BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of the Nebraska Public Service Commission, on its own motion, seeking to establish a long-term universal service funding mechanism.	)	Application No. NUSF-26 FINDINGS AND CONCLUSIONS Entered: November 3, 2004

BY THE COMMISSION:

1. On August 21, 2001, the Nebraska Public Service Commission (Commission) initiated the above-captioned proceeding on its own motion to revise the universal service funding mechanism established in C-1628/NUSF.[1] Notice of this proceeding appeared in the Daily Record, Omaha, Nebraska, on August 24, 2001. In the course of its investigation, the Commission has requested several rounds of comments, held formal hearings, informal workshops and has made progressive findings.[2]

O P I N I O N   A N D   F I N D I N G S

Introduction

Overview of the Nebraska Universal Service Fund

2. The Commission finds, consistent with its statutory authority[3] (NUSF Act), that the three separate programs, which have evolved in the transitional period, supported by the Nebraska Universal Service Fund (Fund) and having distinct eligibility requirements should continue going forward. Those programs are:

a. The High Cost Program (Program), which is designed to ensure customers in all regions of the state, have access to telecommunications services, including

1 Application No. C-1628/NUSF, *In the Matter of the Application of the Nebraska Public Service Commission, on its own motion, seeking to conduct an investigation into intrastate access charge reform*, Findings and Conclusions (January 13, 1999) (C-1628 Order).

2 *See* generally Application No. NUSF-26, *In the Matter of the Commission, on its own motion, seeking to establish a long-term universal service funding mechanism* (NUSF-26).

3 *See* NEB. REV. STAT. §§ 86-316 to 86-329 (2002 Cum. Supp.).

interexchange services, and information services, including advanced telecommunications services, at affordable rates and at rates that are comparable between urban and rural areas.[4]

b. The Nebraska Telephone Assistance Program (NTAP), formerly known as the Nebraska Lifeline and Link-Up Program[5], which provides a reduction in rates to qualifying low-income telephone subscribers within the state.

c. The Nebraska Tele-Health (Tele-Health) Program provides support for telecommunications services to connect rural hospitals to urban hospitals in order to facilitate the provision of tele-medicine services in rural areas[6].

3. The Commission will continue to require companies to meet a unique set of eligibility requirements in order to be designated a Nebraska Eligible Telecommunications Carrier (“NETC”)[7] for each program.

4. NTAP and Tele-Health support amounts are determined by examining the rate(s) charged in absence of the Fund. In the event the rate(s) for services provided by NTAP and Nebraska Tele-Health exceed the Commission’s affordability and comparability standards, Fund support offsets a portion of the amount incurred by the customer, absent the Fund. Synonymously, the Commission finds program funding should only be provided to NETCs, for services determined by the Commission to be made universally available.

5. Current requirements for the NTAP are generally set forth in Section 6 of the Nebraska Universal Service Fund Rules and Regulations[8]. Only companies designated by the Commission as

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4 *See* NEB. REV. STAT. § 86-323(3); see also Application No. NUSF-26 Progression Order No. 2 (August 27, 2002).

5 *See* NEB. REV. STAT. § 86-329.

6 *See* NUSF-26, Progression Order No. 3 (December 17, 2002).

7 The term NETC encompasses all carriers eligible to receive high cost funding from the Program, including both incumbent and competitive service providers.

8 NEB. ADMIN. CODE, tit. 291, ch. 10, § 006.

federal ETCs are eligible to receive support from NTAP. However, the Commission has sought comment on whether it should expand the number of providers eligible to offer NTAP assistance.[9] As provided in the Commission's June 29, 2004 Order, the Commission will continue to use Docket NUSF-35 as the vehicle to examine the eligibility of telecommunications providers to receive NTAP funds.

6. The carrier eligibility requirements for Tele-Health are set forth in Docket NUSF-35.

7. High Cost Program support amounts are theoretically similar to those calculated for the NTAP and Tele-Health. The Commission finds that the Fund should continue to offset amounts in excess of the Commission's affordability and comparability standards. In this Order, the Commission adopts a method for determining Program support, which differs from that established by the Commission in Docket No. C-1628. This new method is further described below.

8. The discussion below pertains exclusively to the High Cost Program (Program).

Affordability and Comparability

9. The Commission finds affordable access to telecommunications and information services at comparable rates is key in developing a long-term universal service mechanism. Neb. Rev. Stat. § 86-317 provides in pertinent part that

> The purpose of the Nebraska Telecommunications Universal Service Fund Act is to authorize the commission to establish a funding mechanism which . . . ensures that all Nebraskans, without regard to their location, have comparable accessibility to telecommunications services at affordable rates.

