicant must "make available sufficient minutes to allow a level of local calling that is practical for consumers' everyday needs." Of course, there is no single amount of local usage (or local calling scope) that best meets the needs of all customers; what is a "sufficient" number of minutes is specific to each customer.

In the end, the amount of local usage that a customer pays for is an issue for that *customer* (not for the Commission, and certainly not for the ILECs) to decide. Customers are in the best position to determine whether a particular service offering, with a given number of minutes, with a given local calling scope, and with a given price will be beneficial to them. CETCs, because they receive support only for customers served, are motivated to develop service offerings that meet the needs of different customers. It is up to end users to decide whether to purchase the CETC's service (so that the CETC receives federal USF support) or not to purchase the CETC's service (so that the CETC receives no federal USF support).

Should the Commission adopt other basic eligibility criteria (Issue II(A)(2))?

Q. **IN YOUR DIRECT TESTIMONY, YOU STATED THAT THE REQUIREMENTS THAT THE FCC DEVELOPED FOR ETC APPLICATIONS ARE THOROUGH AND COVER ALL OF THE**

APPLICABLE ELIGIBILITY CRITERIA SET FORTH IN THE ACT. HAVE ANY OF THE PARTIES PROPOSED ADDITIONAL CRITERIA THAT SHOULD BE ADOPTED?

A. No. Staff witness Marinos describes (pp. 47-48) the statutory requirements for ETC designation, but I am not aware of any dispute regarding the applicability of these requirements.

Mr. Wolf (p. 15) argues that additional service quality standards should apply to CETCs, but notes that "the Commission is prohibited by Oregon law from applying these standards to cooperatives" and that "many of the small commercial companies" may also be exempt from these rules. It is difficult to understand exactly how Mr. Wolf's principle of "equivalency" is being applied in this recommendation.

Mr. Wolf's recommendation to add quality of service standards to the ETC designation requirements should be rejected for two other reasons. First, as addressed previously in my testimony, Mr. Wolf's proposal appears to be the kind of "parity for parity's sake" that the Joint Board and FCC have recommended that states not adopt. The FCC urged states to adopt additional requirements only if those requirements are "necessary to protect consumers," are "necessary to further universal service goals," and do not serve to "disadvantage an ETC specifically because it is not the incumbent LEC." Mr. Wolf offers no reasons why his proposal to apply certain rules would permit any of these conditions to be met.

Second, Mr. Wolf's testimony provides (p. 15) a reason why the application of service quality standards is unnecessary. In support of the

exemption for cooperatives, he notes that "customers exercise control over service quality issues since those customers can change the management of the company by a vote." His reasoning here may be sound, but he fails to apply it broadly enough. The same conclusion can be reached regarding the application of these same requirements to CETCs: customers exercise control over service quality issues since those customers can eliminate the CETC's USF support by "voting with their feet" and obtaining service from another provider. Like the management of an ILEC cooperative, the management of a CETC is highly motivated to meet customer's quality of service expectations.

Should the same requirements apply to applications for designations in rural and non-rural ILEC service areas (Issue II(a)(3))?

Q. **DO YOU HAVE ANYTHING TO ADD TO YOUR DIRECT TESTIMONY ON THIS ISSUE?**

A. No.

Should the same requirements apply regardless of the type of support that the ETC will receive (Issue II(A)(4))?

Q. **DO YOU HAVE ANYTHING TO ADD TO YOUR DIRECT TESTIMONY ON THIS ISSUE?**

A. No.

Should the Commission adopt the public interest criteria proposed by the FCC in order 05-46 (Issue II(B)(1))?

Q. **IN YOUR DIRECT TESTIMONY, YOU RECOMMENDED THAT THE COMMISSION ADOPT THE FCC'S PUBLIC INTEREST ANALYSIS**

EXCEPT FOR THE "CREAMSKIMMING" ANALYSIS. IS THIS STILL YOUR RECOMMENDATION?

A. Yes. It remains my recommendation that the Commission adopt the FCC framework for evaluating the public interest, including a review of the benefits of competitive choice and an analysis of the advantages and disadvantages to consumers of the ETC applicants service offerings. While I do not agree with some of his interpretations (as I will explain in more detail below), it appears that Mr. Wolf also supports the application of the FCC's approach (p. 16). Staff witness Marinos also advocates the adoption of the FCC's approach, but suggests (p. 56) that the Commission, when evaluating the public interest, might want to pay particular attention to a carrier's ability to provide advanced services or other capabilities in areas where they are not currently available. This position seems reasonable.

Q, **MR. WOLF SUGGESTS THAT THE COMMISSION SHOULD PAY PARTICULAR ATTENTION TO THE IMPACT OF A DESIGNATION ON THE SIZE OF THE FEDERAL UNIVERSAL SERVICE FUND. DO YOU AGREE WITH HIS APPROACH?**

A. No. Mr. Wolf asserts (p. 18) that "Oregon must recognize that additional ETC designations do materially increase the size of the universal service fund." While it is true that ETC designations, in the aggregate,[13] have increased the size of the fund, Mr. Wolf omits any discussion of other factors that have had an even greater

[13] It would of course not be accurate to conclude that any given ETC designation will materially increase the size of the federal fund, but all such designations, in the aggregate, have had an impact. The relevant question is not whether the act of designating one CETC or all CETCs will cause the size of the fund to increase in the short run, but rather whether such designations will make it possible to better manage the size of the fund over the long run.

impact. The ongoing transition from implicit to explicit support has had a significant impact, as did the FCC's decision to grant the rural ILECs' request to base high-cost support on a modified embedded cost mechanism. In addition, a decision to continue to support a higher-cost ILEC ETC, in an area that is completely served by a lower-cost CETC, significantly inflates the size of the fund while providing no clear public benefit.[14]

Q. **MR. WOLF REFERS TO THE FCC'S CONSIDERATION OF THE POSSIBLE DISADVANTAGES OF A WIRELESS ETC'S SERVICE OFFERINGS. IS THIS ALL THAT THE FCC NOTED?**

A. No. The FCC explicitly points out that when conducting public interest analyses, it has "examined the benefits of mobility that wireless carriers provide in geographically isolated areas, the possibility that the ETC designation will allow customers to be subject to fewer toll charges, and the potential for customers to obtain services comparable to those provided in urban areas." Clearly the advantages, not just the disadvantages, of a potential ETC's services should be considered.

