USF/ICC:
Rate of Return Recovery Mechanisms

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Universal Service Reform: The Basics

- Extends USF to broadband-capable networks
  - RoR carriers must offer broadband speed of 4 Mbps/1 Mbps upon customers' reasonable request
- Set "firm" budget at no more than $4.5 billion over next 6 years
  - Automatic trigger if threatened to be exceeded
  - RoR carriers will receive approximately $2 billion per year
- Creates new Connect America Fund (CAF)
  - Separate components for price cap and ROR companies
  - Separate mobility and remote areas funds
- Implements specific steps to reduce legacy high cost support

Universal Service Modifications

- Revised corporate operations expense limitation applied to HCL and ICLS (1/1/2012)
  - Update to existing formula for more recent data
  - FNPRM to address impact on ICLS
- Capital and operating expense limitations (7/1/2012)
  - Proposed methodology to be determined after further comment
- Phase out Safety Net Additive
  - If qualified at 14% TPIS, continue for remainder of eligibility period
  - If not, phase down in 2 steps: 50% in 2012, 0% in 2013

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Universal Service Modifications (cont.)

- Reduce HCL for companies with low end-user voice rates in 3 steps (beginning 7/1/2012):
  - Initial rate floor = $10 for 7/1/2012 to 6/30/2013
  - Step 2 = $14 for 7/1/2013 to 6/30/2014
  - Beginning 7/1/2014, to be determined by annual survey of voice rates
  - Support reduced dollar-for-dollar
- Local Switching Support eliminated as stand-alone support mechanism (7/1/2012)
  - Rolled into ICC CAF recovery mechanism

Universal Service Modifications (cont.)

- Revise HCL cap (1/1/2012):
  - Remove amount price cap carriers (and their affiliated RoR carriers) would have received for 2012
  - Recalculate cap and NACPL
- Cap per-line support at $250 per line per month over 3 year transition (7/1/2012):
  - Beginning 7/1/2012 = $250 + 2/3 excess
  - Beginning 7/1/2013 = $250 + 1/3 excess
  - Beginning 7/1/2014 = $250
- Phase out (over 3 years) high cost support in areas with 100% study area overlap by unsubsidized competitor(s)

Universal Service Modifications *(cont.)*

- Streamline study area waiver process
  - Eliminate “one percent” rule
  - Timeline:
    - Public Notice issued
    - Comments and reply comments: 30 and 45 days, respectively
    - Absent FCC action, deemed granted on 60^{th} day following reply comment due date
- “Parent Trap” rule revised (1/1/2012)
  - Lesser of support based on actual cost or existing section 54.305 calculation

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Do They Impact You?

- Corporate operations expense limitation – if already subject to limitation, generally YES.
  - New impact on ICLS
  - Largest impact on companies > 18,000 loops
- CAPEX and OPEX limitations – to be determined
- Safety Net Additive – NO if receiving based on TPIS only, YES if receiving based on loop loss
- Low end floor – YES if local rate is below $10
- LSS “elimination” – probably not
- $250 per month – probably not
- Unsubsidized competitor – probably not as currently implemented

Intercarrier Compensation Reform: The Basics

- Adopts rules to address access stimulation and phantom traffic
- Adopts uniform national bill-and-keep framework
- Implements ICC rate transition for:
  - Interstate switched access rates
  - Intrastate terminating access rates
  - Reciprocal compensation rates
- Adopts Recovery Mechanism as a component of CAF
- "Toll" VoIP to be charged access

ICC Modifications

- Access stimulation:
  - Refile rates if:

    (1) Revenue sharing agreement and

    (2) Either: 3-to-1 ratio of terminating to originating traffic, or 100% increase in traffic
- Phantom traffic
  - Include calling party's telephone number in call signaling
  - Require intermediate carriers to pass along signaling information in unaltered format

ICC Rate Transition

- Nine years to bill-and-keep rates for RoR companies (six years for price cap)
  - 2 steps from Intrastate to Interstate
  - 3 additional steps to \$0.005
  - 3 additional steps to \$0.0007
  - 1 additional step to bill-and-keep
- Terminating rates only
- Intrastate transport rates transition to interstate levels; no further reduction
- Reciprocal compensation rates included to extent above specified rate levels

ICC Rate Transition

Date	Action
Effective date of rules	Cap all interstate switched access rates and intrastate terminating access rates, including transport and recip comp
July 1, 2012	Reduce intrastate terminating switching and transport rates and recip comp by 50% of difference to interstate rates
July 1, 2013	Intrastate and recip comp rates in parity with interstate rates
July 1, 2014	Terminating switched end office and recip comp rates are reduced by 1/3 of differential between end office rates and $0.005
July 1, 2015	... additional 1/3 of differential
July 1, 2016	At $0.005
July 1, 2017	Rates reduced by 1/3 of the differential between end office rates at $0.005 and $0.0007
July 1, 2018	... additional 1/3 of differential
July 1, 2019	At $0.0007
July 1, 2019	Reduced to bill-and-keep

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ICC Recovery Mechanism

- Defines “Eligible Recovery” for RoR carriers as:
  - Baseline for recovery, minus ...
  - Revenues from ICC rates for given year
- Baseline for recovery equals:
  - 2011 <u>projected</u> interstate switched access revenue requirement (from annual tariff filing), plus ...
  - FY 2011 intrastate terminating switched access revenues and FY 2011 net recip comp revenue
    - FY 2011 defined as 10/1/2010 to 9/30/2011
  - RoR baseline for recovery reduced by 5% each year

Eligible Recovery Example

Item	Year 1 Amount	Year 2 Amount
2011 Interstate Switched Access RRQ	$200,000	
FY 2011 Intrastate Terminating Revs	$50,000	
FY 2011 Net Reciprocal Compensation	$5,000	
Total	**$255,000**	**$242,250**
Baseline Reduction	.95	.95
Total Baseline	**$242,250**	**$230,138**
ICC Recovery (rate x MOU)	$100,000	$90,000
Eligible Recovery	**$142,250**	**$140,138**

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ICC Recovery Mechanism (cont.)

- Access Recovery Charge (ARC) for RoR carriers
  - End user charge
  - Allowed to increase over 6 years
  - $0.50 increase per year for residential or single-line business
    - Can't exceed $30 "Residential Rate Ceiling"
    - Not charged on Lifeline customers
  - $1.00 increase per year for multi-line business
    - Maximum SLC + ARC = $12.20

ICC CAF Calculation

	Year 1	Year 2
Total Baseline	**$242,250**	**$230,138**
... minus...		
ICC revenues (at default ICC rates)	**$100,000**	**$90,000**
... minus...		
ARC revenues (imputed if not assessed)	**$6,600**	**$12,780**
... equals ...		
ICC CAF	**$135,650**	**$127,358**

ICC Recovery

- FCC is moving RoR carriers to a form of incentive regulation for ICC:

  "... we adopt an approach to Rate-of-Return Eligible Recovery that takes interstate rate-of-return carriers off of rate-of-return based recovery specifically for interstate switched access revenues ..."

  - What happens if my actual Baseline amount doesn't decrease by 5% each year?
  - What happens if my actual Baseline amount decreases by more than 5%?

So, Where's the Broadband CAF?

- It's in the Further Notice of Proposed Rulemaking (FNPRM)!
  - Seeks comment on the Rural Associations Plan
  - Asks whether savings realized from other programs can be used for increased RoR funding
  - Seeks comment on benefits and costs of supporting "middle mile" facilities
  - Calculation of "take rate" and use in interstate cost allocation
  - Use of urban benchmark
  - Impact of lower RoR