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9 *See* Application No. NUSF-35/PI-69, *In the Matter of the Nebraska Public Service Commission seeking to determine Nebraska Eligible Telecommunications Carrier status for the purposes of receiving state universal service support for providing Lifeline/Link-up services and Telehealth services to rural hospitals,* Findings and Conclusions (April 29, 2003).

10. The Commission further finds access to telecommunications and information services should be affordable and comparable in rural and urban areas.[10] In order to keep local rates affordable, the NUSF should be structured in a manner that will keep the surcharge at a reasonable level and the size of the fund manageable. The Commission previously found the NUSF should not reward inefficient investment.[11] The affordability component is necessary to meet other universal service principles outlined in Neb. Rev. Stat. § 86-323 and the goals adopted by the Commission in Progression Order No. 2. In order to keep rates comparable, the Commission has used a residential access line benchmark of $17.50 during the transition period and proposes to keep that benchmark in place for residential service. The affordability and comparability principles are, in large part, the impetus behind the adopted support guidelines and allocation methodology set forth in further detail below.

11. The Commission finds the proposed methodology for the calculation of support is specific, sufficient and predictable consistent with Neb. Rev. Stat. § 86-323. The proposed methodology highly targets support to the most costly and sparsely populated out-of-town service areas where NUSF support is needed. The methodology specifically pinpoints the support areas and provides companies with a specific model for determining the amount of support available for distribution.

12. One party argued that the methodology could be unpredictable, in that a company would not be able to determine its actual monthly support amounts after Over Earnings Redistribution (OER) because it could not predict the earnings of the other NETCs. The Commission finds this argument unpersuasive. To begin with, the Commission finds the baseline support allocation is sufficient. Secondly, the OER mechanism redistributes over-earnings. The OER does not cause a company to face a reduction in their baseline support; rather, the OER has the effect of *increasing* support due to the over-earnings of other companies.[12] If companies are properly investing in their network, the Commission will not have any over-earnings dollars

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10 NUSF-26, Progression Order No. 2, ¶ 29 (d).

11 *Id.,* ¶ 38.

12 *See* the Testimony of Dr. David Rosenbaum, Transcript (TR) at 163.

to redistribute.[13] In the alternative, the Commission could have decided to redistribute the over-earnings to consumers.[14] Simply put, companies can properly account for the OER mechanism, if they plan on their reasonable baseline allocation and do not budget for the possibility that it will receive additional support due to over-earnings.[15] Moreover, the mere possibility that the amount of support over and above the companies' baseline allocation may fluctuate does not make the NUSF support mechanism unpredictable.[16] In sum, the Commission finds the Support Allocation Methodology (SAM) and the proposed transition mechanism, including the OER, are predictable consistent with § 86-323.

13. No party presented any evidence that the proposed methodology would be insufficient. A couple of the parties argued that the Commission should take consideration of unique circumstances of their companies position and costs. These carriers requested the Commission consider switching or transport costs. However, this position is inconsistent with the Commission's proposal to support only the loop. Further, should the Commission consider supporting other elements or unique circumstances of one or more companies, such an approach would be inequitable and would lead the Commission down a slippery slope of determining which unique circumstance has the most merit. Moreover, as the Commission staff testified, although there were a couple of parties who complained about the sufficiency in regards to their unique circumstances, the majority of the parties had no comments relative to sufficiency and no complaints with the proposed methodology in that regard. The Commission finds that the proposed methodology is specific and sufficient consistent with Neb. Rev. Stat. § 86-323.

14. The Commission further finds the proposed methodology is competitively neutral. The Commission staff gave its interpretation relative to what competitive neutrality requires of the Commission.[17] The Commission finds that section 214(e) of the federal Act does not apply to state universal service funding mechanisms, however, it gives the Commission guidance to congressional intent in defining competitive neutrality. Section 214(e), which addresses ETC designation, gives guidance

13 *Id*.
14 *Id*.
15 *See* TR at 256.
16 *Id.*
17 *See* Testimony of Jeffrey Pursley, TR at 39-40.

as to what Congress intended by the phrase competitive neutrality in the context of universal service. No other party convincingly countered the Commission staff's interpretation. In this order, the Commission adopts a mechanism, which would initially support a single network, with the exception of competition over UNEs.

15. Based on the Commission staff's economic study, the Commission's current policy perspective is that public interest would be adversely affected if the NUSF were to support more than one network in the remote rural areas where support is being targeted. However, the Commission finds an applicant can petition the Commission to designate it as the supported network provider in lieu of the current designated provider in a service area or, in the alternative, can choose to rebut the presumption that the NUSF cannot, consistent with public interest, support more than one network by providing clear and convincing evidence. Relevant factors the Commission will consider are the cost to provide service and the cost to the NUSF. Another important factor should be the amount of support analysis shows is needed in the area. In addition, benefits to consumers, new services provided in un-served areas, the quality of service, compliance with existing interconnection agreements, and the ability of the provider to provide service to everyone on their own network are all factors the Commission will consider.