Q. **THE FCC ALSO INCLUDED IN ITS APPROACH A "CREAMSKIMMING" ANALYSIS. DOES A POTENTIAL FOR "CREAMSKIMMING" EXIST IN EVERY REQUEST FOR ETC DESIGNATION?**

[14] If Mr. Wolf is right that basing a CETC's support on the ILECs' cost is a cause for concern (something that would only be the case if the CETC's costs are lower than the ILEC's), then it is reasonable to conclude that the continuing support of OTA members is creating a material increase in the size of the federal fund that should be considered as a part of the Commission's public interest analysis.

A. No. Mr. Wolf suggests (p. 19) that the Commission's review of "any application" must "pay particular attention to the potential creamskimming effects of granting the application." Such an approach would go far beyond the FCC's recommendation and well beyond what is necessary to protect the public interest.

While I am not yet convinced that "creamskimming" is a real concern (rather than simply a rallying cry of the ILECs), the FCC is clear that even the theoretical potential for "creamskimming" is present only under specific circumstances. Specially, a theoretical possibility of "creamskimming" exists only when (1) a carrier requests ETC designation for an area less than the ILEC study area[15] and (2) an ETC applicant "seeks designation in a disproportionate share of the high-density portion of a service area" such that it "may receive more support than is reflective of the rural incumbent LEC's costs of serving that wire center because support for each line is based on the rural telephone company's average costs for serving the entire service area unless the incumbent LEC has disaggregated its support."[16]

Q. **WHAT IS YOUR UNDERSTANDING OF STAFF'S POSITION REGARDING THE POTENTIAL FOR "CREAMSKIMMING"?**

A. It appears that Ms. Marinos has taken a comprehensive yet pragmatic approach to this issue that successfully gets beyond the rhetoric and addresses the basic issue of whether the FCC's "creamskimming" analysis provides identifiable benefits.

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[15] "When a competitive carrier requests designation for an entire rural service area, it does *not* create creamskimming concerns because the affected ETC is required to serve all wire centers in the designated service area" (emphasis added). *2005 USF Order*, ¶49.

[16] *Id.*

She correctly notes (p. 58) that the potential for "creamskimming" exists "in cases where the ILEC support is calculated based on average costs across all of its wire centers," but that "creamskimming" concerns are lessened "in cases where the ILEC had disaggregated support to reflect differences in costs among wire centers." Based on her balancing of benefits and costs, she concludes that the FCC's "creamskimming" test should not be required for several reasons: (1) "the creamskimming test serves as a barrier to entry, particularly when the CETC must operate within a licensed service area," (2) "the fear that rural ILECs will somehow be harmed if a CETC serves only a portion of their study area has little basis in reality. If the rural ILEC is harmed because it has not disaggregated its support by wire center, it can eliminate that harm by disaggregating its support," and (3) "under the current support system for rural carriers, it is difficult to see how a rural ILEC's financial condition would be significantly impacted if another carrier, a CETC, were also to receive support in the same area."

Q. **DOES MR. WOLF DESCRIBE THE POTENTIAL FOR ILEC HARM RESULTING FROM "CREAMSKIMMING"?**

A. Yes. He explains (p. 21) that any time a second ETC does not provide service to the entire service area over which an incumbent's costs and rates are averaged, the opportunity exists for the second ETC to creamskim." Of course, the problem is created – as Mr. Wolf points out – by the averaging of the ILEC ETC's costs and support. If support is disaggregated at the wire center level, based on cost differences among those ILEC wire centers, it will be impossible for CETC to

receive per-line support based on averaged costs while serving only low-cost areas (the FCC's own definition of "creamskimming").

Q. **YOU HAVE DESCRIBED "CREAMSKIMMING" AS A THEORETICAL CONCERN. DOES MR. WOLF PROVIDE ANY ACTUAL, DOCUMENTED EXAMPLES OF "CREAMSKIMMING" IN HIS TESTIMONY?**

A. No. Because no such information was provided in the prefiled testimony, OTA was asked in a data request to "produce any evidence or examples of where a state commission or the FCC has found creamskimming by a CETC to have occurred anywhere in the U.S." OTA first responded that the issue to be addressed is the "potential" for creamskimming, and that the Commission should focus on this "potential" because of the "adverse effects that may occur if creamskimming is allowed to occur in the first place." Unfortunately, OTA does not explain what these "adverse effects" might be. As Ms. Marinos correctly points out in her testimony, even when the ILEC has not availed itself of the opportunity to disaggregate support "the fear that rural ILECs will somehow be harmed if a CETC serves only a portion of their study area has little basis in reality."

OTA goes on in its response to refer to the FCC's *Virginia Cellular Order* and *Highland Cellular Order*. A review of these orders reveals, however, that the FCC did not conclude that "creamskimming" had occurred or was occurring; it simply noted its belief that where a "great disparity" exists in the population density of ILEC wire centers, some *potential* for "creamskimming" might exist. OTA then refers to an order of the Public Utilities Commission of Nevada. I am

familiar with the order cited and participated in the litigation of that case before the Nevada Commission; at no time was the Commission presented evidence that "creamskimming" had occurred or was occurring and the Nevada Commission reached no such conclusion in its order.

Despite OTA's frequent references to the dangers of "creamskimming," it can produce no evidence that it has actually occurred anywhere. If this risk were material, surely an example could be found somewhere.

Q. **IN YOUR DIRECT TESTIMONY, YOU STATED THAT THE FCC'S METHODOLOGY GENERATES ONLY A ROUGH APPROXIMATION OF COST DIFFERENCES AND THAT ITS RESULTS ARE SUBJECT TO SIGNIFICANT ERROR. HAS ANY INFORMATION BEEN PRESENTED THAT SUPPORTS THIS CONCLUSION?**

A. Yes. Attached to OTA's Response to Joint data Request No. 11 is a cost study performed by Citizens Telecommunications Company. This study shows – for each wire center – the calculated cost, number of lines, and number of square miles. Using this information it is possible to perform a regression analysis in order to determine whether a significant correlation exists between density (expressed here as lines/square mile)[17] and the per-line cost to provide basic services. In other words, it is possible to test how much of the reported variation in cost is explained by differences in density.

