

Testimony of
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Kansas Corporation Commission

Before the Senate Utilities Committee
Regarding Amended HB 2201
March 12, 2013

Chairman Apple and Committee Members:

My name is Christine Aarnes and I am the Kansas Corporation Commission's Chief of Telecommunications. Thank you for allowing me to appear before you this morning on behalf of the staff of the Commission.

Amended HB 2201 is comprehensive and touches numerous elements of the highly complex Kansas telecommunications statutes. Staff notes that the Commission has been working on the following Dockets addressing numerous issues related to the proposed bill: Docket Nos. 11-GIMT-420-GIT, 12-GIMT-170-GIT and 13-GIMT-260-GIT.¹

The Commission staff appreciates the hard work that has gone into drafting the proposed bill and notes that the bill contains many positive aspects, such as the elimination of the filing of tariffs for telecommunications carriers and electing carriers, changes to distributions from the Kansas Universal Service Fund (KUSF)², and the creation of a telecommunications study committee.

The Commission staff is neutral on Amended HB 2201 and appreciates the opportunity to share staff's technical analysis of the proposed changes and potential impacts. My testimony will address various elements of the bill and provide recommendations for the Committee's consideration.

Proposed Legislation - Amended HB 2201

Establishment of a Telecommunications Study Committee

New Section 1 (pp. 1-2)

The proposed legislation creates a telecommunications study committee to study telecommunications issues. The first meeting shall commence following the conclusion

¹ Docket No. 11-GIMT-420-GIT is stayed pending the adoption of a high-cost model at the FCC. Briefs and/or Comments have been filed by the parties in Docket Nos. 12-GIMT-170-GIT and 13-GIMT-260-GIT and orders are pending before the Commission. The Commission also has pending litigation regarding the FCC's Mega Order before the 10th Circuit Court of Appeals.

² The specific KUSF funding obligations are provided in Attachment 1 attached hereto.

of the 2013 regular session of the Kansas Legislature, and the committee shall have the authority to meet until the section expires on June 30, 2016. Commission staff supports the creation of the telecommunications study committee and believes it will be beneficial to the state of Kansas. Commission staff would welcome the opportunity to provide topics for study, if the committee requests.

Consumer Protection

K.S.A. 66-1,188, 66-1,191, 66-1,195 & 66-2005(w) (pp. 4,5 & 19)

Under the proposed legislation, pursuant to K.S.A. 66-1,188, the Commission's jurisdiction, control, and supervision over electing carriers and telecommunications carriers is limited to the provisions in new subsections (y) and (z) of K.S.A. 66-2005, and amendments thereto. Under the modifications to K.S.A. 66-1,191 and 66-1,195, the Commission would no longer investigate: rates, rules and regulations, neglect or violations of state laws, and electing carriers and telecommunications carriers with reference to public safety and convenience. Under the K.S.A. 66-2005(w), as proposed, the Commission would no longer oversee telecommunications carriers to prevent fraud and other practices harmful to consumers and to ensure compliance with quality of service standards adopted for all local exchange carriers and telecommunications carriers in the state.

In addition, it appears to staff that the Commission would not have authority to assert authority over consumer complaints concerning telecommunications carriers and electing carriers, but would continue to receive complaints regarding local exchange carriers. The Commission's Public Affairs and Consumer Protection department handled 1,121 complaints related to telecommunications during the 2012 fiscal year, resulting in \$54,707 in consumer adjustments. Commission staff suggests the Committee consider where these issues and complaints would be addressed – locally at the Kansas Attorney General's Office, or perhaps only at the FCC – and, if locally, whether the Kansas Attorney General's Office has the resources to handle the additional workload.

Kansas Lifeline Service Program

New K.S.A. 66-2006(d) (p. 23)

The proposed new subsection provides that telecommunications carriers and electing carriers may cease participation in the Kansas Lifeline Service Program at any time upon provision of 90-days prior written notification to the Commission.

Pursuant to K.S.A. 66-2009(a), the Commission was required, on or before January 1, 1997, to establish the Kansas Lifeline Service Program to promote the provision of universal service to persons with low income and to maintain affordable rates for residential local exchange service. The Lifeline program provides a discount on low-income consumers' local telephone bill.

In order to ensure low-income consumers have access to an alternative Lifeline provider, the Commission staff suggests language be included in the proposed legislation similar to

that included in 47 U.S.C. § 214(e)(4). Commission staff suggests the language allow an electing carrier or telecommunications carrier to discontinue providing Lifeline service as long as that exchange is served by at least one other Lifeline provider.