16. Contrary to the claims of some commenters,[18] the single network proposal does not disqualify CMRS carriers, or any other competitive carrier, from receiving support. The Commission believes that Sprint, Viaero and DFS do not have a complete understanding of the proposal released by the Commission and supported by staff at the hearing. In its review, the Commission balanced the costs and benefits of designating an alternative provider or supporting an additional provider in the sparsely populated out of town areas where support is targeted and gives a great amount of weight to Dr. Rosenbaum's testimony in this regard. Should the Commission receive a petition for support from a prospective competitive carrier to either be the supported network or, in the alternative, to be an additional supported network, the Commission will consider the factors raised by the Commission staff in this proceeding and any other

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18 *See generally* the late-filed comments of Dark Fiber Solutions, LLC (DFS), NE Colorado Cellular Inc. d/b/a Viaero Wireless (Viaero) filed August 13, 2004 and the Sprint Post-Hearing Brief filed September 30, 2004.

relevant factors. Finally, the Commission staff is correct that the proposal to initially support the ILEC network stems from the fact that no other facilities based provider (other than providers leasing UNEs) has sought to be eligible to draw support from the NUSF.[19]

17. While the NUSF is not bound by section 214(e) of the Act, the Commission will look to that section for guidance in determining the meaning of competitive neutrality. The Commission has adopted and will continue to utilize a public interest test to determine competitive neutrality. The mechanism does not exclude any particular carrier and provides a specific mechanism for an alternative or an additional carrier to petition the Commission. As it stands, there are clear mechanisms for CMRS carriers and other competitive carriers to petition the Commission for state support. Accordingly, the Commission finds that its proposal is competitively neutral, consistent with section 254, and necessary to preserve and advance universal service principles in Nebraska.

Scope of Support

18. To achieve a balance between competition, i.e. multiple networks, and universal service, the Commission finds the proposed methodology highly targets Program support to a supported network(s) within a defined area. Based on the methodology presented, the Commission finds many lower-cost parts of the state do not require Program support, specifically, areas where competition would most logically develop, such as the communities of Omaha and Lincoln. Under the methodology the Commission adopts today, only fifteen percent (15%) of the total households in the state will be eligible for Program support.

19. The Commission finds that all carriers currently designated as an NETC will retain this designation, but only for those supports areas for which they are already designated, irrespective of whether the NETC actually received support during the transition period, unless the Commission designates otherwise at a later date. Attached is Appendix A, detailing all NETC carriers and their respective support areas. Other carriers may petition the Commission to change this designation subject to the necessary criteria discussed herein.

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19 *See* Commission Staff’s Post-Hearing Brief at 6.

20. The Commission continues to believe Fund Program support should not be provided to services provisioned through resale. However, it does propose eligible services, provided via UNE-Loop[20], be eligible to receive support.

Porting Support to Competitive NETC's

21. The Commission adopts the staff's proposal relative to porting support to competitive NETCs providing service by leasing UNEs from the ILEC. The Commission finds that adopting Proposal Number One as modified by the staff adequately addresses the concerns raised by the parties in this proceeding.[21]

22. The Commission's June 29, 2004 Progression Order requested comments on two proposals for the porting of support to competitive NETCs providing service by leasing UNEs from the underlying incumbent carrier. The first proposal was to continue the process of porting support to competing NETCs using program support averaged in the same manner as de-averaged UNE loop rates in the respective support area.

23. In the second proposal, the Commission would have implemented a structure where the ILEC would charge the Competitive NETC provider the rate for the lowest priced zone, regardless of the actual zone in which the Competitive NETC is providing service. The ILEC would then keep any Program support, which would have otherwise been given to the Competitive NETC.

24. The Commission staff offered a third proposal in its prefiled direct testimony and at the hearing, which was a combination of proposals One and Two. In its post-hearing brief, the staff then recommended adoption of Proposal Number One with some modifications.[22]

25. Qwest and Sprint supported Proposal Number One while NT&T, a UNE based provider, supported Proposal Numbers Two and Three.

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20 This encompasses all supported services provided by NETCs through the use of a designated network provider's loop facilities including UNE-P.

21 *See* Commission Staff's Post-Hearing Brief at 10.

22 *Id*.

26. The Commission, upon consideration of the arguments presented, believes that Proposal One along with the modifications suggested by the staff is the fairest way to treat both the ILEC and the CNETC.

