REPORT

ON THE

TENNESSEE RURAL

AFFORDABILITY FUND

EXECUTIVE SUMMARY

During the 2008 legislative session, Senate Bill No. 2147 / House Bill No. 2117, was introduced. Subsequently, an amendment was drafted rewriting the bill, deleting sections (b) through (e) in the existing Tennessee Code Annotated, Section 65-5-107, and replacing those sections with language that would require the establishment of the Tennessee Rural Affordability Fund ("TRAF"). This amendment, referred to hereafter as the "proposed legislation" or the "bill" is provided as Attachment A.

The statutory sections to be deleted by the proposed legislation authorize the Tennessee Regulatory Authority ("TRA" or "Authority") to establish, if found necessary by the TRA, an alternative support mechanism to ensure that all Tennesseans have access to affordable basic telephone service. This policy objective is referred to as universal service. The existing statute that empowers the TRA to meet this policy objective is found in Tennessee Code Annotated, Section 65-5-107. This statute can only be implemented if it is determined "that the alternative will preserve universal service, protect consumer welfare, be fair to all telecommunications service providers, and prevent the unwarranted subsidization of any telecommunications service provider's rates by consumers or by another telecommunications service provider."[1] Further, the existing code sections provide the parameters of any fund, and grant the Authority jurisdiction to monitor and enforce the criteria for such fund.[2] This statute was enacted in 1995 by the General Assembly and has not been implemented by the TRA. Even though the TRA has not seen the need to establish a state universal service fund (USF), there are indications that a major source of

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[1] Tenn. Code Ann. § 65-5-107(b).
[2] Tenn. Code Ann. § 65-5-107(c).

revenue that rural telephone companies have depended upon to help maintain affordable rates is rapidly dropping. The revenue stream in jeopardy is referred to as intrastate switched access. The consequences of losing this historical revenue stream could have a significant impact on telephone services in rural areas of the State. The proposed legislation attempts to remedy this problem.

The proposed TRAF legislation is specific to telephone companies serving the most rural areas of the State [rural incumbent local exchange carriers ("RLECs") and rural telephone Cooperatives] with less than one million (1,000,000) access lines, where it can be argued that competition has been slower to develop. The bill requires these carriers to reduce their intrastate switched access rates[3] to their interstate switched rate levels. The revenue loss resulting from these reductions will be recovered from funds paid into the TRAF. The TRAF is to be funded in a manner similar to the Federal Universal Service Fund, and the Authority is to implement and administer the TRAF.

On May 19, 2009, Chairman Richard Montgomery of the Utilities and Banking Subcommittee of the House Commerce Committee requested the Authority "study this legislation and make recommendations" to the General Assembly during its 2010 legislation session. Subsequently, Representatives Charles Curtiss and Charles Sargent, Jr. submitted additional questions for the TRA to consider when preparing its report. This Report on the Tennessee Rural Affordability Fund ("Report') is provided in response to the requests of Chairman Montgomery and Representatives Curtiss and Sargent. The Report provides a brief background of access charges and rates and an overview of the proposed legislation.

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[3] Switched access services are purchased by interexchange carriers from local telephone companies for use of local facilities necessary to complete long distance telephone calls.

Additionally, the Report contains specific recommendations in the event the General Assembly moves forward with consideration of such legislation.

In summary, the Authority recommends that:

1. Any funding to support rural broadband deployment should be established as a separate portable fund. The proposed legislation should target keeping local telephone rates affordable;
2. No statewide benchmark rate for local telephone service should be established as a litmus test to determine support from TRAF;
3. A statutory sunset provision should be incorporated in the proposed legislation with the requirement that the TRA provide a report and recommendation to the legislature before consideration is given to extending the life of the TRAF;
4. A statutory provision to cap the size of the TRAF should be established once determined by the TRA. Such a cap will control the growth of the TRAF;
5. The language deeming recipients as carriers of last resort should remain. Additionally, the legislation should include provisions that all receiving entities provide certain social and safety services such as Lifeline/Link-up;
6. Companies electing Market Regulation under Tenn. Code Ann. § 65-5-109 should not be allowed to draw from the fund. Because a carrier operating pursuant to market regulation can adjust its rates to respond to competition, the need for specific subsidies such as that from the TRAF would become unnecessary. Therefore it is appropriate to cease such TRAF assistance if the carrier elects Market Regulation;

7. The requirement whereby each provider contributing to the Federal Universal Service Fund must contribute to the TRAF should remain;
8. Language should be added empowering the Authority to assess and collect fees and providing the TRA with specific rulemaking authority to establish criteria and procedures for assessing, collecting and dispensing fees, and for monitoring the operation of the TRAF;
9. The proposed TRAF language should be added to Tennessee Code Annotated § 65-5-107 with the existing language in Section (b) through (e) remaining in place; and
10. The effective date of any legislation enacted should be delayed one year to enable the Authority to adopt rules putting into effect procedures and criteria for operation of the TRAF.