[17] It is important to note that by beginning the analysis with access lines/square mile rather than population/square mile, one of the sources of error inherent in the FCC's methodology has been eliminated. For this reason, it is reasonable to expect the regression analysis performed using the information in Citizen's cost study to show a high degree of correlation. Put another way, if an analysis using access lines/square mile show a weak relationship between density and per-line costs, then persons/square mile (the density measure used by the FCC) can be assumed to have an even lower correlation.

Confidential Exhibit RCC-USCC/5 shows the results of this analysis. I first attempted to determine how much of the variation in the reported total cost could be explained by the density of access lines in each wire center (this analysis is shown on page 1 of the exhibit). Using a linear regression, only 40.28% of the variation in total cost can be explained by differences in lines density (the coefficient of determination, R^2, is only .4028). This means that some factor (or factors) other than access line density account for almost 60% of the variation in per-line cost.

I next attempted an exponential (logarithmic) regression to see if a better correlation could be identified. Using this curve rather than a straight line to describe the relationship of the variables improved the results only slightly: this analysis shows that only 47.31% of the variation in total cost can be explained by differences in line density (the coefficient of determination, R^2, is only .4731). This means that some factor (or factors) other than access line density still account for over half of the variation in per-line cost.

Because local loop costs are most likely to be sensitive to differences in access line density, I repeated the analysis using the reported local loop cost rather than the reported total per-line costs. As page 2 of Exhibit RCC-USCC/5 shows, the results did not change materially. Using a linear regression, differences in access line density explain only 40.28% of the variation in local loop cost. Using an exponential regression, differences in access line density explain only 46.99% of the variation in local loop cost.

Q. **WHAT CAN YOU CONCLUDE FROM THIS ANALYSIS?**

A. That access line density is an inadequate predictor of per-line costs. This means that access lines/square mile tells us something, but not much, about what the level of per-line cost is likely to be. Other (as yet identified factors) are needed to explain over half of the observed cost variation.

Q. **BASED ON THE TESTIMONY OF THE PARTIES, HAVE YOU BEEN ABLE TO DRAW ANY GENERAL CONCLUSIONS ABOUT THE "CREAMSKIMMING" ISSUE?**

A. Yes. Given the fact that no documented cases of actual "creamskimming" have been found, the issue continues to consume an inordinate amount of attention in designation proceedings and rulemakings. As Ms. Marinos correctly points out, "the fear that rural ILECs will somehow be harmed if a CETC serves only a portion of their study area has little basis in reality, and "under the current support system for rural carriers, it is difficult to see how a rural ILEC's financial condition would be significantly impacted if another carrier, a CETC, were also to receive support in the same area."

Perhaps even more puzzling is that while a mechanism to effectively prevent even the possibility of "creamskimming" is readily available, many ILECs have not taken advantage of the opportunity to disaggregate support. In fact, many rural ILECs have actively resisted doing so.[18] I can only conclude that the rural ILECs have decided that the ability to claim harm from "creamskimming" in ETC designation proceedings is more valuable to them than

[18] As I will explain in more detail in response to Issue II(B)(4), the disaggregation of support by wire center need not be difficult, time-consuming, or costly.

actually implementing a mechanism that will prevent "creamskimming" from occurring. As Ms. Marinos astutely observes, "it appears that under current conditions, ILECs have no incentive to disaggregate support on their own ... the creamskimming test gives rural ILECs an additional reason to retain averaged support because it prohibits CETCs from being designated in many rural areas."

Should the criteria differ between designations in rural and non-rural ILEC service areas (Issue II(B)(2))?

Q. **DO YOU HAVE ANYTHING TO ADD TO YOUR DIRECT TESTIMONY ON THIS ISSUE?**

A. No.

Should the Commission require an ETC to include entire ILEC wire centers in its service area, regardless of the boundaries of its licensed area (Issue II(B)(3))?

Q. **DO YOU HAVE ANYTHING TO ADD TO YOUR DIRECT TESTIMONY ON THIS ISSUE?**

A. No.

Should the Commission require ILECs to disaggregate and target support in a different manner, as permitted by 47 CFR §54.315(c)(5) (Issue II(B)(4))?

Q. **IN YOUR DIRECT TESTIMONY, YOU RECOMMENDED THAT ILECS BE REQUIRED TO DISAGGREGATE THEIR SUPPORT AT THE WIRE CENTER LEVEL. DO THE ILECS PROVIDE A REASON WHY THIS CAN'T OR SHOULDN'T BE DONE?**

A. No. As I indicated in my direct testimony, the disaggregation of support eliminates the potential for "creamskimming" and encourages investment in high-cost areas. Staff witness Marinos correctly points out (pp. 67-68) that the disaggregation of support "results in per-line support amounts that more closely

reflect the costs of serving each individual wire center" thereby sending "the correct economic signals to encourage CETCs to expand into higher cost areas" and "eliminat[ing] the need for a creamskimming test."[19] For these reasons, Ms. Marinos recommends that the Commission require the ILECs to disaggregate support to the wire center level.

Q. **MR. WOLF ASSERTS (P. 23) THAT "THE QUESTION OF WHETHER DISAGGREGATION SHOULD OR SHOULD NOT OCCUR IS NOT A QUESTION FOR THE ETC DESIGNATION PROCESS." DO YOU AGREE?**

A. Not at all. The disaggregation of support is an essential part of any attempt to develop ETC designation guidelines, and the ILECs themselves have made it a central part of this case. Mr. Wolf and Mr. Fulp both argue that the potential for "creamskimming" must be carefully examined by the Commission before designating a carrier as an ETC and that the potential for "creamskimming" represents one reason that the Commission should deny a carrier such designation. The disaggregation of support represents a means of rendering those concerns moot and is an explicit part of the FCC's analysis. As the FCC states in the *2005 USF Order* (¶49), state regulators are encouraged to consider the following factors when evaluating the potential for "creamskimming: (1) the degree of population density disparities among wire centers within rural service areas,[20] (2) the extent to which an ETC applicant would be serving only the most densely

[19] Ms. Marinos also correctly points out that such disaggregation has been required in Washington, and that the WUTC has concluded that this disaggregation eliminates creamskimming concerns.
[20] To be clear, the FCC does not suggest that any population disparity creates a potential for "creamskimming," but states only that a "great disparity" *might* do so.

concentrated areas within a rural service area, and (3) *whether the incumbent LEC has disaggregated its support at a smaller level than the service area (e.g., at the wire center level).*

Clearly it is impossible for a CETC to realize some financial gain from receiving per-line support based on average costs while serving only a low-cost area if the per-line support is *not* based on average costs, but instead has been disaggregated in order to reflect the costs associated with the area of below-average costs. If the ILEC ETC has disaggregated properly so that the level of per-line support available to a CETC serving each of its wire centers reflects the costs of serving that wire center, then there is no possibility that "creamskimming" can occur.