Access Revenue Recovery from the KUSF
K.S.A. 66-2005(c)(1) (p. 9)

The proposed language indicates “any reduction of a rural telephone company’s cost recovery due to reduction of its intrastate access revenue, except such revenue recovered from another support mechanism, shall be recovered from the KUSF.” This provision appears to fail to consider the fact that rural carriers’ intrastate access revenues have been declining every year due to declining long distance minutes of use, and that the FCC has declared that states are *not* left with responsibility for recovering intrastate access revenues that are reduced by intercarrier compensation reform.

As part of its reform efforts, the FCC is transitioning to a bill-and-keep regime for intercarrier compensation by gradually reducing the carriers’ terminating intercarrier compensation rates (reducing the monies received from and paid to other carriers), while providing the carriers with other revenue recovery mechanisms. The FCC stated that its recovery mechanisms will provide carriers with recovery for reductions to eligible interstate *and* intrastate revenue. As a result, states will not be required to bear the burden of establishing and funding state recovery mechanisms for intrastate access reductions.³ The FCC predicted that this recovery mechanism will be more than sufficient to provide carriers reasonable recovery for regulated services. Nevertheless, as an added measure of protection, the FCC provided for a “Total Cost and Earnings Review” process “to allow individual carriers to demonstrate that ... additional recovery is needed to prevent a taking.”⁴

The Commission has an open proceeding, Docket No. 12-GIMT-170-GIT, in which it is investigating the most appropriate approach (and whether) to compensate rural telephone companies for terminating access revenue reductions, while taking into consideration all relevant factors, including declining intrastate intercarrier compensation revenues and the FCC’s Total Cost and Earnings Review process, rather than automatically requiring the KUSF to provide revenue-neutral recovery that, according to aggregated data provided by the rural telephone companies, could amount to an additional \$1 million funding obligation being forced upon the KUSF.

Commission staff suggests “*shall* be recovered” be changed to “*may* be recovered” to avoid any potential conflict with the FCC’s Orders and 47 U.S.C. § 254(f). This very issue has been briefed and a decision is pending before the Commission.

³ FCC Mega Order, ¶¶ 795, 851.

⁴ Id. at ¶ 924.

KUSF Cap for Price Cap Carriers
New K.S.A. 66-2008(c)(1)(2) and (3) and 66-2008(d) (pp. 25-26)

Pursuant to the bill, beginning January 1, 2014, the high-cost KUSF support for local exchange carriers subject to price cap regulation will be as follows:

- high-cost KUSF support is capped at 90% of the high-cost KUSF support the carrier received for the 12-month period ending February 28, 2013;
- the carrier shall not receive high-cost KUSF support for any residential or business lines within an exchange for which it has been granted price deregulation, except for areas within any census block in such an exchange in which there is no wireline carrier providing local exchange access lines that does not receive KUSF high-cost support;
- the carrier shall receive the same per line, per month KUSF support as established in the price cap model proceedings, except the amount shall be reduced by any funding received by such carrier from the FCC's Connect America Fund (CAF) Phase II; and
- the Commission is required to review the capped amount of high-cost KUSF support and determine if a lesser amount is appropriate for KUSF distributions made after March 1, 2019.

These provisions currently affect only CenturyLink. Under the proposed language, CenturyLink would not receive high-cost KUSF support if it avails itself to the price deregulation provisions in the statute and the language reduces CenturyLink's support by the amount of CAF Phase II support the carrier receives. The FCC is in the process of adopting the CAF Phase II support model; therefore, it is currently unknown how much CAF Phase II support CenturyLink may be eligible to receive for Kansas and whether CenturyLink will accept the CAF Phase II support and the obligations that come along with accepting such support.

CenturyLink's KUSF support for the year ended February 28, 2013 was \$13.3 million and its KUSF support declined to \$11.0 million on March 1, 2013. The \$11.0 million consists of \$9.5 million of cost-based KUSF support as determined by the high-cost model and \$1.5 million of revenue-neutral support the Company recovers due to reducing its intrastate access rates to interstate levels.

The proposed legislation caps CenturyLink's KUSF support at 90% of the support it received as of February 28, 2013, or \$11.95 million – approximately \$950,000 more than it began receiving on March 1, 2013. The proposed cap would prevent CenturyLink from receiving KUSF support above the cap, should CenturyLink seek high-cost KUSF support to compensate for reduced federal support if CenturyLink elects not to receive CAF Phase II support.

CenturyLink has assured the Commission staff that the proposed legislation merely caps CenturyLink's support and would not increase CenturyLink's high-cost KUSF support or

preclude the Commission from reducing CenturyLink's support due to line losses or changes to CenturyLink's revenue-neutral KUSF support as a result of reducing its access rates to parity.

