

ORDER NO. 95-1103

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BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON

In the Matter of the Investigation of Universal
Service in the State of Oregon

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)ORDER

DISPOSITION: UNIVERSAL SERVICE PROPOSAL ADOPTED SUMMARY

Four Main Issues

There are four main issues addressed by the Commission in this docket:

1. The definition of universal service
2. The design objectives for a universal service funding mechanism
3. The collection mechanism to acquire funds for the plan

4. The distribution mechanism to provide funding to support universal service goals

In summary, the Commission reached the following conclusions on these issues:

Definition. Basic telephone service, for universal service purposes, is affordable switched access to the network, consisting of single-party, voice grade service with touch-tone capability. A customer would have access to local calling, including extended area service (EAS), and to ancillary services (e.g. operator services, 911). Toll blocking would be available at no cost for low-income customers. No specifications for data transmission or information service access are mandated at this time, but the Commission will monitor these issues.

Design. A universal service fund should (1) be administratively simple and low cost, (2) provide the minimum amount of support necessary to maintain affordable basic network access service, and (3) require the price of basic service to cover costs prior to applying universal service credits. The universal service fund collection mechanism should (1) be supported by a broad user base and (2) be as competitively neutral as possible. Finally, distribution of universal service support should (1) maintain affordable basic local exchange service, (2) promote operating efficiency, and (3) eliminate artificial investment incentives.

Collection. The Commission adopts a gross revenue fee on all telecommunications providers to fund universal service. Legislation will be required to extend the Commission's statutory authority to include radio common carriers (RCCs) in the universal service collection and distribution mechanisms.

Distribution. The Commission adopts three basic methods of support for universal service: (1) support for local exchange carriers (LECs) who are carriers of last resort and whose overall rates would be excessive without universal service support; (2) support for targeted high-cost residential customers, triggered if the Commission orders fully regulated LECs to deaverage; and (3) expanded support for low-income residential customers.

Two-Year Review. The Commission adopts this universal service plan, subject to a review in two years, concurrent with the expiration of the Oregon Customer Access Fund (OCAF) plan, and possible sunset or changes in the Residential Service Protection program (chapter 290, Oregon Laws 1987, as amended). This will allow the Commission to adjust the plan as necessary to recognize the effects of UM 351, increased competition, OCAF changes, federal actions, and other developments.

EXISTING UNIVERSAL SERVICE SUPPORT

A number of support mechanisms already are in existence at the state and federal levels.

Federal. Under the jurisdiction of the Federal Communications Commission (FCC), three explicit universal service support programs are currently operating: (1) the Universal Service Fund, a high-cost local exchange carrier (LEC) assistance program based on study area loop costs; (2) Lifeline Assistance programs, including Link-Up America, targeted to qualifying low income residential subscribers; and (3) Telecommunications Relay Service (TRS), targeting individuals with hearing and speech disabilities.

Oregon. Oregon has three counterparts to the federal programs: (1) OCAF, supporting the cost of basic local exchange service in high-cost areas; (2) Oregon Telephone Assistance Program (OTAP) for low-income residential customers; and (3) the Telecommunications Devices Access Program (TDAP) for disabled persons. Additional methods used by the Commission to foster universal service include low service connection charges, low-cost service options (e.g. budget measured service), and the elimination of mileage charges for rural customers. Rate stability and network modernization are also important elements in enhancing universal service. In the Matter of the Investigation into the Revenue Requirement and Rate Structure of Pacific Northwest Bell Telephone Company, dba U S WEST Communications, UT 85, Order No. 90-920, p. 10-11.

Unless otherwise noted, these support mechanisms are not affected by this order. A more detailed description of these programs is attached to this order as Appendix A.

PROCEDURAL HISTORY

On January 12, 1995, Hearings Officers Simon ffitch and Nadine Faith held a prehearing conference in Salem, Oregon, to identify parties and interested persons, and to adopt a procedural schedule. At staffs request, the Hearings Officers bifurcated this proceeding into two parts. Phase I addresses policy issues and proposals relating to universal service funding, while Phase II addresses specific implementation issues for the funding proposal approved in Phase I.

Staff identified the four following issues for Phase I:

- (1): How should universal service be defined?
- (2): What should the objective criteria be for universal service funding?
- (3): Who should pay for universal service and how should the assessment be levied?
- (4): Who should receive universal service assistance?

On April 7, 1995, parties filed opening comments and draft proposals regarding universal service in Oregon. After a series of workshops, staff filed a revised proposal for a universal service funding mechanism on May 15, 1995.

The following parties commented on staffs proposal: U S WEST Communications, Inc., (USWC), GTE Northwest Inc. (GTE), PTI Communications (PTI), Oregon Independent Telephone Association (OITA), Oregon Exchange Carrier Association (OECA), Sprint Corporation and United Telephone Company of the Northwest (Sprint/United), MCI Telecommunications Corporation (MCI), AT&T, McCaw Cellular Communications (McCaw), Electric Lightwave Inc. (ELI), Teleport Communications Group (Teleport), Oregon Cable Telecommunications Association (OCTA), and Parker Communications.