27. The Commission, as recommended, will freeze the support level for residential lines at the pre NUSF-26 transitional support amounts throughout the 5-year post NUSF-26 transition period. Therefore, the rates used to calculate the monies to be ported from ILEC to CNETC during the post NUSF-26 transition period will be as follows: Zone One residential: $0.57, Zone Two residential: $20.35, Zone Three residential: $69.59. Support should continue to be ported, based upon the total support amount, from the ILEC to the providing CNETC on a dollar-for-dollar basis.

28. At the end of the post NUSF-26 transition period, the Commission will re-evaluate the support structure and open a proceeding to address any needed modifications.

29. As a general matter, the Commission will no longer be porting support for business lines. However, with respect to the business lines from which CNETCs are currently receiving support, the Commission, as recommended, adopts a hold harmless provision during the transition period to avoid any disruption to the CNETCs who are currently competing in rural areas. Specifically, the NUSF Department should calculate business line support using the current zone port rates, which are as follows: Zone One business: $0.00, Zone Two business: $15.15, and Zone Three business: $56.87.

30. The hold harmless provision will only be applicable for the number of lines reported for September 2004. CNETCs will then continue to receive NUSF support for the business lines unless and until such lines are lost. The CNETCs could fall below the current support level for business lines but could never receive support above the level established by the September 2004 access line report. CNETCs are required to notify the NUSF Department when they no longer provide service to such a grandfathered business line.

31. The Commission will re-evaluate this issue after the post NUSF-26 transition period, or at any point during the transition period if necessary, and will consider opening a proceeding to address any necessary modifications.

SERVICES

32. Existing Commission authority provides generally for the availability, to all Nebraskans, of three types of services: telecommunications, advanced, and information services.

Telecommunications Services

33. The Commission finds that the following two types of telecommunications services be made universally available: Basic Local Exchange service and Interexchange service. Interexchange service encompasses both access services and toll services.

34. The Commission finds that it should continue to support Basic Local Service as defined in the Nebraska Universal Service Fund Rules and Regulations.[23]

35. In the C-1628 Order, the Commission adopted rate benchmarks of $17.50 and $27.50 per month for residential and business basic local exchange services respectively. In order to qualify for support under the transitional mechanism, an eligible telecommunications provider was required to price both of these services at or above these benchmarks. The Commission finds it should retain this requirement relative to residential service. The Commission will remove this requirement relative to business service. Given the Commission is adopting a support mechanism based upon households, which would exclude most businesses, it is no longer appropriate to retain the business rate benchmark. Moreover, the Commission finds the evidence shows businesses typically are located in more dense areas, which would have received little or no support under the Commission's adopted methodology. Support will be ported to CLECs only as provided herein. At the hearing, the Commission staff indicated it may be appropriate to impute the business benchmark going forward even though the benchmark would be removed. The Commission will further evaluate imputation of the C-1628 business benchmark rates during its later review of EARN form modifications.

36. While the Commission believes access services are a component of universal service and a supported service, the

23 Neb. Admin. Code, tit. 291, ch. 10, § 001.01D.

Commission finds that no support should be provided for access services at this time. However, companies must comply with all orders relative to access charges to qualify to receive Program support.

37. While the Commission finds toll services are a component of universal service and a supported service, it finds that support is not required at this time.

Advanced Services and Information Services

38. The Commission has limited authority over advanced services (including xDSL and cable modem) and information services (i.e., the Internet). However, the Commission believes it can facilitate access to such services through its universal service policies and its support of the underlying physical network.

Components of Service

39. The Commission finds it necessary to begin to separate the underlying physical network from the service itself. As networks continue to evolve and new technologies are deployed, the emphasis for universal service needs to shift, from directly supporting services, to supporting comparable access to services determined to be made universally available. Comparable access continues to incorporate the same statutory standards of ensuring telecommunication services are available to persons living in rural and high cost areas at reasonable, comparable rates and quality. It may also have the ultimate effect of expanding the quantity of services available in rural and high cost areas.

40. As the Commission examined the cost of providing telecommunications service, the most significant cost difference, between high and low cost areas, appears to be the cost relating to connecting customers to the service provider's network. In this regard, the Commission defines the service provider's network as the first selective routing device that is owned, leased or otherwise used under a wholesale agreement by the telecommunications provider that bills the customer for service(s).