Elimination of KUSF Support for Electing Carriers
New K.S.A. 66-2008(c)(5) (p. 26)

Beginning January 1, 2014, electing carriers would no longer be eligible to receive high-cost KUSF support. This provision would only affect AT&T, and would result in a reduction of approximately \$5.2 million from the KUSF.

Phase Down of Competitive ETC Support
New K.S.A. 66-2008(c)(4) (pp. 25-26)

As proposed, the high-cost KUSF support received by Competitive ETCs would be capped as of March 1, 2013, and beginning March 1, 2014, the carriers' high-cost KUSF support would be phased down in four equal installments. Competitive ETCs currently receive approximately \$11.2 million in high-cost KUSF support. Competitive ETCs' support would be reduced by approximately \$2.2 million on January 1, 2014, when the support the carriers received for serving in the AT&T service areas is eliminated. Beginning March 1, 2014, the Competitive ETCs' support would be reduced by approximately \$2.25 million each year for four years.

Commission Authority to Modify KUSF
New K.S.A. 66-2008(d) (p. 26)

As proposed, the current K.S.A. 66-2008(c) would become K.S.A. 66-2008(d) and the language currently included in K.S.A. 66-2008(c) would be eliminated. The current language in K.S.A. 66-2008(c) provides that "[t]he commission shall periodically review the KUSF to determine if the costs of qualified telecommunications public utilities, telecommunications carriers and wireless telecommunications service providers to provide local service justify modification of the KUSF. If the commission determines that any changes are needed, the commission shall modify the KUSF accordingly." Removing this language may require the Commission to rely on several other statutes that are less clear to accomplish needed modifications to the KUSF.

If the goal was to remove language affecting telecommunications carriers, wireless telecommunications service providers and electing carriers, the Commission staff recommends the language be modified to reflect as such, but not remove the existing language.

Supplemental KUSF Funding
New K.S.A. 66-2008(e) (pp. 26-27)

This subsection provides that any local exchange carrier may request supplemental funding from the KUSF based on a percentage increase in access lines over the 12-month

period prior to the request, and additional funding may be requested for: the recovery of shortfalls due to additional rebalancing of rates to continue maintenance of parity with interstate access rates; shortfalls due to changes to access revenue requirements resulting from changes in federal rules; additional investment required to provide universal service and enhanced universal service; and for infrastructure expenditures in response to facility or service requirements established by any legislative, regulatory or judicial authority. Such requests shall be subjected to simplified filing procedures and the Commission shall issue an order on such request within 120 days of such filing.

The bill eliminates the references in the current statute to qualified telecommunications carriers, telecommunications public utilities and wireless telecommunications service providers so as not to conflict with the provision in the new K.S.A. 66-2008(c)(4) that caps and phases down Competitive ETC support. The subsection was further modified to explicitly state that local exchange carriers can request supplemental KUSF funding. This provision conflicts with both current and proposed statutes and likely trumps current case law.

The current subsection that allows for supplemental KUSF requests has been applicable only to Competitive ETCs, AT&T, and CenturyLink. This subsection has not been applicable to rate-of-return local exchange carriers since the Kansas Court of Appeals determined in *Bluestem Telephone Co. v. Kansas Corporation Commission* that because K.S.A. 66-2008(e) states that for each local exchange carrier electing traditional rate of return regulation, all KUSF support, including any adjustment thereto pursuant to this section shall be based on such carrier's embedded costs, revenue requirements, investments and expenses. Thus, it was determined that the Commission cannot and should not provide rate-of-return regulated carriers with supplemental KUSF support because the support would not be based on the carriers' embedded costs, revenue requirements, investments and expenses.

The only local exchange carrier, by statutory definition, that hasn't elected rate-of-return regulation is CenturyLink, which has elected price cap regulation. As discussed in depth above, the bill sets out specific guidelines for CenturyLink's support, which would be at odds with this subsection of the statute.

New K.S.A. 66-2008(e) conflicts with multiple facets of the bill and current statutes, and would provide rate-of-return carriers with an avenue to receive additional KUSF support without a full review of the carriers' embedded costs, revenue requirements, investments and expenses. Commission staff suggests this subsection be stricken in its entirety.

Commission Authority to Implement FCC Reforms
New K.S.A. 66-2008(f) (p. 27)

The proposed language states that until at least March 1, 2017, any modification of KUSF support for local exchange carriers electing rate-of-return regulation shall be made only as a direct result of changes in the carrier's embedded costs, revenue requirements, investments and expenses.

Current statute provides for high-cost KUSF support for rate-of-return regulated carriers to be based on the carrier's embedded costs, revenue requirements, investments and expenses; therefore, it appears unnecessary to reiterate this and further limit changes in support to only those that are the direct result of changes to the carrier's embedded costs, revenue requirements, investments and expenses.