On June 21, 1995, a hearing was held before Hearings Officers Simon ffitch and Nadine Faith in Portland, Oregon. The parties listed above appeared to respond to questions and to comment

orally on staffs proposal and other docket issues.

On July 12, 1995, staff filed a post-hearing brief to address three legal issues that had been raised at hearing.

I. DEFINITION

Staff Proposal

Staffs proposed definition for basic service is divided into three primary headings: access parameters, access to services, and service standards.

1. Access Parameters

Staff proposes that the basic universal service standard include the following access parameters:

Affordable switched network access that provides: (1) single-party service with (2) voice grade or equivalent transmission parameters, (3) touch-tone capability, (4) toll blocking capability, and (5) a single directory listing.

Toll blocking and a directory listing should be provided free, if requested.

2. Access to Services

Staff proposes that the public switched network allow access to:

- (1) the local exchange network, Extended Area Service (EAS) where ordered by the Commission, and long distance services;
- (2) emergency 911 services (including E-911 by the year 2000);
- (3) relay services for the hearing and speech impaired;
- (4) operator services such as call completion assistance, special billing arrangements, service and trouble assistance, and billing inquiry; and
- (5) directory assistance.

3. Service Standards

Staff proposes that the basic universal service standard should include service quality standards set forth in the Commissions Administrative Rules. (i.e. OAR 860-23-005, 860-23-055, 860-34-380 and 860-34-390.) In making the proposal, staff acknowledges that some service standards may need modification to better define where universal service standards are not being met and to accommodate other technologies, such as wireless telecommunications.

Summary of Party Comments; Discussion

Most parties submitting comments in this proceeding agreed that a definition of services should be dynamic in order to respond to changes in the marketplace. Most suggested that the Commission conduct a periodic review of the issue to keep current with the ever-continuing proliferation of new services. The parties also agreed, however, that the definition of basic services should be based on current network capabilities. Such a pragmatic approach, it is argued, will allow timely development of a workable funding mechanism and enable the prompt resolution of related regulatory issues.

1. Access Parameters

No party disputes the inclusion of the first three and the last of staffs proposed components. Voice grade, single party service with touch-tone capability is perhaps the most basic service provided by the local exchange company. Directory listing is commonly recognized as an integral part of that service.

Several parties, however, oppose the inclusion of free toll-blocking capability. PTI contends that toll blocking is just one of many service options a customer may chose to purchase and, as such, should not be subsidized. MCI argues that toll blocking is not part of plain old telephone service, and, accordingly, should not be considered an essential service. GTE acknowledges that toll blocking serves a useful purpose in some customer situations, but adds that the service does not have widespread customer demand. USWC notes that it currently assesses a recurring charge for that service and contends that the proposed elimination of that charge would cause a significant revenue impact on the company. As an alternative, USWC proposes the option of providing toll blocking at no charge to qualifying low income residential customers.

The Commission adopts the USWC toll-blocking proposal. Toll blocking is a useful service, particularly for those low-income customers who rely on it to prevent unauthorized long-distance calls that could jeopardize their access to the network. In this sense, toll blocking works as a mechanism to help achieve the goal of universal service. The service, however, is not used by a majority of residential customers, and the cost of subsidizing the service to all households does not appear to be in the public interest. The alternative proposal makes the service available to those customers who need it the most, while minimizing the cost incurred to provide the support. Free toll blocking should be limited to one line per residential household. The other disputed access parameter is data capability. The opening order in this docket proposed that the universal service standard include transmission quality to transport low-speed data (2400 bps) facsimile (fax) transmission as well as voice. Several parties opposed or questioned the inclusion of that parameter. Other parties recommended that the data transmission figure be increased. Parker, for example, proposed a 9600 bps capability.

In its revised proposal, staff did not include a specific data capability parameter in its definition of the universal service standard. Staff noted that access lines that meet the proposed service quality standards (see discussion below) would permit basic data transmission with a 9600 bps capability.

Based on that fact, the Commission concludes that this is a sufficient interim standard and should be adopted. In recognition of the need and desire for data transmission capability on the part of a growing number of customers, however, the Commission will continue to monitor this issue.

Resolution: Access Parameters:

The following access parameters should be adopted:

Affordable switched network access that provides: (1) single-party service with (2) voice grade or equivalent transmission parameters, (3) touch-tone capability, (4) toll blocking capability at no charge for OTAP customers (one line per residential household), and (5) a single directory listing. No specific data transmission capacity above current service standards is mandated at this time.

2. Access to Services

All parties generally support staff's proposal. Most view the access to these services as ancillary to the provision of basic service. Several parties did raise minor points, however.

Teleport recommends clarification of one aspect of the definition. It believes that the wording access to the local exchange network may cause confusion because the concept of the local exchange network will change as competition transforms existing exchange boundaries.

