



The USF Reform Order: Remaining Challenges on the Path to New Success & Stability

Missouri Telecommunications Industry Association
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A Watershed Moment

- USF Mechanisms Dating Back to Late 1990's Reformed
- Creation of Standalone Broadband Mechanism
- Introduction of Model Support for First Time (on OPTIONAL Basis)
- *Critical Question: Is this Good, Bad, or Both?*
 - Answer won't be clear until we know who elects what and until other implementation details are defined

How Did We Get Here?

- 2010 National Broadband Plan
 - Recommends mandatory conversion of all RLECs to Model
 - Cap budget at 2010 levels and use “savings” for Model distributions tied to broadband buildout obligations
- 2011 “Transformation” Order
 - Creates \$2B budget “target”
 - No broadband-oriented changes or updates
 - Creates QRA as OpEx and CapEx caps
 - 100% Study Area Competitive Overlap rule
 - Threatens sub-9% RoR and further Competitive Overlap changes

How Did We Get Here? (cont.)

- 2014 Further Notice
 - Reaffirms commitment to \$2B budget as part of any further reforms
 - Seeks comment on optional model and broadband changes and updates
 - Seeks new prospective capital expense limits and expanded OpEx caps
 - Suggests disallowing USF in any “competitive” census block
- 2016 Reform Order
 - Adopts \$2.15B budget, subject to budget control Adopts standalone broadband update and model option
 - Adopts new prospective capital expense limits and expanded OpEx caps
 - Adopts 85% overlap by census block, with disaggregation options
 - Reduces RoR to 9.75% over 6 years

How Did We Get Here? (cont.)

- To Summarize, We Got Here in Part Because the National Broadband Plan Charted a Far Worse Destination Years Ago . . .
- But Good Progress Made Since Then:
 - RoR: 11.25% → Eliminate → 9% → 7.5% → 9.75% Over 6 Years
 - OpEx/CapEx: No Caps → Mandatory Model → QRA → Prospective CapEx Budget and More Predictable OpEx Limit, or Voluntary Model
 - Competitive Overlap: 75% Study Area Coverage/Undefined Disaggregation → 50% Census Block Coverage/Per-Line Disaggregation → 85% Census Block Coverage/Several Cost-Based Disaggregation Options

Devils and Details

1. Distribution Reforms

- a. Standalone Broadband Update
- b. Voluntary Model Option

2. Expense Limits and Budget Controls

- a. CapEx Limits
- b. OpEx Limits
- c. Budget Control
- d. RoR Represcription

3. Competitive Overlap (Non-Model and Model)

4. Buildout and Reporting Requirements (Non-Model and Model)

Distribution Reforms: Standalone Broadband Update

- **Basics - Standalone Broadband Update**
 - ICLS expanded and remade into CAF-BLS
 - Voice component of CAF-BLS subject to \$6.50 SLC
 - Broadband component of CAF-BLS subject to \$42 threshold
- **Thoughts/Questions**
 - Moves USF away from rural growth factor and “shrinking USF”
 - Allows certain limits to apply only to portions of USF support
 - **But will it actually make standalone broadband affordable?**
 - What are possible shifts among RLECs as a result of structure?
 - Short-term benefits for carriers vs long-term gains for industry

Distribution Reforms: Voluntary Model Option

- **Basics – Model Election**

- FCC publishes “Initial Final Offer,” leveraging \$150M in CAF Reserves
- RLECs have 90 days to express interest; if budget is sufficient, then expressions of interest are binding
- If budget is insufficient, FCC will re-run model “Final Final Offer” at lower per-location cap; RLECs have 30 days to confirm interest
- RLEC can accept or reject Final Final Offer

- **Thoughts/Questions**

- Provides 10-year stability for defined obligations
- Is support sufficient for each individual RLEC to elect?
- What is budget between model and non-model RLECs?
- What happens at end of 10 year model term?

Expense Limits and Budget Controls:

CapEx Limits

- **Capital Investment Allowance**
 - Intended to “pace” investment over many years
 - Tied to current state of depreciated plant and level of unserved locations as compared to national average
 - Will provide prospective budgets
 - This is non-model – model has “built-in” limits of course
- **Thoughts/Questions**
 - Not unpredictable or retroactive like QRA, but . . .
 - Is the prospective budget sufficient given inflationary factor?
 - Will the “streamlined waiver” process be effective in overcoming any individual company issues?