The Commission is in the process of reviewing the KUSF and policies related to the KUSF in Docket Numbers 12-GIMT-170-GIT and 13-GIMT-260-GIT. The issues that are being investigated include policies related to implementation of the FCC's reforms that were adopted in its November 18, 2011 Order. The proposed language may limit the Commission's ability to implement policies related to the FCC's reforms.

According to estimates provided by the rural local exchange carriers of the potential impact of the FCC reforms, this could potentially push \$8 million to the KUSF for recovery in 2013 alone and an additional \$16 million for 2014. This provision could potentially negate any KUSF reduction achieved as a result of other provisions of the bill.

Commission staff suggests the new language be modified or deleted to allow the Commission to continue its current investigations into the KUSF, including modifying KUSF support as a result of implementing the FCC's reforms.

Timeframes for KUSF Audits
New K.S.A. 66-2008(g) (pp. 27-28)

This proposal specifies that any request for additional KUSF support and any audit of a rural telephone company to determine its cost-based KUSF support will be subject to the 240-day period that is applied to rate cases pursuant to K.S.A. 66-117.

The reference to K.S.A. 66-117 is confusing. K.S.A. 66-117 contains additional explicit timeframes in addition to the 240-day deadline, including a requirement that an Application be suspended within 30 days or the proposed rate shall be deemed approved by the Commission and shall take effect on the proposed effective date.

Staff recommends the proposed language be modified by either removing the reference to K.S.A. 66-117 or clarifying that such filings shall be subject to the deadlines for rate case applications pursuant to K.S.A. 66-117.

Carrier of Last Resort
K.S.A. 66-2009(a) (p. 28)

The proposed language eliminates the Carrier of Last Resort (COLR) requirement for electing carriers. This provision is applicable to only AT&T. The elimination of the COLR requirement is not problematic in areas where there are competitors, but that may not be the case in all 134 exchanges served by AT&T.

AT&T achieved price deregulation in 59 exchanges pursuant to K.S.A. 66-2005(q)(1)(B)(C) and (D). K.S.A. 66-2005(q)(1)(C) and (D) requires the requesting carrier to demonstrate that there are two or more nonaffiliated telecommunications carriers or other entities, that are nonaffiliated with the local exchange carrier, providing local telecommunications service to business or residential customers. One of the nonaffiliated carriers or entities is required to be a facilities-based carrier or entity and not more than one of such nonaffiliated carriers or entities may be a provider of commercial mobile radio services in that exchange.

The remaining 75 AT&T exchanges were price deregulated as a result of the passage of Senate Bill 72 in 2011. Therefore, the demonstration of competitors was not required for these 75 smaller, more rural AT&T exchanges.

Pursuant to 47 U.S.C. § 214(e)(4), an eligible telecommunications carrier cannot exit a market unless there is at least one other provider in the area to serve the customers. To ensure that all Kansas customers have access to telecommunications services, staff suggests you consider inclusion of similar language in the proposed bill.

Conclusion

The Commission staff appreciates the hard work and collaboration that went into the proposed revisions to the Kansas telecommunications statutes and the opportunity to speak to the Committee today about Amended HB 2201.

Thank you for your consideration of these comments. I am available for questions at the appropriate time.

**Commission Staff Testimony - Amended HB 2201
Attachment 1**

<u>KUSF Obligations:</u>	KUSF Year 17 (3/1/13 - 2/28/14)	% of KUSF	Portion of 6.42% KUSF Assessment
Rural LECs	\$26,239,286	41.73%	2.68%
Southwestern Bell Telephone Company d/b/a AT&T Kansas	\$5,239,381	8.33%	0.54%
United-Kansas d/b/a CenturyLink	\$11,060,508	17.59%	1.13%
Competitive ETCs	\$11,205,322	17.82%	1.14%
Kansas Relay Service Inc. (KRSI)	\$869,297	1.38%	0.09%
Telecommunications Access Program (TAP)	\$635,948	1.01%	0.06%
Lifeline	\$4,657,579	7.41%	0.48%
Kan-Ed	\$1,249,968	1.99%	0.13%
Administration and Audits (GVNW, carrier audits, and third-party audits)	\$422,869	0.67%	0.04%
Gross KUSF Obligations	\$61,580,159		
Less: Projected Year 16 Ending	-\$3,085,579	-4.91%	-0.32%
Adjusted KUSF Obligations	\$58,494,580		
Plus: Contingency Allowance	\$4,387,094	6.98%	0.45%
Net KUSF To Collect	\$62,881,674	100.00%	6.42%
Total Assessable Revenues	\$978,937,291	6.42%	

* Information from Direct Testimony of Sandra K. Reams in Docket No. 13-GIMT-130-GIT, Exhibit SKR-1.