41. Currently under this definition, in the context of basic local exchange service, the service provider's network

would begin at the local switch. The loop connecting the customer to the switch, which in many cases is also owned by the same company, would constitute access to the service provider’s network. The loop connects the customer typically through a telephone or a computer, to the service provider’s network through a routing device, which in most cases, is currently a central office switch. Usually the service provider owns both the routing device(s) and related network between such device(s), and the loop. The loop carries the information the customer wishes to transmit or receive to the service provider’s network and the routing device(s) determines the route the information will travel. The routing device then either routes the traffic to the designated loop connected to the same routing device or to another routing device or device(s) that will then route the traffic to the designated loop.

42. This same general network design is used to provide inter-exchange services and access to advanced and information services. A physical connection links customers to the service provider’s network. The service provider’s network uses a series of interconnected routing devices to route the information to its destination, irrespective or whether the service is based on circuit switched or packet switched technology, e.g. Internet protocol. However, in most rural and high cost areas, the physical connection linking the customer to the service provider’s network is longer and may encompass services traditionally referred to as transport.

43. In the context of access services, the service provider’s network begins either at the toll switch or the point of interconnection between the local exchange and long distance carrier. In the context of an information service, such as Internet service, the service provider’s network begins at either the selective router or the point of interconnection where the traffic is handed off to the Internet service provider.

44. With this approach, universal service funds would be used to ensure everyone has access to these service providers’ networks at reasonably comparable costs. For the purpose of this proceeding, the Commission has focused on access to basic local exchange service through the loop. As the Commission previously indicated, in a subsequent proceeding, it will seek comment on issues relative to access to other telecommunications and information services.

<u>Fund Support Allocation Methodology</u>

Overview

45. The Commission finds that it should utilize the Nebraska Universal Service Fund Support Allocation Methodology, (SAM) in order to allocate Program support to NETCs providing service to high cost areas. The SAM provides for the allocation of Fund Program monies to NETCs based on the cost an NETC incurs in the provisioning of service, relative to the cost of service throughout the state.

46. As previously stated, the SAM utilizes 2000 Census household data, by census block, collected by the U.S. Bureau of the Census, to create support areas. The SAM utilizes the Benchmark Cost Proxy Model (BCPM), Version 3.1, and a common set of inputs, to calculate household densities and estimate forward-looking loop costs. Econometric regression techniques are employed to link forward-looking loop cost to household density. Finally, with the use of the regression results and support area densities, expected loop cost is calculated for each support area.

47. The SAM compares expected loop cost, for each support area, to a loop cost benchmark. When expected loop cost exceeds a loop cost benchmark, a base support amount for the support area is calculated. Results are aggregated. Finally, each NETC’s allocation of the Program loop support is calculated based on relative base support amounts.

48. The SAM utilizes the cost of the local loop as a proxy for the total cost of service. The SAM does not include a switching cost element in its estimation methodology.

49. The Commission finds the SAM is practical, manageable, flexible, and focuses support to high cost areas in Nebraska. The SAM provides a fair and reasonable process in which to allocate NUSF support to NETCs providing service to high-cost areas. Therefore, the Commission hereby adopts the SAM, as described in detail in the Commission’s June 29, 2004 Order, its Appendices, and at the hearing, for the determination of Fund Program support.

50. The Commission finds the SAM's use of the BCPM is appropriate in the context of this docket. Additionally, the Commission finds the SAM should reflect the costs of a most efficient carrier and thus also concurs with the SAM's use of a common set of inputs for all companies.

51. The Commission further finds the SAM's use of the local loop cost as a proxy for the total cost of service, as well as its exclusion of a switching cost element, is appropriate. A high correlation between the cost of provisioning service and the cost of the local loop provides a sufficient mechanism in which to associate more closely the allocation of the Fund with cost causation. In addition, as the cost of service in high cost areas is also vastly related to the increased cost of providing the "last mile," the SAM ensures the allocation of the Fund is one that furthers the goals of the NUSF Act.

The SAM Process of Determining Support

Introduction

52. As adopted herein, the SAM will utilize 2000 Census household data, by census block, collected by the U.S. Bureau of the Census. Using the census data, the SAM should aggregate the state into multiple urban and rural support areas that reflect cost causation and prevent any arbitrage that may occur if high and low cost loops are combined into one support area.

53. The SAM will then develop forward-looking loop costs in each support area. The process for determining forward-looking loop cost occurs in four steps. 1) The SAM utilizes the BCPM, and a common set of inputs for all companies, to calculate household densities and forward-looking loop costs in areas definable by a cost model. 2) Regression techniques are then employed to link forward-looking costs to household density for those well-defined areas. 3) Densities are determined in the proposed support areas. 4) Finally, with the use of the regression results, expected loop cost, as a function of measured density, is calculated for each support area.