Q. **MR. WOLF ARGUES (P. 23) THAT DISAGGREGATION OF SUPPORT SHOULD NOT BE REQUIRED BECAUSE DOING SO REPRESENTS A "RELATIVELY EXPENSIVE SITUATION." DO YOU AGREE THAT THIS IS INHERENTLY THE CASE?**

A. No. Mr. Wolf provides no basis for his suggestion that the task of disaggregating support would somehow be unduly burdensome for the rural ILECs to accomplish, and it appears that this claim has very little factual basis.[21]

In response to a data request seeking the states in which "OTA members have disaggregated their support to the wire center level" and "the cost to disaggregate in each of those states," OTA responded that "the only OTA member to have disaggregated their USF support to the wire center level is Pioneer

[21] Mr. Fulp makes a similar assertion at pp. 6-7 of his testimony, but also provides no support for his claim.

Telephone Cooperative," and that because of the "length of time that has passed," "it is not possible to reconstruct the amount of costs incurred by the company."[22]

When the request was broadened to include the costs incurred by "any rural ILEC (not limited to OTA members) in any state to develop and file plans to disaggregate to the wire center level," OTA responded that its members' "counterparts in the state of Washington" have characterized the exercise as having "a high level of cost" but provided no quantification of any of the costs actually involved. OTA does state that it is "aware"[23] that an unidentified ILEC in an unidentified state "did a disaggregation study that cost the company in excess of $90,000."[24]

Finally, OTA was asked to produce "all data and documents to support the claim that disaggregation would be unduly costly and burdensome." In response OTA provided no data and no documents, but did offer the assertion that "any time an activity has costs that outweigh its benefits, it is unduly costly and burdensome." This claim is worth exploring in the context of disaggregating USF support. If the potential for "creamskimming" represents the threat that the ILECs claim it does, then a tangible benefit of disaggregating support by wire center is readily apparent. The open question is whether such disaggregation is inherently costly to perform.

Q. **DO YOU HAVE ANY EVIDENCE THAT SUGGESTS THAT THE DISAGGREGATION OF SUPPORT IS NOT INHERENTLY COSTLY?**

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[22] OTA Response to Joint Data Request Nos. 3, 5, 6.
[23] Presumably this awareness came by way of a friend of a friend who heard someone say that an ILEC somewhere had paid $90,000 for a disaggregation study.
[24] OTA Response to Joint Data Request No. 4.

A. Yes. Exhibit RCC-USCC/6 is an Excel spreadsheet that I created that can be used to disaggregate the federal USF support that a rural ILEC ETC receives.

Q. **WAS THIS SPREADSHEET "UNDULY COSTLY AND BURDENSOME" TO PRODUCE?**

A. No. Because my Excel skills are admittedly a little rusty, it took me approximately two hours to create this spreadsheet in its current form.

Q. **PLEASE EXPLAIN YOUR METHODOLOGY FOR THE DISAGGREGATION OF SUPPORT.**

A. In order to be consistent with the requirements of 47 CFR §54.315, the disaggregation of support must reasonably reflect the differences in cost among geographic areas (in this case, wire centers). It is not necessary to develop a measure of the actual level of cost for each wire center; it is only necessary to develop a way to reflect the relative cost levels.[25] Wire center-specific costs are available from several different proxy models, including the HAI, BCPM, and the FCC's synthesis model. There is no reason to debate whether the results of these models represent the appropriate level of costs for the ILEC to recover or whether rural ILECs should receive USF support based on embedded or forward-looking costs, because the absolute level of cost has no impact on the process. What these model results can be used to produce is a set of factors that represent the relative differences in cost among wire centers. The ILEC's level of per-line support, based on average costs, can then be multiplied by each wire center-specific relative cost factor to produce a wire center-specific level of per-line support. As

[25] For example, it is not necessary to be able to definitively calculate that the cost per-line for wire center X is $15 and the per-line cost for wire center Y is $30, it is only necessary to be able to determine that the per-line cost for wire center Y is two times the per-line cost of wire center X.

shown at the bottom of the spreadsheet, the amount of support based on these disaggregated amounts can be compared to the current level of support to confirm that the amount of support received by the ILEC remains the same, consistent with the requirements of §54.315.

Q. **IS IT REASONABLE TO USE THE RESULTS OF COST PROXY MODELS FOR THIS PURPOSE?**

A. Yes. The use of the results of these models in this way is fully consistent with the requirements of §54.315. OTA asserts that "the available cost models such as the BCPM or the FCC's hybrid proxy model have been found to be inadequate for use in determining universal service support for rural companies."[26] This is not quite right; these models were found inadequate for determining the *level* of USF support for rural ILECs. In my illustrative process, the level of support is determined – as it must be – by the application of the FCC's modified embedded cost methodology; the ILECs will receive the same amount of total support as they do prior to disaggregation. The proxy model results are used only to create a set of relative cost factors that can be used to distribute the existing amount of USF support among wire centers based on the relative cost to serve each area.

Based on my review of these models, it appears that the models consistently err by overstating the cost to provide service in the lowest density areas. If this is the case, my illustrative method of disaggregation may result in per-line support in the higher-cost wire centers that is slightly higher than it should be, and per-line support in the lower-cost wire centers that is slightly lower than it should be. This bias is not problematic for two reasons. First, this

[26] OTA Response to Joint Data Request No. 7.

approach remains well within the §54.315 requirement that the disaggregated support "must be reasonably related to the cost of providing service for each disaggregation zone." Second, this amount of error, to the extent that it exists, can be considered as additional protection against the possibility of "creamskimming." A carrier serving only the lower cost areas will receive even less support than the cost of those areas would otherwise dictate. Similarly, a carrier's incentives to invest in the higher cost areas would be enhanced by the level of per-line support available in those areas.

