BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of the Application of the Nebraska Public Service Commission, on its own motion, to conduct an investigation into intrastate access charge reform.	))))))	Application No. C-1628 PRELIMINARY FINDINGS AND CONCLUSIONS Entered: October 2, 1998

BY THE COMMISSION:

On September 15, 1997, the Commission opened this docket for the purpose of investigating the structure of intrastate access charges and establishing a Nebraska state universal service fund (NUSF). Public notice of this docket was published in the Daily Record, Omaha, Nebraska, on September 17, 1997. All certificated interexchange and local exchange carriers were named as parties in this matter. Formal interventions were filed by the Nebraska Independent Telephone Association and the Nebraska Telephone Association.

After receiving comments from interested parties and reviewing the Nebraska Universal Service Task Force Initial Report dated July 1997, the Commission issued a prehearing conference order and requested further substantive comments and reply comments. Such comments have been received and have been given careful study by the Commission.

On May 22, 1998, a petition was filed with the Nebraska Secretary of State (the Initiative 414 Petition) seeking certification to place a measure on the November ballot which would generally require the Commission to (a) eliminate implicit subsidies contained in access charges as of the effective date of the statutory amendment set forth in the Petition; (b) establish access charges based on forward-looking economic costs; (c) develop competition in the access services marketplace; (d) adopt rules and regulations requiring incumbent local exchange carriers to provide access services on a cost-based, competitively-neutral and nondiscriminatory basis; (e) establish and maintain a filing system for tariffs by providers of access; and (f) average prices in the aggregate for intrastate long-distance services to reflect the reduction of access charges applicable to such long-distance services. The Petition, now known as Initiative 414, if approved by the voters of Nebraska, would have a significant effect on this docket, including the potential need to implement NUSF support immediately after the potential effective date of the Petition.

A further development impacts this docket. On July 17, 1998, the Federal Communications Commission (FCC) entered an order effectively delaying the implementation of the Federal universal service fund for non-rural local exchange carriers until July 1, 1999 (the FCC Order).

Based upon the foregoing developments, on August 11, 1998, the Commission entered Progression Order No. 2 in this docket and requested further comments from interested parties with regard to the impact of possible approval of the Petition and the impact of the FCC Order. The Commission received such comments on September 15, 1998, and has reviewed them.

Based upon (a) the comments submitted to the Commission in this docket; (b) the provisions of the Telecommunications Act of 1996 (the Act); (c) the mandate to continue and enhance universal service as required by Section 254 of the Act; (d) the provisions of the Nebraska Universal Service Act; (e) the recommendation of the Nebraska Universal Service Task Force; and (f) consideration of the requirements of the Petition and the FCC Order, the Commission issues the following Preliminary Conclusions and Findings which will be the subject of a full hearing before the Commission beginning on October 27, 1998.

PRELIMINARY FINDINGS AND CONCLUSIONS

The concept of universal service is not new. In the past, universal service has been funded by a conscious policy of pricing certain incumbent local exchange carriers (ILEC) services above cost, such as access service, toll service and local business service. The "implicit subsidies" contained in these charges are and have been used to keep local residential exchange service rates well below actual cost in order to maintain affordable local rates for all subscribers. This policy was adopted by both federal and state regulators and implemented by the telecommunications industry.

Due to the opening of ILEC markets to competition, this practice can no longer continue. As a result, the rates for services priced above costs should be reduced to reflect actual costs. The lost subsidies should, over a reasonable period of time, be replaced (a) through increases in rates for services priced below cost and (b) from state and federal universal service funds.

The Commission has been investigating the need for lowering access rates and creating a state universal service fund for some time. In early 1996, the Commission opened Docket C-1176, which established a Nebraska Universal Task Force to compile public comment and to develop a plan for the implementation of a NUSF. The Task Force concluded, and the Commission agrees, that quality services should be made available at just, reasonable and affordable rates to consumers in all regions of Nebraska, including low-income consumers and those in rural, insular and high-cost areas, and that such services should be comparable to those services provided in urban areas and at rates that are reasonably comparable to urban rates.