54. The SAM will then compare expected loop cost, for each support area, to a loop cost benchmark. When, in a particular support area, the loop cost is above the benchmark, the difference between the two is multiplied by the number of

households in that support area to obtain the base support amount for that support area. Support area results are aggregated to the NETC level to get the base amount of support for each NETC. NETC amounts are aggregated to get the statewide base amount. The SAM then calculates each NETC's allocation of Fund Program support calculated as the NETCs base amount, relative to the statewide base amount.[24] The Commission sought comment on whether each NETC's allocation of Fund Program support should be adjusted for Federal Universal Service Fund (FUSF) support amounts. Upon review of this issue, the Commission finds that support should not be adjusted for FUSF support amounts. Finally, transitional support adjustment will be applied.[25]

Validity of the SAM

55. The Commission finds the purpose of the Fund Program is to ensure all Nebraskans, without regard to their location, including those in rural and high cost areas, have comparable access to telecommunications services at affordable prices.[26] The Commission finds the SAM fulfills this purpose.

56. SAM salient statistics indicate greater than 98 percent (98.0%) of Program support is allocated to support areas with less than seven (7) households per square mile, and nearly 100 (100.0%) percent of Program support is allocated to support areas with less than thirteen (13) households per square mile. Further, greater than 99 (99.0%) percent of support is allocated to rural, "out-of-town", support areas.

57. The Commission finds that no other commenter in this proceeding provided sufficient evidence to discredit the staff's proposed SAM methodology. The Commission finds that the SAM is statistically sound and reasonable allocation of support.

58. The Commission further finds explaining average loop cost as a function of density has a reasonable basis. The

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24 As an example, suppose an NETC has a base amount, adjusted for FUSF support amounts, of $400,000 and the statewide base is $40,000,000. That NETC would receive 1/100th of the loop fund.

25 *See* NUSF-26, Progression Order No. 5 (June 29, 2004) Appendix A for further discussion.

26 NEB. REV. STAT. §§ 86-317 and 86-323.

Commission is persuaded by the staff's expert witness that when calculated appropriately, the R^2 is 0.78, indicating that 78 percent of the variation in average loop cost can be explained by the variation in density. The Commission finds that density is the most significant factor in estimating loop costs, particularly in light of the fact that no other alternative was proposed.

59. The Commission is not persuaded that changes to the model are warranted based on unique circumstances of a company.

60. Upon review of the evidence presented herein, the Commission finds the SAM meets the objectives of the Fund.

NUSF-EARN

61. The Commission will continue to employ an earnings test to determine that NUSF support does not exceed the level required by NETC's to recover their costs. While the Commission desires to develop a permanent earnings test, additional study is required for this development. Therefore, the Commission finds, for the present time, the current earnings test obtained through the NUSF-EARN form should continue to be utilized.

Transition to SAM

62. The Commission adopts the proposed transition mechanism to accompany the permanent funding mechanism. The Per-Line Backstop and Over-Earnings Redistribution are for a period of five years, whereas NUSF-7 sunsets when the investment made by the company is fully depreciated. The Commission finds this transition period allows carriers an opportunity to make adjustments, prevents undue hardship to customers and is in the public interest.

63. The Commission adopts the following transitional support adjustments in an effort to judiciously prevent financial hardship on those NETCs experiencing decreases as Fund Program support is transitioned from the current methodology to the SAM.

Transitional Support Adjustments

64. Once SAM support amounts are calculated and support area results are aggregated to the company level, the Transitional Support Adjustments should be applied. All Transitional Support Adjustments amounts will be subject to the earnings test. NUSF-7, Per-line Backstop and Over-earning Redistribution transitional support mechanisms shall only be available to those companies experiencing a decrease in Program Fund support subsequent to the implementation of the SAM and will be subject to the earnings test.

65. The Commission should recalculate the Transitional Support Adjustments, as necessary, with the same frequency as employed for the earnings test.

Proposed Methodology for NUSF-7 Waiver Recipients

66. If a company experiences a significant reduction in Fund Program support under the SAM, and has received an NUSF-7 grant, the NUSF-7 monies will be added to the NETC’s allocation of the Fund Program support determined by the SAM. This ensures the costs, related to investments made pursuant to NUSF-7 grants, are fully recovered.

67. In conjunction with the proposed changes to the support mechanism, the Commission believes it also necessary to make adjustments to the NUSF-7 grant methodology. Earlier, the Commission proposed to recalculate the NUSF-7 waiver amounts, based on proposed changes in the Fund Program support methodology. The Commission adopts this proposal. Appended herewith as Attachment B and fully incorporated herein is a list of the NUSF-7 waiver recipients along with the recalculated amounts as adopted in this Order.