Q. **HOW LONG SHOULD IT TAKE FOR THE ILEC ETCS IN OREGON TO DISAGGREGATE SUPPORT BY WIRE CENTER?**

A. For the single wire center ILECs, there is no theoretical possibility of "creamskimming" and no action is required (in effect, their support is already disaggregated by wire center). Because the opportunity exists for ILECs with multiple wire centers to disaggregate support using at least one method that (1) complies with the requirements of §54.315, (2) is straight-forward, simple, and based on readily-available information, and (3) is unlikely to be controversial, it is reasonable for the Commission to expect that the ILECs could complete a plan for the disaggregation of USF support at the wire center level within 30 days.

Q. **IS THERE ANY REASON FOR THE RURAL ILECS TO RESIST DISAGGREGATION ON THIS BASIS?**

A. Not that I can think of. If they are truly concerned about the potential for "creamskimming," this approach represents a way to prevent it that is certainly not unduly costly or burdensome. Of course, if the rural ILECs are not really all

that interested in preventing "creamskimming," but are instead primarily interested in having a "creamskimming boogeyman" that can be used to deter competitive entry or the designation of a CETC, then I expect that they will continue to resist disaggregation on any basis.

Should the Commission adopt an upper limit on the number of ETCs that can be designated in any given area (Issue II(B)(5))?

Q. **DOES THE PROCESS OF CAPPING THE NUMBER OF ETCS IN AN AREA PRODUCE ANY PUBLIC BENEFIT?**

A. No. As I explained in my direct testimony, such a cap would be duplicative of effective market forces and could artificially limit competitive entry that would be beneficial for consumers. Staff witness Marinos also points out that while limits on the number of ETCs that can be designated in a given area are sometimes proposed as a means of minimizing growth in federal fund, "there are other, better ways to accomplish that objective."

Both Mr. Wolf (p. 24) and Mr. Fulp (pp. 7-8) recommend capping the number of ETCs in a given area.[27] While Mr. Wolf offers no specifics, Mr. Fulp proposes a "presumptive limit" of only one ETC in a rural study area and two ETCs in a non-rural study area. Mr. Fulp asserts that this is sound public policy "at a time when USF support mechanisms are already strained."

As Ms. Marinos points out, "cap proposals are discriminatory in that they grant support based on order of designation and exclude other carriers from

[27] As OTA has clarified in response to Joint Data Request No. 20, Mr. Wolf is not actually recommending that a cap be applied, but only that the Commission "give careful consideration to this concept." Because Mr. Wolf is only recommending "careful consideration" and not the actual adoption of a cap, OTA objected to the request to provide any "studies, reports, analyses, or other documents" that might support a capping proposal.

consideration." This observation puts the ILECs' capping proposals in a new light. Presumably, the ILECs are suggesting that a cap be applied based on the order of designation rather than on the merits of any given carrier's application. Since the ILEC is almost always the first ETC designated for its service area, capping the number of ETCs based on the timing of the application assures the ILEC of a secure position and creates the discrimination problem described by Ms. Marinos.[28] This kind of "first in" capping mechanism might reduce growth in the fund over the short term, but clearly a "most efficient" capping mechanism would be a much effective means of reducing "strain" on the federal fund. Under such a mechanism, the Commission could adopt Mr. Fulp's proposal to designate only a single ETC in a rural study area, but would select that ETC based on an applicant's ability to provide the area with the broadest possible coverage at the lowest cost (and therefore with the lowest amount of required support). If Mr. Wolf is right when he claims that wireless CETCs have a lower cost than rural ILECs (the only logical basis for suggesting that wireless CETCs should not receive per-line support based on ILEC costs), then it is likely that under this more efficient capping mechanism the wireless CETC, and not the ILEC, would be the single ETC in the area.

It is possible that the ILECs have proposed capping the number of ETCs in their service areas because they are genuinely interested in controlling the growth of the federal fund. It is also possible that they are primarily interested in creating the kind of discriminatory barrier to entry noted by Ms. Marinos. One

[28] In Mr. Fulp's proposal, there would be a presumption that only one ETC – the rural ILEC – would be designated in its study area.

way to determine their true motives is to seek their support of an efficiency-based cap. An ILEC supporting such a cap is likely to have a genuine interest in the welfare of the federal fund, while an ILEC that opposes such a cap is likely to be primarily interested in creating a barrier to entry.

Q. **MR. WOLF ALSO SUGGESTS (P. 24) THAT THE COMMISSION SHOULD "GIVE CAREFUL CONSIDERATION" TO CAPPING THE NUMBER OF ETCS BECAUSE SUCH A PROPOSAL HAS BEEN MADE BY THE CONSUMER ADVOCATE IN WEST VIRGINIA. DO YOU AGREE WITH HIS REASONING?**

A. No. Mr. Wolf refers specifically to a proposal developed by Mr. Billy Jack Gregg.[29] Mr. Wolf does not mention that in its recommendation the Joint Board rejected a similar proposal by the same author, or that the Public Service Commission of West Virginia has (at least twice) rejected the same proposal.[30]

Equally importantly, the fundamental premise of the proposal is flawed. The current level of per-line support is a measure of the modified embedded costs of the existing wireline ILEC. Mr. Wolf is suggesting that the Commission treat this amount as some sort of economic cost benchmark that represents the relevant costs of an efficient provider utilizing the most efficient technology to serve a given area. In reality, it may be none of these: it is a measure of regulatory accounting, not economic, cost; the ILEC may or may not be an efficient provider, and a wireline network may or may not be the most efficient means of providing service to the area.

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[29] I have had the honor of debating this issue with Mr. Gregg on several occasions. While I agree with his objectives, I disagree that this kind of mechanism will permit those objectives to be achieved

[30] *Recommended Decision*, CC Docket 96-45, FCC 04J-1, released February 27, 2004, ¶44.