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Introduction

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the need to establish a state universal service fund (USF), there are indications that a major source of revenue that rural telephone companies have depended upon to help maintain affordable rates is rapidly dropping. The revenue stream in jeopardy is referred to as intrastate switched access. The consequences of losing this historical revenue stream could have a significant impact on telephone services in rural areas of the State. The proposed legislation attempts to remedy this problem.

The proposed TRAF legislation is specific to telephone companies serving the most rural areas of the State [rural incumbent local exchange carriers ("RLECs") and rural telephone Cooperatives] with less than one million (1,000,000) access lines, where it can be argued that competition has been slower to develop. The bill requires these carriers to reduce their intrastate switched access rates[3] to its interstate switched rate levels. The revenue loss resulting from these reductions will be recovered from funds paid into the TRAF. The TRAF is to be funded in a manner similar to the Federal Universal Service Fund, and the Authority is to implement and administer the TRAF.

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request of Chairman Montgomery and Representatives Curtiss and Sargent. The Report provides a brief background of access charges and rates and an overview of the proposed legislation. Additionally, the Report contains specific recommendations in the event the General Assembly moves forward with consideration of such legislation.

A. Background of Switched Access and Local Rates

When evaluating the proposed legislation it is important to understand the history and relationship between switched access charges and local rates of RLECs and telephone Cooperatives in Tennessee. Although the Authority does not have jurisdiction over the Cooperatives' rates, the following discussion regarding RLEC rates can also be generally applied to telephone Cooperatives.

In order to make residential telephone service available and affordable to all Tennesseans, the Authority and its predecessor agency, the Tennessee Public Service Commission, established and maintained low telephone rates for residential consumers.[4] In order to maintain these low rates, other services provided by RLECs had to be priced above their respective costs in order to subsidize residential consumer rates. Many of the higher rates contained implicit subsidies making them difficult for customers to identify. Switched access, which is a system of rates purchased by interexchange carriers ("IXCs") for use of the local telephone company facilities in completing long distance calls, was one

[4] The FCC's most recent report on telephone penetration was issued in August, 2009 and included data through March, 2008; the report states that 92.8 percent of all Tennessee households had telephone service.

such service priced above its related costs so that residential local rates could remain low. This built-in implicit subsidy exists today and is an important factor in local residential rates in Tennessee remaining low. Attachment B contains a list of the current residential rates for the RLECs and telephone Cooperatives with less than one million access lines in Tennessee.

Revenues received from switched access services have historically allowed RLECs and telephone Cooperatives to offer lower rates for residential service. Over the past several years, however, consumers have gained the ability to place long distance calls via wireless, Voice over Internet Protocol ("VoIP") and other technologies – technologies capable of completing calls without using the switched networks of local telephone companies or, at least, can avoid the use of part of the network. Further, the number of wired access lines for RLECs has declined with the advent of these technologies. Accordingly, the levels of switched access minutes and associated revenues have declined, thereby reducing the amount of revenues that flow to support local residential rates.

Moreover, like many other telephone companies, rural providers face challenges from competitors, technological changes and changes in consumer preferences. Unlike larger telephone companies with a higher concentration or density of customer base, RLECs and Cooperatives generally do not have as diverse a set of revenue streams to offset potential revenue losses. Rural providers also operate in areas with a cost generally higher than that of the urban areas. The combination of factors threatening their revenue streams, coupled with higher service costs, potentially endanger the financial stability of

RLECs and Cooperatives, which in some instances are the only facilities-based wireline providers in their rural service areas.