This Commission is the proper regulatory body to determine the level of support needed by Nebraska subscribers. The Commission finds that the NUSF should support service for all customer access lines whether business or residential. However, initially the Commission believes different benchmarks for residential and business service are appropriate. The Commission agrees with the analysis provided by the USF Task Force and at the outset, selects $22 per month as the residential affordability benchmark, which includes surcharges such as the federal subscriber line charge, the 911 surcharge, the relay surcharge, etc. While the

Commission has little evidence before it regarding the appropriate benchmark for business service, we find at this time, that $33 should be utilized for the purpose of determining USF funding needs. The current supported services should consist of: single-party service; touch-tone; standard "white page" (or alpha directory) listing; access to directory assistance; access to interexchange services; access to emergency services such as 911 or E911; access to operator services; toll blocking to qualifying low-income consumers; and access to advance services as defined by the Commission.

A change of this magnitude takes time and a concerted effort on behalf of all parties involved; therefore, the Commission proposes a transition period for adoption of the goals addressed in this order. Recognizing the potential effect on consumer rates, this order will first outline the end goals desired by this Commission, followed by a description of how the transition period will achieve the end result. Considering the potential impact upon consumers across the state, the Commission reserves the right to modify after notice and hearing, any and all adopted NUSF requirements at any time should the Commission deem it to be in the public's best interest.

The Commission will determine the costs to provide such local services and the benchmark above which costs will be eligible for universal service funding. Universal service costs for non-rural companies shall be developed in accordance with the Commission's recommendation to the FCC contained in Docket C-1633. The costs of service for rural companies shall be based upon embedded costs while the Commission seeks further comment relative to the appropriate cost methodology for rural companies. The Commission reserves the right to designate other services to qualify for NUSF support.

To the extent that a carrier receives federal universal service funding, such funding amounts will be subtracted from the carrier's total universal service requirement. The service area for rural and non-rural carriers shall be the carrier's certificated exchange(s). In order to qualify for the NUSF, a carrier must be a facilities-based carrier and commit to serve an entire service area that is acceptable to the Commission. Initially, the support area for all carriers shall be a census block.

A carrier must be designated an Eligible Telecommunications Carrier (ETC) to receive state universal service support. Carriers shall be designated as ETCs for non-rural service areas as long as they meet the criteria set forth in the 1996 Telecommunications Act (Act). Additional carriers other than incumbent LECs will be designated as ETCs in areas served by rural carriers only if such designation is found to be in the public interest, which shall be determined on a case-by-case basis.

The Commission will administer the NUSF. The NUSF will be sized in the following manner: (a) Develop the cost to provide local service within each census block; (b) Determine the support level within each census block by subtracting the benchmark price selected by the Commission from the cost to provide local exchange service within a census block; and (c) For each carrier, determine the census block high-cost support amounts by multiplying the census block support levels by the number of lines served by the carrier within each census block. Each carrier's high-cost support shall be the sum of its census block support amounts less any federal high-cost support received by the carrier. The total amount of the high-cost support fund for the State of Nebraska shall be the sum of each carrier's high-cost support.

The NUSF will be funded through a flat percentage surcharge on retail, end-user revenues from services provided via the public switched network. The surcharge will be assessed on all interstate and intrastate telecommunication services. This surcharge will be applied in a manner consistent with the state sales tax. This surcharge will not apply to intermediate services, such as access, that are provided to another company as long as that company collects the universal service surcharge from the retail service it provides to end-users. For example, a LEC will not levy the surcharge on access services provided to an IXC; instead the IXC will collect the surcharge on its retail toll services. This will prevent double billing of the universal service surcharge on its retail end-users. The retail services that are provided to that service provider by a LEC or other carrier will be subject to the universal service surcharge.

This surcharge will be determined by dividing the total high-cost support amount by the retail, end-user revenue subject to the universal service surcharge. This amount should be explicitly displayed on customers' bills. In order to qualify for the NUSF, a carrier shall, within its service area, provide all supported services to all subscribers. Further, a carrier shall demonstrate that implicit subsidies have been removed from access, toll and local exchange service prices and that these services are priced at actual cost. For non-rural carriers, the Commission finds that actual cost for these services shall be based upon forward-looking costs, consistent with Commission findings in Docket C-1633. While currently, the Benchmark Cost Proxy Model (BCPM) does not explicitly calculate costs for access and toll services, actual costs for such services should be developed in a manner consistent with the cost principles and inputs approved by this Commission. Rural companies may continue to use embedded costs until such time as the Commission adopts a cost methodology for rural carriers.

Generally, the state access charge structure should approximate the interstate access charge structure except for the primary interexchange carrier charge (PICC). A PICC recovers loop costs from IXCs and the Commission does not currently believe this is competitively neutral in light of interconnection requirements contained in the Act. This access structure requires that carriers implement the local transport restructure (LTR). Additionally, carriers shall bifurcate the local switching element into a per call setup element and a per minute element. This bifurcation will more accurately reflect the manner in which costs are incurred.