This kind of capping proposal is based on a purely short run view that distorts the analysis. By limiting entry by carriers as an ETC, the size of the federal fund will be kept small over the short run but will be larger than necessary over the long run. As the FCC has consistently concluded, the entry of CETCs can be expected to provide incentives for the ILECs to improve both efficiency and service quality. The way to minimize the size of the federal USF over the long run is to ensure that only the most efficient provider of the supported services is ultimately funded. The efficient network for a given high cost area may be wireline or wireless, and may be provided by the ILEC or a CETC. The only way to identify the efficient network configuration is to permit CETCs to serve an area on an equal footing with the ILEC.

It is possible that the ILECs are, or have the capability to become, the low-cost network solution for serving high cost areas. Of course, it is quite possible that another carrier can serve the area more efficiently. Because wireless and wireline costs vary in different ways, it is possible that wireless represents a lower cost solution to serve many areas that are high cost for the wireline ILEC. The only way to reach this efficient solution is to make ETC designations on a technology neutral basis. Once a CETC has the ability to provide service throughout the area in question, it may then be reasonable to apply a "most efficient" capping mechanism in order to minimize the size of the federal fund.

Q. **HAVE ANY OTHER STATE REGULATORS ADOPTED A CAP ON THE NUMBER OF ETCS DESIGNATED IN A GIVEN AREA?**

A. Not that I am aware of. OTA was asked in a data request to identify "any and all state commissions that have placed a restriction on the total number of ETCs in a given area." In response, OTA stated that it "had not done a survey of other state commissions," but referenced an order of the Idaho Public Utilities Commission as supportive of their position.[31]

Q. **ARE YOU FAMILIAR WITH THE IDAHO COMMISSION ORDER REFERENCED BY OTA?**

A. Yes. I am familiar with the order and participated in the litigation of the referenced case before the Idaho Commission.

Q. **IN THE ORDER REFERENCED BY OTA, DID THE IDAHO COMMISSION CAP THE NUMBER OF ETCS TO BE DESIGNATED IN A GIVEN AREA?**

A. No, nor am I aware that the Idaho Commission has done so in any other order.

III. Annual Certification of ETCs

Q. **WHAT IS YOUR POSITION REGARDING THE INFORMATION THAT SHOULD BE PROVIDED TO THE COMMISSION BY ETCS AS A PART OF THE ANNUAL RECERTIFICATION PROCESS?**

A. As Ms. Marinos correctly points out (p. 73), each year the Commission must certify to the FCC that all ETCs in the state are eligible to continue receiving federal USF support, and in doing so the Commission is "vouching for the ETCs' compliance with federal universal service obligations." Ms. Marinos goes on to state that "ideally, to grant recertification to an ETC, the Commission should make sure that the ETC has met its federal universal service obligations in the

[31] OTA Response to Joint Data Request No. 21.

past year and is likely to continue meeting them in the coming year." I would suggest that this is an essential, rather than "ideal," exercise: before recertifying to the FCC that any ETC – CETC or ILEC ETC – is fully in compliance with all ETC obligations, the Commission should have the information needed to make such a certification.

I agree with Ms. Marinos' conclusions that when determining annual reporting requirements for ETCs, the Commission should "strive for neutrality across carriers for reporting and minimize reporting burdens to the extent possible," but my concern is that the objective of minimizing burdens should not override the need for essential information. The fact that the ILEC ETCs, as regulated former monopoly providers, currently provide a series of reports to the Commission does not mean that the ILECs should be excused from providing the information necessary for the Commission to certify their compliance with the requirements that are imposed on these carriers as ETCs. The FCC reached this same conclusion in its *2005 USF Order* and urges state regulators to apply these requirements to both CETCs and ILEC ETCs: "we encourage state commissions to adopt these annual reporting requirements. To the extent that they do so, we urge state commissions to apply the reporting requirements to all ETCs, not just competitive ETCs."[32] While there is no reason to require any ETC to provide the same information twice, it is essential that information that is provided for a different purpose (and that does not demonstrate whether support has been properly used or is needed for the ILEC to provide the supported services) not be

[32] *2005 USF Order*, ¶71.

accepted as a substitute for the information needed to ensure compliance with ETC obligations.

Q. **HOW DOES MR. WOLF ATTEMPT TO JUSTIFY EXCUSING THE ILECS FROM ETC COMPLIANCE REPORTING?**

A. Mr. Wolf argues (p. 26) that while the Commission should adopt all of the FCC's requirements for CETCs, some of these requirements are "not needed for the incumbent."

Mr. Wolf attempts to justify this conclusion, not with concrete examples of ILEC reports that demonstrate how USF funds have been used, but rather by way of an analogy. He describes Employee I, who goes out, incurs expenses, produces an itemized accounting of those expenses, and is reimbursed. In contrast, Employee C in Mr. Wolf's parable seeks an advance on the expenses without submitting the itemized accounting. According to Mr. Wolf, this distinction justifies additional reporting by Employee C.

The problem, of course, is that this example (1) misrepresents how CETCs actually receive support, and (2) is not analogous to the larger issue of how CETCs and ILEC ETCs should demonstrate that they have used all federal USF support for the purposes intended. Mr. Wolf continues to have his facts wrong regarding his assumption that ILEC ETCs receive USF support only after making network investments, while CETCs can receive support before making investments. A better analogy would be the following:

Suppose an engineering company has a federal contract to work on a project. The company has an obligation, on an annual basis, to verify to the

federal government that its employees have in fact worked on the project for the number of hours specified in the contract. Employee C[33] does not normally turn in a timesheet, so she prepares a report each month showing how many hours she worked on the project. Employee I is required to turn in a time sheet showing total hours worked (he is paid in arrears based on this timesheet), but does not show a breakout of hours worked on any given project.

If this company is going to verify that the correct number of hours is being devoted to this project, it will need a report from both Employee C and Employee I showing the number of hours worked *on the project*. Employee I may insist that this is unnecessary because he already reports his total time and is only paid after he has worked the reported number of hours, but the fact remains that he has *not* shown that he has devoted a portion of the total hours to the for which the company is being reimbursed.