Expense Limits and Budget Controls: OpEx Limits

- **Operating Expense Limits**
 - In addition to – not in place of – current corporate OpEx caps
 - Formula will be calculated 2Q/3Q 2016
 - 50% phase-in year 1
 - This is non-model – model has “built-in” limits of course
- **Thoughts/Questions**
 - Not unpredictable or retroactive like QRA, but . . .
 - FCC to revisit every few years – does this recreate QRA-style concern?
 - **Lack of inflationary factor a problem?** (Corporate OpEx and CapEx do have inflationary factors)

Expense Limits and Budget Controls:

Budget Control

- **Budget Control “Haircut”**
 - Half per-line, half % reductions, intended to “share pain”
 - Tied to \$2.15B, but really only affects non-model companies after model electors lock in
 - Applies to broadband portion of CAF-BLS first, and then voice portion of CAF-BLS
 - FCC tried to start it July; got it pushed back to September (\$14M)
- **Thoughts/Questions**
 - Lack of inflationary factor on budget control is looming issue
 - Effect on standalone broadband rates? Common Line cost recovery? State funds?

Expense Limits and Budget Controls: RoR Represcription

- **Represcription from 11.25% to 9.75% over 6 Years**
 - Starts July 2016
 - Affects all high-cost and interstate rates
- **Thoughts/Questions**
 - What is real impact given prior inability to realize 11.25%?
 - What is real impact given budget control?
 - What is value of certainty given RoR threats for years?

Competitive Overlap: Non-Model Side

- **Limit CAF-BLS Support in Competitive Areas**
 - Competitor must file showing 85% of locations in census block covered with voice and broadband of certain quality/rates
 - Competitor bears burden of proof; RLEC can rebut
 - If competition found, CAF-BLS (not HCLS) is eliminated for the block(s)
 - If competition found, RLEC can disaggregate pursuant to 3 options
 - Analysis done only once every 7 years
- **Thoughts/Questions**
 - How many competitors will actually show?
 - Will disaggregation work to help as intended?

Competitive Overlap: Model Side

- **Competitive “Challenge” Process as Farce**
 - RLECs given limited window to disprove June 2015 Form 477 data
 - Competitors given opportunity to expand Form 477 data
 - RLECs bear burden of proof: “NFL instant replay” standard
 - Only one location needs to be served for whole census block to be lost
- **Thoughts/Questions**
 - Will any census blocks be “re-inserted”?
 - Will competitors knock out any more census blocks?
 - False positives – “shared” census blocks by RLECs

Buildout and Reporting Requirements: Non-Model Side

- **Non-Model Buildout Duties**

- Buildout obligations based upon % of Projected CAF-BLS divided by your choice of Cost per Loop formulas
- Report on new locations on geocoded basis; 5-year plans eliminated

- **Thoughts/Questions**

- Will Projected CAF-BLS accurately reflect future support?
- Will Cost per Loop formulas provide sufficient flexibility to RLECs?
- After 5 years, what is potential for “reset”?

Buildout and Reporting Requirements: Model Side

- **Model Buildout Duties**

- Certain % of Model Locations must be reached within 10 years
- % Differs by Density and Levels of Funding at locations
- Milestones apply over 10 years
- Report on all locations installed (old and new) on geocoded basis; 5-year plans eliminated
- Consequences for missing buildout

- **Thoughts/Questions**

- Even with model funding increases, can one obtain financing and deliver?
- What happens to partially funded locations?
- **After 10 years, will services/networks be self-sufficient?**
- What happens if buildout reports don't match prior coverage claims?

Other Pending Issues

- **Further Notice**
 - Permissible Expenses
 - Cost Allocations
 - Revised/reduced Reporting Requirements
 - Tribal Area Support
- **Reporting Requirements**
 - Performance measurement for speed and latency
 - Rationalize/reconcile with Open Internet transparency duties?
- **CAF 2 Competitive Bidding**
 - Alliance with Electricians on “Future-Proof” Networks
 - Challenges from WISPs and Satellite

Having Shared My Thoughts and Questions, What are Yours?