Teleport also argues that, in the near future, the local exchange network will no longer be just one network, but rather a number of interconnected networks. Teleport interprets the phrase to mean local calling within a limited area, and recommends that the definition be worded to that effect. Accordingly, it proposes the phrase local exchange network be replaced with calling within a local area. While Teleport is correct that competition is likely to change the definition of local calling, its proposed alternative - calling within a local area - is too unclear to be an adequate replacement. Staff's language is consistent with the current configuration of the network. For the most part, competition in the local exchange network in the near term is expected to make use of that existing network. Because universal service support is in part predicated on the provision of local service, staff's definition is more workable at this time and should be retained. General language can be added to the definition to indicate that equivalent service is also included.

GTE raises some concerns regarding the availability of emergency services. The company fully supports the availability of 911 and E-911 as part of the basic universal service package. It notes, however, that the universal deployment of those services depends, in part, on the appropriate governmental entities contracting with telecommunications providers for the service. GTE raises

a valid point. Implicit in the inclusion of 911 is the understanding that the underlying emergency service is provided by a third party. In effect, this part of the definition is subject to a where available condition. The Commission can address problems on this issue on a case-by-case basis through a waiver process if a particular company encounters problems with local emergency services.

OCTA agrees that, from a policy perspective, all callers should have access to operator services and directory assistance. It is concerned, however, about possible increases to the price of basic service if these two currently bundled services are made part of basic service. Consequently, it believes that further pricing information is required to determine the impact of including these services in the universal service concept. While pricing is a concern for any service, as OCTA concedes, operator service and directory assistance are essential components for basic service. They should be included in the definition of basic service for universal service purposes.

Resolution: Access to Services. Staff's list of proposed services is reasonable and should be adopted. Access to these services will enable customers to effectively interconnect with the public switched network while minimizing the cost incurred to provide universal service support. Mandatory access to advanced information services and other options, such as 800 services and voice mail, is not adopted at this time. As a practical matter, existing parameters allow access to a reasonable range of such services. In addition, at present, these services have not been selected by a substantial majority of residential customers. Mandating access to such services would impose a considerable cost burden on providers and on the support fund. As discussed above with regard to data transmission capacity, the Commission can revisit this issue to keep current with technological innovations and customer needs and expectations.

3. Service Quality Standards

AT&T and McCaw question the need to include service quality standards in the universal service definition. Both note that such standards were developed to ensure service quality in the context of a monopoly provided environment. In an emerging competitive environment, however, they contend that providers must meet or exceed these standards to satisfy customer expectations. They believe that market-place incentives should dictate service quality.

Resolution: Service Quality Standards. The Commission agrees that market forces may soon effectively determine service quality standards for competitive providers. Nonetheless, in order to qualify for universal service funds, service providers should at least meet minimum service criteria. In other words, these service criteria are not a condition to entry into the market, but rather a requirement to qualify for support funds. Accordingly, with that clarification, we conclude that staff's proposal should be adopted.

Criteria for Defining Universal Service

Certain criteria should be adopted to help the Commission in future proceedings to identify what services are to be considered essential for universal service policy. The criteria should focus on whether a service is so essential to the use of the telecommunications network that no customer should, as a matter of public interest, be denied access to the service on the basis of affordability. The criteria, however, must also be sufficiently flexible to be useful in classifying future services. The need for and scope of universal service will undoubtedly change in unanticipated ways. Any rigid formula adopted in this proceeding might limit the Commission's review in future proceedings.

After a review of these considerations, the Commission concludes that the following factors be included in the consideration of what basic services are covered for purposes of universal service support:

1. What is the level of demand for the technology or service?
2. Does the service or technology enable customers to access other telecommunication services?
3. Is the service optional?
4. To what extent would support for the service burden the universal service fund?
5. Is the service or technology generally available without regulatory intervention?

6. Is the service or technology necessary or desirable for public policy reasons?

II. DESIGN OBJECTIVES

Staff Proposal

Staff's proposal contains the following design objectives:

General: A universal service fund should (1) be administratively simple and low cost, (2) provide a minimum amount of support necessary to maintain affordable basic network access service, and, (3) require the price of basic service to cover costs prior to applying universal service credits.

Collection criteria (who pays): Universal service should (1) be supported by a broad user base and (2) be as competitively neutral as possible.

Distribution criteria (who receives): Universal service should (1) maintain affordable basic local exchange service, (2) promote operating efficiency, and (3) eliminate artificial investment incentives.

Staff comments that a universal service mechanism will, of necessity, represent a compromise among potentially conflicting objectives, existing statutes, and a dynamic balance between regulation and competition.