68. The Commission also proposed to sunset the NUSF-7 amounts at the point in time NUSF-7 investments are fully depreciated. Upon further consideration, the Commission finds when a company’s NUSF-7 waiver is about to expire, it will consider, on a company-by-company basis, a request to extend such grant or to make the grant permanent. The continuance of NUSF-7 support will be contingent on sufficient funds being available.

Per-Line Backstop

69. A Per-Line Backstop is adopted as the Commission's second transitional support adjustment.

70. If applicable, the Per-Line Backstop is based on a per-line decrease in Program support. Should a company experience a decrease in support greater than $5.00 per line, per month, an amount equal to the difference in the company's per-line support decrease and the $5.00 maximum is multiplied by the respective company's residential access lines.[27] The resulting amount is the Per-Line Backstop adjustment. This adjustment ensures, subject to the earnings cap, an individual company does not experience a per-line reduction in Program support, when transitioning from the current mechanism to the SAM, greater than $5.00 per-line per month in a given year, as described by Commission staff at the hearing. Accordingly, the per-line reduction will be limited to $5.00 per line per month in year one, $10.00 per line per month in year two, $15.00 per line per month in year three and so forth.

71. Any Program monies determined due to the Per-Line Backstop are subject to the earnings cap. Therefore, any company experiencing a per-line reduction in support greater than the maximum, but at or above the earnings cap, will receive no additional support.

72. The Commission finds the Per-Line Backstop a viable transitional mechanism, subject to the earnings test, relative to access lines, when transitioning from the current Fund support methodology to the SAM

Over-Earnings Redistribution (OER)

73. As previously stated above, the Commission finds that it should utilize the current NUSF-EARN methodology to determine if an NETC exceeds the earnings cap. Subsequent to the NUSF-7 and Per-Line Transitional Support Adjustment, any additional Program support available, due to the earnings cap, will be made available via Over-Earnings Redistribution (OER). The

27 Company residential access lines are those included in the Commission's 2004 Annual Report on Telecommunications.

Commission will retain the OER transition mechanism for five years.

74. Once an OER amount is determined, OER allocations will be calculated for those companies not at the earnings cap. OER allocations will be determined based on SAM results. For those NETCs not currently at the earnings cap, the OER allocation is the expected loop cost, by support area, relative to the total expected loop cost for all NETCs not currently at the earnings cap. OER allocations, by support area, will then be aggregated by NETC and applied to the OER amount to determine each NETC's OER allocation. The earnings cap should apply to all OER allocation amounts. This process should be repeated, iteratively, until such time as all NETCs reach the earnings cap or all available OER is allocated.

75. As companies invest additional monies into their networks, those at or above the earnings cap will see a decrease in their respective rate-of-return. As such, additional SAM support amounts will begin to flow back to those companies. Thus, as a company invests and stakes claim to its SAM support amounts, OER monies available will gradually decrease. The Commission finds this to be a reasonable and viable transitional mechanism.

76. The Commission encourages companies to utilize this transition period to accomplish investments necessary to further the goals of the Fund.

Access Line Factor Adjustment

77. In their post-hearing brief, the Rural Independent Companies argued that the Commission's access lines per household factor of 1.15 in equation 2 is illogical.[28] The post-hearing brief is the first time this issue was raised by the parties. Had this argument been raised earlier in the proceeding, parties could have studied this issue more closely and perhaps recommended a change or modification that could have satisfied the concerns on this issue. However, because of the delay in raising this concern, neither the Commission nor the parties have had the opportunity to consider the impacts a change to the factor would have. The Commission therefore finds

28 Post-Hearing Brief of the Rural Independent Companies (Sept. 30, 2004) at 12.

that the Rural Independent Companies request for removal of this factor is untimely, and further finds that the model including the access lines per household factor of 1.15, as presented at the hearing, should not be modified at this time. The Commission may consider making adjustments in the model during a later review when the issue has been properly presented, when the opportunity for all parties to review potential adjustments exists, and after all parties have had an opportunity to comment.

The Zone Adder-Adjustment

78. Currently, various NETCs charge additional "zone" rates to the end-user customer, dependent on distance from a central office. The proposed SAM contained an Adder-Adjustment to the residential loop benchmark to account for the contribution made by this source of revenue toward recovery of loop cost. Many of the commenters opposed the Zone Adder adjustment and requested that the Commission eliminate it altogether.

79. Upon consideration of the testimony, the Commission finds that it is appropriate to encourage the elimination of such zone charges in order to foster the goal of rate comparability found in Neb. Rev. Stat. § 86-323(3). However, the Commission is aware that if it encourages the elimination of zone charges certain companies will lose a revenue source. Therefore, the Commission finds it appropriate to establish the following mechanism for NETCs that eliminate or reduce zone charges. This support should be available effective concurrently with the implementation of the SAM distribution mechanism.