A. Overview of the Tennessee Rural Affordability Fund (TRAF)

Two of the basic revenue streams that RLECs depend upon to maintain affordable local rates are switched access revenues and monthly rates for local service. Loss or substantial decline of either revenue source can put in jeopardy the present price of residential services. The creation of the TRAF recognizes the fact that switched access revenues and the cash flow they provide are declining and are likely to continue to erode; in fact, the number of billed switched access minutes for RLECs has declined 29% since 2004 (see attachment C for a list of RLEC billed intrastate switched access minutes from 2004 through 2008). The TRAF provides a reasonable means to lessen this impending financial impact on RLECs and Cooperatives. Specifically, the TRAF would remove a large portion of the existing implicit subsidy in intrastate switched access rates by reducing the rates to the interstate switched access rate levels. To make up for this revenue loss, however, a fund will be created essentially equal to the total amount of access revenues lost by the RLECs and telephone Cooperatives collectively. As written, the proposed legislation requires that contributors to this new fund consist of all providers of voice communications in Tennessee, including competitive local exchange companies (CLECs), cable providers, VoIP providers, resellers of local service and wireline telephone companies themselves. Contributions would be based either upon a percentage of total intrastate revenues or a fee per working telephone number. In turn, RLECs and Cooperatives would draw monies from this fund to make up for their lost switched access revenues. The practice of collecting funds from this broad base of carriers is analogous to that used by the Federal Communications Commission ("FCC") in administering the Federal Universal Service Fund.

In other words, the existing revenues received from switched access charges once paid by IXCs for aid in maintaining low residential rates would be replaced by a system of funding to be recovered from all providers of communications services in Tennessee. Carriers paying into this fund would be able to recover their contributions through a line item surcharge on consumer bills. The Authority would administer and oversee all aspects of fund assessments, collections and disbursements.

Size of Fund and Customer Charge

Based upon information available to the Authority, along with an analysis of interstate switched access rates, it is estimated that the initial size of the fund would be approximately $20 – 25 million dollars.[5] Using this approximate size of the fund and the number of telephone lines in Tennessee based upon the latest FCC data, consumers could expect to see a line item surcharge of approximately $0.20 to $.25 per month on their monthly bills for communications services. As stated above, RLECs and telephone Cooperatives would draw monies from the fund; the amounts would vary by carrier, and it is estimated that individual RLECs would receive anywhere from $0.50 per residential line to over $29 per residential line on a monthly basis. The variation of the reimbursement

[5] The Authority does not have available data from telephone Cooperatives regarding the effect of reducing access rates; therefore, this amount approximates the need of these carriers.

rate depends upon several factors, including the switched access rates charged by individual RLECs, the amount of switched access minutes and the number of residential lines. Attachment D shows the approximate residential per line amount and total annual payment to be received by each RLEC.[6]

Effects of Establishing the TRAF

The TRAF would provide necessary financial stability to the RLECs and telephone Cooperatives by requiring an explicit subsidy (rather than implicit subsidy) flow from all communications providers in Tennessee to these rural carriers, instead of placing the financial burden of loss of access revenues entirely on the customers of the RLECs and telephone Cooperatives. This explicit subsidy should, in theory, allow rural carriers to maintain rates and quality of service at their current levels and thus aid in maintaining the goal of universal service. The proposed legislation, however, does not provide for a determination as to whether a continued subsidy would be necessary to ensure affordable rates. In response to Authority data requests, some potential contributors to the TRAF expressed the need to evaluate the RLECs' earnings prior to establishing this funding mechanism. Although current revenue streams from switched access continue to decline, local rates for RLECs and telephone Cooperatives have remained affordable, and only one RLEC in the past twenty years has petitioned the Authority for a general rate increase. While there can be many explanations for not filing for a rate increase, it does not

[6] The Authority does not have sufficient data from the telephone Cooperatives to calculate amounts for telephone Cooperatives.

necessarily mean that the financial condition of a company is healthy. In fact, there are examples across the nation where large incumbent telephone carriers are selling off their rural exchanges. At least one of these acquisitions has resulted in the purchasing carrier filing for bankruptcy. Moreover, in Tennessee, there is some evidence that the decline of access revenues may be impacting the earnings of RLECs. In financial reports submitted to the TRA, 12 (twelve) out of 15 (fifteen) RLECs indicate they did not earn their authorized rate of return for the latest twelve (12) months.[7]

It is important to note that the TRAF is distinctly different in scope and application from a traditional universal service fund, as envisioned by the existing statute. The revenue stream created by the TRAF should not be confused with universal service support, because the subsidy established by the TRAF is not designated to provide specific support for local rates and does not offer portable support to all carriers providing local service. This limited availability of subsidies for local rates is one of the primary differences between the proposed TRAF legislation and the general manner in which a Universal Service Fund ("USF") normally operates. Through a USF, subsidies are provided to any and all providers of local service in an area that is generally designated as a high cost area. In this manner, competition is encouraged in high cost areas, which most often are rural areas. As such, universal service is funded and preserved regardless of the carrier providing service in the area. One weakness of the USF strategy is the potential growth of the fund due to the subsidy being available to all comers. The design of the

[7] Based upon monthly and quarterly reports filed with the TRA.