Party Comments

There is broad agreement among the parties with the proposed design parameters. Most comments addressed issues of competitive neutrality or limiting support to carriers of last resort. These issues are discussed below in the collection and distribution sections. GTE argues that General criterion 3 should state that price will cover cost plus a reasonable contribution. The company takes the view that, while the starting point for pricing is total service long run incremental cost (TSLRIC), that prices for all services should include some reasonable contribution level. In GTE's view, if service prices are capped at TSLRIC, then a firm cannot have a sustainable business, because there is no contribution to the common costs of the firm. In addition, GTE urges that whatever plan is adopted should retain some flexibility to respond to events at the federal level, so that eventually there can be a joint state/federal program.

Discussion

The General and Collection criteria track those set out in the Commission's opening order. Staff proposes two new distribution criteria, promotion of operating efficiency and elimination of artificial investment incentives. These are reasonable and should be adopted. GTE's arguments in favor of including contribution are better addressed in UM 351. In effect, the cost of basic service referred to here as a design parameter will incorporate the costing policies and methodologies adopted by the Commission in that docket.

Resolution. The Commission adopts the proposed design objectives.

III. COLLECTION MECHANISM

Staff Proposal

Staff proposes two alternative funding mechanisms for universal service support:

1. An intrastate gross revenue fee assessed upon all intrastate telecommunications services, including dedicated private line and radio common carrier (RCC services), or
2. A combination of line charges on local exchange end users and network access usage charges on interconnected interexchange traffic (excluding EAS) and interconnected RCC traffic.

Staff prefers the gross revenue fee. Intrastate gross revenues include revenues derived from both regulated and non-regulated telecommunications and ancillary services excluding uncollectible revenue, but including payments (reductions to gross revenue) to other Oregon telecommunications providers who (1) record the payments as gross revenue and (2) are similarly subject to the intrastate universal service fee. Reducing gross revenues by access payments prevents universal service fees from being collected twice on the same revenue dollar. This would be the most competitively neutral way, in staff's view, to finance universal service, and would provide long-term means of funding all Oregon universal service subsidies. Staff believes, however, that implementation of this approach would require legislation to include services provided by RCCs, including cellular, in the definition of telecommunications service under ORS 759.005.

Staff's second choice, a combination of line charges and access charges, does not require legislation. Both LECs and certified alternative exchange carriers (AECs) would be responsible for billing line charges to their customers and for billing usage charges for interconnected interexchange and RCC traffic. This is similar to the mechanism in place today to fund the OTAP and TDAP programs (end user line charges) and the Oregon Universal Service Fund (OUSF) (terminating network access usage charges). This second approach is not as competitively neutral as the first because the universal service charge would not be applicable to all providers and services and may encourage bypass.

Summary of Party Comments

ELI, Teleport Communications Group (Teleport), Sprint/United, PTI, MCI, OCTA, and Parker Communications support staff's gross revenue fee approach. In general, these parties agree that the approach is competitively neutral. There is general agreement also that the Commission may not currently have the authority to include RCCs within the fee. Parties who support the proposal indicate, however, that they would support an effort by the Commission to seek legislative approval to cover RCCs. Support among these parties for the staff's second line/usage alternative is mixed at best. It is seen as an interim approach.

GTE, USWC, AT&T, and McCaw generally oppose staff's proposed collection mechanisms. These parties propose a retail end-user surcharge, based on access lines or their equivalent. Sprint also advocates this approach as an alternative to the gross revenue fee. Under this third option, each customer would pay the same amount regardless of provider and regardless of use. The surcharge would be competitively neutral and easy to administer. It would make the universal service charge explicit to the customer.

Discussion

Of the three mechanisms suggested, the first and third are the most competitively neutral, to the

extent they can be applied to all or most providers. The staff's second alternative is primarily useful, as staff concedes, as an interim measure until a better mechanism is available, such as a gross revenue fee. At present, the retail end-user surcharge is arguably the most competitively neutral, assuming that the RCCs could not be made subject to the gross revenue charge.

Commission Authority. McCaw argues that the Commission has authority to authorize universal service support for RCCs under its general universal service authority, and because the Commission has already allowed LECs to use wireless technology for remote customers and held orders. Staff takes a contrary position, seeing the Commission's current authority over universal service as limited to LECs and AECs. Having reviewed the briefs of the parties, the Commission concludes that it does not have authority to impose a gross revenue charge and provide support to the RCCs under current Oregon law. The fundamental problem is that RCC services, such as cellular, were intentionally excluded from the definition of telecommunications service in ORS 759.005(2)(g). The universal service goals of the state are limited by statute to the support of telecommunications service. ORS 759.015. McCaw is correct that telecommunications service has been interpreted broadly. This has occurred, however, where the service provided (wireless, yellow pages, access, inspection and repair) was a part of or associated with regulated service. Where, by statutory definition, a RCC is not a regulated public utility, and its service not a telecommunications service, the Commission has no basis to incorporate RCCs in the universal service support mechanisms.