As Mr. Wolf points out (p. 27), the progress report that he argues should be required from CETCs, but not from ILEC ETCs, "shows how the high-cost funds have been expended." If the reports that the ILECs provide to the Commission show the equivalent of total time (but not time spent on the project in question) – and my review suggests that this is the case – then the ILECs are *not* showing "how the high cost funds have been expended" and the Commission is in no position to verify the proper use of these funds to the FCC.

The problem would be magnified if Employee I had already worked his budgeted hours for the project, while Employee C had specific tasks associated

[33] Mr. Wolf used I and C, presumably to indicate ILEC ETC and CETC. For clarity I will follow his naming convention.

with the project that she was expected to perform in the current period. It would then be even more prudent to require project-specific reporting from Employee I, as he is now claiming that some unspecified portion of his time is being spent on tasks that he had previously claimed to be completed.

Should the Commission adopt any, or all, of the FCC reporting requirements proposed in Order 05-46 (Issue III(A)(1))?

Q. **SHOULD THE FCC'S REPORTING REQUIREMENTS BE ADOPTED FOR ALL ETCS?**

A. Subject to the exception identified in my direct testimony,[34] the answer is: yes, unless and until the ILECs can demonstrate that reporting that is already being performed provides the same information (and not simply the equivalent of a timesheet with only total hours reported). If the information is truly duplicative, then it need not be provided twice.

Q. **DO YOU AGREE THAT, BASED ON THE REPORTS CURRENTLY BEING PROVIDED TO THE COMMISSION BY THE ILECS, THAT THEY SHOULD BE EXEMPT FROM THESE REPORTING REQUIREMENTS?**

A. No. As Ms. Marinos correctly states (p. 83), a report to the Commission "should address, in detail, how the ETC actually used the support money it received during the past year."

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[34] As I explained in my direct testimony (p. 41), annual reports showing progress in meeting a buildout plan should be tied to the requirements of the buildout plan. If the plan is based on a detailed two-year projection as proposed by Staff, then the annual reporting requirements should be consistent with that two-year projection, and not the FCC's five-year projection. I believe that this position is consistent with Ms. Marinos' testimony at p. 83.

Mr. Wolf provides no demonstration that such reporting is currently being done by the rural ILECs. When asked if "any of the reports currently provided by OTA members to the Commission include a description of how much universal service support was received and how the support was used," OTA referred to Form I.[35] I have reviewed Form I and its corresponding instructions, and have been unable to identify any information that purports to demonstrate that all (or any) federal USF received was used for the intended purposes.

Form I includes an accounting of an ILEC's expenditures, broken out by USOA account, and does include a line item indicating the amount of federal USF support received. What Form I does *not* do is connect the dots: it does not require the ILEC ETC to show how the identified federal USF support was used only for the "provision, maintenance, and upgrading" of facilities for which the support is intended. The information provided to the Commission on Form I, like the information provided to the FCC through NECA, does not provide an up-front accounting of how the funds are going to be used, but simply confirms that a given level of total cost was incurred. The use of the funds must be determined in a separate step before the Commission should certify to the FCC that the ILEC is in full compliance with its ETC obligations.

Should the Commission adopt any other reporting requirements (Issue III(A)(2))?

Q. **ARE YOU AWARE OF ANY ADDITIONAL REPORTING REQUIREMENTS THAT NEED TO BE ADOPTED?**

[35] OTA Response to Joint Data Request No. 14.

A. No. The relevant information can be obtained through the FCC's requirements. The key is for the Commission to ensure that it has *all* of the necessary information for *all* ETCs that it is being asked to recertify to the FCC.

Should the same reporting requirements apply to all types of ETCs – ILEC ETCs and competitive ETCs (Issue III(A)(3)?

Q. **IS IT YOUR POSITION THAT ALL ETCS MUST PROVIDE IDENTICAL REPORTS TO THE COMMISSION?**

A. No. I agree with Ms. Marinos that competitive neutrality "does not mean that all ETCs must have the exact same annual reporting requirements for universal service recertification," and that "all ETCs should demonstrate compliance with all ETC requirements, but not necessarily in the same ways." As explained above, however, I do believe that before deciding that certain ETCs need not report a particular kind of information, that the Commission be assured that the information is already being collected in another manner.

I must disagree with Ms. Marinos that this assurance can be assumed with regard to all relevant information. Regarding a demonstration that funds have been used only for the intended use, for example, I do not agree that ILECs should be exempt from such reporting. Ms. Marinos suggests (pp. 89-90) that ILECs need not demonstrate their use of funds because "while they are expected to maintain acceptable service and network quality, they are not expected to use universal service funds to expand their networks." This may be true in most cases, but the ILECs *are* expected – and required – to use the funds only for the "provision, maintenance, and upgrading" of facilities used to provide the

supported service functionalities. They are not expected (or permitted), for example, to use the funds frivolously[36] or to invest the funds in equipment or facilities to provide non-basic services. While Ms. Marinos is correct that the ILECs currently "submit financial reports to the Commission on an annual basis," as described above I have been unable to identify any report that demonstrates the appropriate use of USF funds. When asked in discovery, OTA could not do so either.

In summary, the fact that the ILECs currently submit reports to the Commission is not a substitute for a process of collecting the information necessary for recertification. Until it is shown that an existing report actually contains the requisite information, the ILECs should not be excused from the FCC reporting requirements.

Should the same reporting requirements apply regardless of the type of support received by the ETC (Issue III (A)(4))?

Q. **DO YOU HAVE ANYTHING TO ADD TO YOUR DIRECT TESTIMONY ON THIS ISSUE?**

A. No.

Q. **DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

A. Yes.

[36] By spending $90,000 for a disaggregation study, for example.