80. The Commission adopts the following procedures:

a. The NETC should be required to notify the Commission in writing before December 1, 2004 of its intent to eliminate zone charges effective January 1, 2005. In that notice, the NETC should commit that the company would refrain from re-instituting the zone charges for a period of not less than five years. This notice should also contain the revenue realized in 2003 from said zone charges that were included in the 2003 EARN Form, broken down into zones, if appropriate.

b. The NETC should also file a tariff amendment with the Commission that eliminates zone charges effective January 1, 2005.

c. Following steps a) and b) above, the NETC's Zone Adder-Adjustment in the SAM will be set to zero, and the Commission staff will make an adjustment to the model as if zone charge revenue had not been received in 2003.

d. The NETC that has eliminated zone charges will provide to the Commission concurrent with its NUSF-EARN Form for 2004, an attachment detailing the revenues realized from zone charges that are included in the 2004 EARN Form.

e. The NETC will be eligible for any increased program support so long as all other conditions precedent to the receipt of support are also met. The Commission shall make model adjustments equal to the amount indicated in (a) and reflected in the model in (a) and (c), less additional revenue received in (c) and this shall continue for a period of seven years.

f. The Commission directs the Department to take sufficient action to adjust NUSF support as necessary when a company re-instates zone charges.

Periodic Adjustments

81. There is no doubt that the SAM process will initially be a complex process to administer. Over time, the Commission anticipates adjustments will be required to account for changes to the data used to calculate support. The Commission grants discretion to the NUSF Department to make changes from time to time as necessary and that are consistent with our findings herein. Any company that receives a payment from the Program may request the underlying information used to determine said payment, excluding information that is the confidential and proprietary property of another company pursuant to State law. If a company disagrees with the NUSF Department's application of the Commission's findings relative to the calculation of Program payments, it may file a request for the Commission to review the matter.

82. Annually, the Department should run the model and release the results at a Commission public meeting. The Commission will then direct the staff to make changes, or in the alternative, if no changes are anticipated, the Commission will formally approve the payments for the year.

83. The Commission will largely carry through the conditions precedent to receiving support from the transitional period. Companies are required to maintain their NETC designation and continuously meet those requirements as a condition of support. As previously stated, eligible telephone companies will no longer be required to charge the $27.50 floor benchmark for business line service in order to receive permanent program support. Rather, NETCs will be required to charge a minimum of the $17.50 benchmark for all lines as a condition of support. ILEC NETCs will further be required to file timely NUSF-EARN forms. The Commission will examine in a later proceeding whether to require NUSF-EARN forms from other NETCs.

84. Finally, NETCs are required to abide by all applicable statutes, rules and regulations and Commission orders in order to receive support. Pursuant to statutory authority in Neb. Rev. Stat. § 86-324, the Commission may withhold support as a penalty for violation of any NUSF statutes, rules and regulations and Commission orders.

Subsequent Proceedings

85. The Commission will open further proceedings at a later date to address, at least, the following:

a. As Advanced Services and Information Services continue to evolve, the Commission anticipates opening a docket to explore whether it should adopt standards for deployment and whether additional NUSF Program Support is needed to ensure access to these services.

b. The Commission anticipates exploring the possibility of modifying the earnings test to be more focused on investment levels and less reliant on company supplied data.

c. The Commission anticipates exploring the possibility of making service quality standards contingent upon NUSF Program monies.

<u>Workshop Schedule</u>

86. The Commission finds that it should hold a workshop where the application of the SAM, and the SAM results in terms of support payments for the 2005 calendar year are discussed in practical terms. This workshop is hereby set at 10:00 a.m., on December 15, 2004, in the Commission Hearing Room, 300 The Atrium, 1200 N Street, Lincoln, Nebraska.

O R D E R

IT IS THEREFORE ORDERED by the Nebraska Public Service Commission that the findings and conclusions detailed herein, be and they are hereby adopted.

IT IS FURTHER ORDERED that the proposed NUSF-7 recalculations provided in the Commission Staff's Post-Hearing Brief and as set forth in Attachment B to this Order be and they are hereby adopted.

IT IS FURTHER ORDERED that a workshop be held on December 15, 2004 at 10:00 a.m. in the Commission Hearing Room, 300 The Atrium Building, 1200 N Street, Lincoln, Nebraska.

MADE AND ENTERED at Lincoln, Nebraska, this 3rd day of November, 2004.

NEBRASKA PUBLIC SERVICE COMMISSION

COMMISSIONERS CONCURRING:

Chairman

ATTEST:

Executive Director