The situation is different for AECs. Unlike RCCs, AECs provide telecommunications service. See ORS 759.005(2)(g). Moreover, while AECs are excluded from the definition of telecommunications utility under ORS 759.005(1)(b)(C), the Commission is authorized to require AECs to make universal service support contributions. Specifically, ORS 759.050(2)(c) provides:

At the time of certification of a telecommunications provider, or thereafter, the commission may impose reasonable conditions upon the authority of the telecommunications provider to provide competitive zone service within the competitive zone including, but not limited to, conditions designed to promote fair competition, such as interconnection, and contributions of the type required of a telecommunications utility on account of the provision of local exchange service, including those to the Residential Service Protection Fund or the Telecommunications Devices Access Program.

To ensure fair competition, the Commission could provide, as part of the conditions for certification, that the AEC's customers be eligible for universal service support, provided that the support does not exceed the total contributions from the AEC or its customers. Such a condition would ensure that AEC customers are not being subsidized from funds raised under authority other than ORS 759.050(2)(c). For these reasons, the Commission concludes that AECs may be incorporated in the universal service mechanisms as set forth in this order.

Retail End-user Surcharge. There are public policy implications involved with the retail end-user surcharge. Use of a wholesale fee (gross revenue fee) treats the universal service fund as a cost of the system, or a cost to the companies operating in Oregon through which they contribute to enhance the infrastructure. While they are free to pass this cost on to customers, it is more consistent with the infrastructure philosophy than the surcharge. Stating the charge separately (explicitly) may create customer opposition and confusion, since it is likely to be perceived as a rate increase based on a subsidy, a welfare or social service charge grafted on to the rates which

has little to do with the majority of customers. This in turn may threaten universal service goals. This is inconsistent with the historical view of universal service, in which the goal of greater penetration of service yields a network of greater value to all users.

Resolution. The Commission will adopt the gross revenue fee approach, excluding the RCCs on interim basis, pending legislation to extend coverage to RCCs. The revenue fee is more competitively neutral than staff's second choice. The impact of exclusion on the RCCs during the interim, in any event, may not be great, since they do not compete for local exchange service or currently act as carriers of last resort and are unlikely to do so in the near term. Administratively, the revenue fee should not be too burdensome. The mechanism is already in place, and the methodology is understood by staff and the providers. Calculation of gross revenues for most providers already takes place for purposes of the utility assessment. The gross revenue fee, as a wholesale charge, avoids the public policy problems created by a retail end-user surcharge.

IV. DISTRIBUTION MECHANISM

Staff Proposal

Staff identifies three different circumstances which warrant financial support in order to increase the affordability of basic telecommunications service. These are:

Category 1: Support for LECs whose overall rates would be excessive without universal service support. Under this category, financial support would be provided only to the regulated LEC, or those firms which currently have the responsibility to act as the local carrier of last resort.

Category 2: Support for targeted high-cost residential areas under a deaveraged rate design. Financial support under this category would be available independent of which telecommunications firm provides the NAC or its equivalent. Category 2 support would be made available only if and when the Commission orders the fully regulated LECs to implement a distance- and density- related deaveraged rate design.

Category 3: Expanded support for low-income residential customer assistance. Support under this category would also be available regardless of the telecommunications firm providing the network access channel (NAC) or its equivalent.

In summary, staff proposes that the Commission retain the current OCAF/OUSF pooling mechanism (Category 1a) for an interim period for small LECs and establish two new programs (Category 1b and Category 2) with an expanded OTAP program (Category 3) in response to local exchange competition and the UM 351 costing and re-pricing docket. While these additional programs will not protect residential ratepayers completely, they will provide the Commission with a mechanism to help control residential rate increases and foster universal service in a more competitively neutral fashion.

Category 1 - Support for High-Cost LECs

Staff Proposal

All regulated LECs that make available basic universal services as defined above would be eligible for Category 1 support under staff's proposal. LECs not able to provide the basic level of service would need to request a Commission waiver and submit a plan to remedy the service deficiency.

The support mechanism would differ, depending upon whether or not the company is a current participant in OCAF. For the most part, the OCAF participants are smaller LECs, with the exception of PTI.

Category 1a: Support for LECs participating in OCAF. For LECs participating in the OCAF pooling mechanism (including PTI), small LECs (less than 15,000 access lines) and cooperatives, staff proposes that the Commission should continue, at least for an interim period, to use the OCAF plan to provide high-cost LEC support and high-cost residential rate support (that is, both Category 1 and 2 support). The plan is designed to provide overall cost support for LECs, as well as protect basic residential service from increasing beyond a \$15 basic flat rate (excluding the \$3.50 federal subscriber line charge (SLC)). The plan provides cost controls designed to limit the growth of the fund. The current funding arrangement for the OCAF plan, based on a per minute charge on all intrastate terminating toll/access minutes, would be retained for the interim. As part of the proceeding to review OCAF in 1997, the Commission would reevaluate the use of OCAF to provide support for high-cost LECs and residential rates.