With regard to terminating access, the Commission finds that because toll traffic is largely billed to the originator of the toll call and carriers have little choice in terminating toll traffic, rates for this service should be set at cost. These rates shall not include access charge residuals (ACRs) or residual or transition interconnection charges (RICs or TICs) associated with the local transport restructure. The Commission tentatively adopts this same finding for originating access; however, the Commission may seek additional comment on the matter of originating access charges. Consistent with this finding, effective July 1, 1999, carriers will be required to eliminate the ACR charges from their rate structures. The RIC/TIC charges will be phased out during the transition period described later in this order. Carriers not in compliance with the Commission's findings, regarding the structure of access charges, shall not be eligible for USF support.

The Commission recognizes there may be significant shifting of revenues as well as costs that will occur under this plan and will allow carriers a period of transition. Non-rural companies will be allowed a transition period of two years and rural carriers four years. Each carrier shall file a transition plan with this Commission by March 31, 1999, for Commission approval. Said plans shall detail any and all rate adjustments during the applicable transition period. This plan shall include an annual tariff filing to be made on or before July 1 of each year during the transition period to affect the changes detailed in the carrier's transition plan. The affected carrier shall also detail the level of access, toll and local exchange service charges and the magnitude of the changes being made in its annual tariff filing each year during the transition period.

The Commission intends to give considerable weight to the fact that a company has a Commission-approved transition plan, should an access charge complaint be filed against that carrier, if the carrier has met or exceeded their commitments during the transition period. If a company has met its obligations, embedded costs will be determined based on an interim rate of return of 12 percent for purposes of interim universal service support. To the extent a carrier's earnings exceed this designated rate of return, the carrier will forfeit the corresponding amount of NUSF funding.

At the end of the transition period, the Commission expects that local residential and business services will be priced at cost or the benchmark, whichever is lower, and that access and toll services will be priced at cost. Costs for non-rural companies are forward-looking costs consistent with principles and inputs contained in Docket C-1633. Costs for rural companies will be embedded costs until such time as the Commission determines the appropriate costing methodology for rural companies. In each annual filing, companies should increase local service prices by the maximum percentage permitted by Statutes 86-803 and 75.709.01 until such time as these services are priced at cost or the benchmark, whichever is lower. Carriers not using the maximum permitted flexibility to increase rates that are below the applicable benchmark or cost, whichever is lower, will receive a reduced amount of interim universal service support.

Should Initiative 414 pass, it will apply to only three companies: US West, Aliant Communications and GTE. These companies will be required to set their access charges at forward-looking economic costs; the same level that these companies will be required to set their access charges at the end of the transition period. However, this Initiative will require these reductions in a significantly shorter time frame than the transition period contemplated by this order. To the extent the reductions result in earnings below the target level, the companies will receive appropriate interim state universal service support.

The Commission seeks further comment by October 20, 1998, from all interested parties on the following issues:

1. Should the Commission adopt benchmark costs or prices?

2. What should be the level of the benchmarks? (Please provide details of how the benchmarks should be determined.)

3. Should originating access be set at the same level as terminating access?

4. Is there any public policy benefit to be derived by authorizing originating access to be priced higher than terminating access?

5. Ultimately, should a rural carrier's costs be determined in a different manner than non- rural companies? If so, what is the appropriate methodology?

6. What should the authorized rate of return be?

7. What advanced services should be supported and at what levels?

8. Should service providers using Internet protocol contribute to Universal Service? If so, does the Commission have the authority to require them to do so? How will these providers be identified?

O R D E R

IT IS THEREFORE ORDERED by the Nebraska Public Service Commission that a copy of this order be served upon each of the parties to this docket.

IT IS FURTHER ORDERED that the public hearing on the Preliminary Findings and Conclusions set forth in this order shall commence at 9:00 a.m. on October 27, 1998, and continue as necessary through October 30, 1998.

IT IS FURTHER ORDERED that comment on the enumerated issues be filed on or before October 20, 1998, which is the date previously established for parties who will be presenting testimony at the hearing to pre-file such testimony.

MADE AND ENTERED at Lincoln, Nebraska, this 2nd day of October, 1998.

NEBRASKA PUBLIC SERVICE COMMISSION

COMMISSIONERS CONCURRING:

Chairman

ATTEST:

Executive Director