Illustrative Disaggregation Analysis

Wire Center	Access Lines	Per-Line Cost (Proxy Model)	Relative Cost Factor	Per-Line Disaggregated Support
1	100	$23.00	1.16	$34.68
2	200	$19.00	0.96	$28.65
3	100	$24.00	1.21	$36.19
4	300	$18.00	0.90	$27.14
5	250	$20.00	1.01	$30.16
Total	950			

Development of Relative Cost Factor:

Weighted Average Cost, all wire centers $19.89 (weighted by access lines)

Wire Center	Per-Line Cost (Proxy Model)	Relative Cost Factor = Wire Center Per-Line Cost/Weighted Average Cost
1	$23.00	1.16
2	$19.00	0.96
3	$24.00	1.21
4	$18.00	0.90
5	$20.00	1.01

Cross Check

Current Per-Line Support $30.00

Total Current Support $28,500.00 ($30.00/line x 950 lines)

Disaggregated Support:

Wire Center	Per-Line Disaggregated Support	Wire Center Access Lines	Wire Center Total Support
1	$34.68	100	$3,468.25
2	$28.65	200	$5,730.16
3	$36.19	100	$3,619.05
4	$27.14	300	$8,142.86
5	$30.16	250	$7,539.68
		Total Disaggregated Support	$28,500.00

CERTIFICATE OF SERVICE

UM 1217

I hereby certify on this 8th day of February, 2006, the Rebuttal Testimony of Don J. Wood on behalf of RCC Minnesota, Inc. and United States Cellular Corporation was sent via UPS overnight mail to the Oregon Public Utility Commission.

Also, a copy of the filing was sent electronically to the service list which is attached.:

DAVIS WRIGHT TREMAINE LLP

By: _____
Mark P. Trinchero

Public Utility Commission

eDockets

Docket Summary

Docket No: UM 1217 **Docket Name:** TELCO CARRIERS ELIGIBLE FOR FEDERAL UNIVERSAL SERVICE SUPPORT

Print Summary

In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Staff Investigation to Establish Requirements for Initial Designation and Recertification of Telecommunications Carriers Eligible to Receive Federal Universal Service Support. (Staff report for...

Filing Date: 8/16/2005

Case Manager: KAY MARINOS **Phone:** (503) 378-6730 **Email:** kay.marinos@state.or.us

Law Judge: CHRISTINA SMITH **Phone:** (503) 378-6208

Email Service List (semi-colon delimited) Email Service List (comma delimited)

ACTIONS **SERVICE LIST (Parties)** SCHEDULE

W=Waive Paper service **Q=Confidential** Sort by Last Name Sort by Company Name

AT&T WIRELESS SERVICES

CINDY MANHEIM
16331 NE 72ND WAY RTC1
REDMOND WA 98052
cindy.manheim@cingular.com

CITIZENS' UTILITY BOARD OF OREGON

JEFF BISSONNETTE
610 SW BROADWAY STE 308
PORTLAND OR 97205-3404
jeff@oregoncub.org

JASON EISDORFER
610 SW BROADWAY STE 308
PORTLAND OR 97205
jason@oregoncub.org

DAVIS WRIGHT TREMAINE LLP

MARK P TRINCHERO **(Q)**
1300 SW FIFTH AVE STE 2300
PORTLAND OR 97201-5682
marktrinchero@dwt.com

DEPARTMENT OF JUSTICE

MICHAEL T WEIRICH **(Q)**
ASSISTANT ATTORNEY GENERAL
REGULATED UTILITY & BUSINESS SECTION
1162 COURT ST NE
SALEM OR 97301-4096
michael.weirich@state.or.us

EDGE WIRELESS, LLC

KEVIN KEILLOR
650 SW COLUMBIA - STE 7200
BEND OR 97702
kjkelllor@edgewireless.com

FRONTIER

CHARLES L BEST
ATTORNEY AT LAW
PO BOX 8905
VANCOUVER WA 98668-8905
cbest@eli.net

FRONTIER COMMUNICATIONS OF AMERICA INC

INGO HENNINGSEN
3 TRIAD CTR STE 160
SALT LAKE CITY UT 84180
ingo.henningsen@czn.com

GVNW CONSULTING INC

JEFFRY H SMITH
CONSULTING MANAGER
PO BOX 2330
TUALATIN OR 97062
jsmith@gvnw.com

LAW OFFICE OF RICHARD A FINNIGAN

RICHARD A FINNIGAN **(Q)**
ATTORNEY AT LAW
2112 BLACK LAKE BLVD SW
OLYMPIA WA 98512
rickfinn@localaccess.com

MALHEUR HOME TELEPHONE CO

JAMES TODD **(Q)**
CORPORATE PRESIDENT
PO BOX 249
ONTARIO OR 97914
jimmy.todd@qwest.com

MILLER NASH LLP

BROOKS HARLOW **(Q)**
ATTORNEY
601 UNION ST STE 4400
SEATTLE WA 98101-2352
brooks.harlow@millernash.com

OREGON TELECOMMUNICATIONS ASSN

BRANT WOLF
EXECUTIVE VICE PRESIDENT
707 13TH ST SE STE 280
SALEM OR 97301-4036
bwolf@ota-telecom.org

PUBLIC UTILITY COMMISSION OF OREGON

KAY MARINOS
PO BOX 2148
SALEM OR 97308-2148
kay.marinos@state.or.us

QWEST CORPORATION

ALEX M DUARTE **(Q)**
CORPORATE COUNSEL
421 SW OAK ST STE 810
PORTLAND OR 97204
alex.duarte@qwest.com

SPRINT/UNITED TELEPHONE CO OF THE NORTHWEST

WILLIAM E HENDRICKS **(Q)**
ATTORNEY
902 WASCO ST A0412
HOOD RIVER OR 97031
tre.e.hendricks.iii@sprint.com

DAVID PAULSON
902 WASCO ST

	HOOD RIVER OR 97031 david.paulson@mail.sprint.com
STOEL RIVES LLP	
TIMOTHY J O'CONNELL **(Q)**	ONE UNION SQUARE 600 UNIVERSITY ST STE 3600 SEATTLE WA 98101-3197 tjoconnell@stoel.com
VCI COMPANY	
STACEY A KLINZMAN DIRECTOR - REGULATORY COMPLIANCE	3875 STEILACOOM BLVD SW #A LAKEWOOD WA 98499 staceyk@vcicompany.com
VERIZON	
SCHELLY JENSEN MANAGER REGULATORY & GOVT AFFAIRS	PO BOX 1100 BEAVERTON OR 97075-1100 schelly.jensen@verizon.com
WANTEL INC	
MARTY PATROVSKY **(Q)** CONSULTANT - LIAISON OFFICER	1016 SE OAK AVE ROSEBURG OR 97470 marty.patrovsky@comspanusa.net