Staff makes a number of arguments in support of its proposal. First, the OCAF plan is designed to shift cost recovery from toll/access to local/EAS rates and provide universal service support to LECs that cannot make the cost recovery transition. Second, the Commission has limited authority over the local rates for small LECs and none for cooperatives. Third, small LECs and cooperatives are exempted from ORS 759.050 (local exchange competition) until January 1, 1998, which coincides with the end of the OCAF plan. Fourth, while 29 out of 33 Oregon LECs are exempted from ORS 759.050, the exempt companies serve only 7 percent of the state's access lines. At the present time, PTI is the only large LEC (access lines exceeding 15,000) participating in OCAF which is subject to competition under ORS 759.050. Staff believes that, while it may be appropriate to exclude PTI from the OCAF universal service mechanism at some future time, the additional administrative cost is not worth incurring at this time.

As previously discussed, services provided by RCCs are excluded from the definition of telecommunications services by ORS 759.005(2)(g)(A). RCCs, therefore, are not covered by ORS 759.050 and are not precluded from providing service in small LEC territories.

Category 1b: Support for LECs not participating in OCAF For the large LECs which do not participate in OCAF, staff proposes that a high-cost LEC could qualify for support if its average intrastate cost per NAC for its entire service territory exceeds a predetermined benchmark after credits are taken into account due to federal universal service support, Category 2 universal service support, and contributions provided by toll and access services, directory publishing, and other vertical and miscellaneous services.

In developing the LEC's average network access line cost-estimates, embedded costs should be used, consistent with the LEC'S intrastate revenue requirement. The Category 1b support mechanism would be designed to provide incentives to minimize cost. Two such incentives are (1) limiting the universal service recovery to a percentage of intrastate costs (e.g. 80 percent) of intrastate costs above the benchmark, or (2) setting growth limits on intrastate costs (e.g. not to exceed the growth in access lines adjusted by inflation and any productivity offsets) subject to

this mechanism. The latter incentive mechanism is similar to the cost control mechanism currently in place in Category 1a support. A LEC'S receipt of Category 1b support should not be conditional upon adherence to some Commission-specified utility rate structure requirements. However, the Commission would have authority as to the method used to provide universal service support to the LEC'S customers. Funding for the large LECs eligible for Category 1b support would be incorporated into the collection mechanism proposed by staff, described below.

Summary of Party Comments

There is general agreement among the participants in the docket that Category 1a support (OCAF) should continue as scheduled until the end of 1997. There is only limited support, however, for extending support, via Category 1b, to large non-OCAF LECs. PTI argues that the existing universal service component of OCAF is narrow, and that it should be able to avail itself of Category 1b support if it otherwise qualifies. OITA urges that small non-OCAF LECs be allowed to qualify. OCTA urges adopting standards to narrow Category 1b. Much of the opposition of the remaining parties stems from the view that Category 1b is merely a safety net for incumbent LECs and would not be available to other providers such as AECs. A number of parties object to a requirement that they make payments to a plan which would distribute funds to LECs with operations in competitive zones. In addition, because support would be based on revenue requirement, Category 1b is criticized as a continuation of old subsidy thinking which is inconsistent with the move toward cost-based pricing. USWC and GTE question whether any company would actually qualify under the parameters set out by staff.

Sprint and MCI propose alternatives, both of which depart from revenue requirement based calculation of support. Both proposals calculate the universal service support amount based on the difference between a reasonable rate and the total service long-run incremental (TSLRIC) of basic service. MCI would base the reasonable amount on a nationwide average, while Sprint would have the Commission set the rate.

Discussion

Staff and all parties agree that OCAF should continue as scheduled until the end of 1997. The more difficult issue is whether there should be additional support available, under Category 1b, if a LEC'S average cost per NAC exceeds a benchmark rate. Sprint, MCI, and others question the reliance of Category 1b on a revenue requirement approach to determine LEC cost. The alternatives proposed by MCI and Sprint, however, are essentially variations on Category 2 support. They would move the LECs away from revenue requirement cost calculation immediately. This is premature. Staff's Category 1b proposal is consistent with the fact that nearly all LECs in Oregon are still regulated on a rate of return basis. Rate of return regulation is likely to continue for some Oregon companies for the foreseeable future. Both MCI and Sprint proposals acknowledge that the TSLRIC approach might leave a shortfall which would need to be made up by supplemental support. To meet concerns about LEC costs, staff proposes cost-control incentives for companies receiving Category 1b support. From a LEC customer perspective, Category 1b mitigates the rate impact as competition takes hold in the Oregon telecommunications market. In addition, the groundwork required to develop and implement Category 1b support will be useful as the Commission reviews universal support options in two years.

Resolution. The Commission adopts Category 1 support (1a and 1b). Both categories should continue only until the end of 1997, however. Category 1b would only be available to large

LECs not participating in OCAF. The benchmark for calculating eligibility for receiving support would be developed in Phase II of this proceeding. At the end of 1997, the Commission will review the continuing need for Category 1b support to determine whether future universal service funds should be limited to Category 2 and 3 support.

Category 2 - High Cost Residential Customers Under a Deaveraged Rate Design Staff Proposal
Category 2 support is targeted at residential customers of large LECs (which do not already receive support through OCAF) who live in sparsely populated areas, are costly to serve, and receive at least basic universal service as defined above. Category 2 support would be triggered if and when the Commission orders the fully-regulated LECs to implement the deaveraged rate design.

Staff believes this category of support should be available independent of the telecommunications provider. Residential customers would qualify for support if the TSLRIC that would be incurred if service were provided through their currently regulated telecommunications provider is greater than a benchmark target of \$25 per month inclusive of the federal SLC. Given that the TSLRIC of the staff-identified dense and less-dense NACs is much less than \$25 per month, staff believes that the only NACs that would qualify for this kind of support would be sparse type NACs.

Each LEC, therefore, would have to identify the geographic areas served by its sparse-type NACs and the residential customers served by those high-cost NACs. A limit of one universal service credit per qualifying household would be available. Administrative tracking to ensure this limitation, regardless of provider, would be required via a virtual voucher mechanism monitored by an independent administrator. The level of financial support available to residential customers would equal the difference between TSLRIC for sparse-type NACs and \$25. For example, if the TSLRIC of sparse-type NACs averages around \$45 per month, the level of support would be \$20.

Summary of Party Comments

There is general support among the parties for Category 2 support. The primary difference of opinion has to do with whether distribution should be limited to the carrier of last resort. To the extent the plan allows any provider of service to receive universal service support, LECs (GTE, USWC, PTI) have a major concern about the effect of providers who are not carriers of last resort (AECs, RCCs) picking and choosing customers, receiving the universal service distribution, but not assuming any general obligation to serve.

Discussion

Category 2 support provides support targeted to customers who would face unreasonably high local rates because of the cost of their NAC. This support would only be implemented, however, if the Commission were to order deaveraging on the part of the fully regulated LECs. The most likely recipients would be those customers who are served by so-called sparse-type NACs. This is the only category of NAC currently expected to exceed the benchmark rate of \$25 proposed by staff.

As noted, the chief concern raised in the comments was the fact that staff proposes that this support would be available to all providers. The LECs argue that this would enable AECs or other providers to receive support for providing service selectively to their desirable customers without undertaking the cost of carrier of last resort obligations. The Commission is not persuaded that this concern is warranted. The customers targeted for Category 2 support are by definition located in less populated areas which are costly to serve. Only residential customers would qualify. The degree to which AECs or others will seek out this particular market in the near term would seem limited at best.

Resolution. The Commission will adopt Category 2 support as proposed by staff. This aspect of the distribution mechanism will provide a means of mitigating the significant rate increases which some customers could incur if deaveraging is implemented. The support should be available regardless of provider. The Commission's authority to provide support to customers of providers other than LECs is discussed above. The LEC's concern that this mechanism makes them subject to cherry picking of the most desirable customers by competitors, is substantially mitigated by the fact that Category 2 support relates only to residential customers served by high-cost NACs.

Moreover, deaveraging, if it occurs, will result from a Commission decision in UM 351. At this point, it is not clear whether the parties will recommend deaveraging in the near term.

Category 3 - Support to Low-Income Residential Customers

Staff Proposal

Under staff's proposal, Category 3 universal service support would be targeted to low-income customers statewide. Staff points out that the first two categories of support may not be sufficient to make the telecommunications services covered by the universal service definition available to low-income customers. If basic residential service still costs \$25 per month after the first two categories of support are applied, staff's position is that this is too high for low-income customers.

The third category of support would be a universal credit on the customers bill which would be targeted specifically at low-income residential customers. A customer would qualify for only one credit, regardless of the number of lines purchased. For customers also eligible for Category 2 support, the two categories of support would have to be applied to the same provider.

Staff recommends that the initial maximum monthly charge net of credits should be \$11.50 for basic services as defined in this order. The level is based on a benchmark local exchange rate of \$15.00, which the Commission established for OCAF in Order No. 93-1133, less the \$3.50 per month intrastate OTAP credit. The maximum charge would be subject to periodic review by the Commission, and adjustment if necessary. The low income credit would supplement the existing OTAP, which provides a local service rate reduction of \$3.50 per month for qualified low-income customers. This matches the FCC Subscriber Line Charge waiver, which also amounts to a \$3.50 waiver, for a total reduction of \$7.00. OTAP is currently limited to customers of LECs and cooperatives. Funds to operate the OTAP and to provide the match for SLC waivers, as well as the TDAP and OTRS programs, are obtained by means of a \$0.25 per line surcharge currently assessed on the customers of LECs, cooperatives, AECs and cellular companies.

Staff recommends that Category 3 supplemental funding be funded using the same funding mechanism proposed for Category 2. In general, the size of the supplemental low-income credit equal the difference between \$11.50 and the rate for basic residential service, less the state OTAP credit, \$3.50 and any high-cost residential NAC credit received under Category 2 support.

Staff provides the following illustration:

TSLRIC sparse NAC \$45.00

Commission approved residential rate 41.50

Federal SLC 3.50

Total residential rate to cover cost 45.00

Subtract:

Category 2 high-cost NAC credit 20.00

Federal SLC waiver 3.50

State OTAP (statutory) 3.50

Balance 18.00

Subtract:

Benchmark low-income rate 11.50

Supplemental Category 3 support 6.50

If a provider were to charge more or less than TSLRIC, the Category 3 supplemental low-income support would be increased or decreased accordingly. For customers of competitive AECs, the supplemental low-income credit would be \$10.00 in the above example. The additional \$3.50 reflects the fact that competitive providers are not required to charge the federal SLC and currently do not participate in OTAP.

Summary of Party Comments

Overall, there is general agreement with staff's Category 3 support proposal, although McCaw takes the position that supplementing OTAP may be premature at this time, in light of the recent increase approved by the legislature.

Discussion

There is an issue as to whether, by setting a maximum access line surcharge for the OTAP program by statute, the Oregon legislature precluded any broader Commission action to assist low-income customers, such as the Category 3 plan here. Staff briefed the issue, concluding that the Commission had the necessary authority. First, the original 1987 statutory provisions indicate that the legislature did not intend the OTAP funding mechanism to be the sole means to finance universal service. Although the 1987 Act specifically states that the maximum access line surcharge is the most that can be assessed, the restriction relates only to the surcharge to support the OTAP program created by that specific legislation. The legislature did not repeal the generic funding mechanism already in existence and based on separate authority in ORS 759.030(9). In enacting the OTAP legislation, therefore, the legislature intended to supplement, not supersede, the existing universal service provisions. Second, section 4 of the 1987 Act authorizes the Commission to approve differential rates for low income ratepayers to help carry out the state's universal policy goals. The legislative history of that provision shows that the legislature did not intend the differential rate authorization to be limited to merely OTAP. In separate testimony before both houses, Representative Eachus, chair of the House Telecommunications Subcommittee to the House Environment and Energy Committee, indicated that the differential rate language would allow the Commission to operate a low income program separate from that funded by the OTAP access line surcharge. For these reasons it is reasonable to conclude that the Commission's authority under ORS 759.030(9) is not restricted by the funding limits found in the statutory OTAP program and that the Commission has current authority to expand low income support as proposed by staff.

Resolution. For the reasons discussed above in the description of the proposal, the Commission adopts the Category 3 support proposal.

DURATION OF UNIVERSAL SERVICE PLAN

The Commission will conduct a review of the universal service approach adopted in this order in two years. The review will coincide with the expiration of the OCAF Plan at the end of 1997 and the determination of additional issues in that docket. The review also will occur after the 1997 legislature has decided whether to extend the life of chapter 290, Oregon Laws 1987, including the low income differential rates authorization and OTAP. Adoption of this two year review period will allow the Commission to amend or supplement the universal service plan to take into account new developments in technology, competition, and in the federal treatment of universal service.

ORDER

IT IS ORDERED that:

1. The universal service plan set forth in this order is adopted.
2. This docket shall proceed to Phase II for a determination of implementation issues related to the universal service plan.
3. The Commission will review its universal service plan during 1997 to coincide with the review arising from the expiration of the OCAF plan.

Made, entered, and effective _____.

Roger Hamilton
Chairman

Ron Eachus
Commissioner

Joan H. Smith
Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-14-095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-13-070(2)(a). A party may appeal this order to a court pursuant to ORS 756.580.

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Telephone Utilities of Oregon, Inc., and Telephone Utilities of Eastern Oregon, Inc., do business as PTI.

McCaw Cellular Communications, Inc., is a wholly-owned subsidiary of AT&T Corp., and filed its comments on behalf of its subsidiaries, Interstate Mobile phone Company, Salem Cellular Telephone Company, Medford Cellular Telephone Company, Inc., Eugene Cellular Telephone Company, Inc., Crystal Communications Systems, and RSA 698 Cellular, Inc., each doing business as AT&T Wireless Services.

Directory assistance has been designated an essential service in OAR 860-32-200. See Order No. 88-1522 at 15. No changes are recommended for the Lifeline Assistance (LA), TDAP, and OTRS programs.

Oregon Universal Service Fund

Dense, less-dense, sparse network access channels (NACs) are classifications under discussion in UM 351.

The Commission acknowledges that section 4 of chapter 290, Oregon Laws 1987, along with the specific programs prescribed in the 1987 Act are scheduled to sunset on January 1, 1998. Section 16, chapter 290, Oregon Laws 1987, as amended.

ORDER NO.

Transmitted by linda.martin@state.or.us on Thu Mar 14 14:11:13 1996

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