TRAF, on the contrary, is more likely to keep the size of the fund smaller by limiting those who can tap into the fund. Clearly, the TRAF should not be viewed as a USF, but rather as a replacement revenue-neutral stream flowing to RLECs and telephone Cooperatives to strengthen them financially in return for their continuing status as carriers of last resort, as well as a means by which these carriers may maintain affordable rates. Clearly, the TRAF is more of a revenue stabilizer for rural carriers which should work to complement the goal of universal service. The Authority believes that institution of a TRAF is likely to delay the need for a state Universal Service Fund for recipients of the TRAF.

Although the TRAF should allow rural companies to maintain local rates and service quality at their current levels, there is a trade off. The TRAF could also make it more difficult for competition to emerge and evolve in rural areas because competitors offering local service would not receive the benefit of a consistent revenue stream. Accordingly, competition in certain areas could be impeded where one utility must compete for the same service with another utility (the RLEC or telephone Cooperative) receiving a subsidy. Of course, unlike RLECs and Cooperatives, competitors have no obligation to serve all customers in areas they enter and often refuse to expend the capital to serve the most rural, low density areas of the State. This is why there is a need for a financially stable carrier of last resort.

There are alternatives to establishing the TRAF if reductions to intrastate switched access rates are mandated. One option is to increase local telephone rates. A carrier under the Authority's jurisdiction that is experiencing a loss in access revenues can always petition the Authority to increase rates if the lost revenues result in the carrier not earning a fair rate of return. Our analysis indicates that the loss of RLEC revenue from reducing intrastate switched access rates to the interstate level ranges from $0.51 to $29.14 per month per residential line. (See Attachment E) The boards of telephone Cooperatives can vote to increase local rates. Such action, however, could result in local residential rates increasing to a level which might bring into question the affordability of rates and running counter to the goal of universal service. The proposed legislation, however, does not address the affordability of local rates nor does it provide a test to determine whether local rates are affordable.

To aid in maintaining affordable residential rates, RLECs and telephone Cooperatives have the ability to receive revenues from the Federal Universal Service Fund to help cover the cost of local service. To receive this revenue, a telecommunications service company must apply for, and be designated as an eligible telecommunications carrier ("ETC"). Typically, the FCC grants designation for carriers not regulated by the state and the Authority grants designation for the state-regulated carriers. Since 1997, the Authority has designated all rural companies, including telephone Cooperatives and the RLECs, as ETCs.

Specifically, all ETC designated companies must annually certify either directly to the FCC or through the Authority that they are using the federal universal service subsidies in the manner prescribed by federal regulation. This attestation ensures a certain degree of regulatory accountability. In addition, as a part of that certification, the Authority must certify that the rural rates charged by the ILEC are deemed affordable and reasonable and generally comparable to the national benchmark rural rate. To assist the states in making the comparison of rural rates, the FCC adopted a rate benchmark of two standard deviations above the average urban rate in an annual publication called the *Reference Book.* This "safe harbor" or benchmark is used by states to make the reasonable rural rate determination. To ascertain whether rural residential rates are affordable, the Authority compares Tennessee's rural residential rates to the highest residential rates charged by the state's largest non-rural carrier, BellSouth Telecommunications, Inc. d/b/a AT&T Tennessee ("AT&T").

Additionally, the Authority reviews other relevant factors to determine whether rural residential rates charged by non-rural carriers are reasonably comparable. This review includes service standards, the availability of toll free county-wide calling and access to expanded calling areas. The Authority continues to evaluate the affordability of residential local rates and carrier-of-last resort obligations in Tennessee under the current statutory provision contained in Tenn. Code Ann. § 65-5-107. This statute, unlike the proposed legislation, provides the Authority with the ability to create a universal service fund in case the affordability of local residential service is threatened. While we believe the creation of the TRAF may postpone the need for a more costly state universal service fund, it is important to not remove the universal service provision from existing state law. Accordingly, the Authority maintains that even if the proposed legislation is adopted and the TRAF is created, the existing statutes relating to universal service should be retained as a backstop to ensure the continued affordability of residential local rates throughout Tennessee.

FCC Access Reform

Access rates charged to carriers, and ultimately to consumers, come in the form of interstate and intrastate. The FCC has exclusive jurisdiction of interstate access rates and has already moved to drop this rate. When it reduced the interstate access rates, it compensated the local telephone companies by making the implicit revenue stream formerly contained in access rates explicit via a line item on consumers' bills. This approach is identical to the approach of the proposed legislation The FCC is considering additional alternatives for access charge reform. Primarily, the FCC is considering a mandate that would require that all local telephone companies reduce their switched access rates. How this revenue would be made up is not clear. If such a reduction is mandated for intrastate access, the local companies that depend on switched access revenues as a source of revenues to maintain current residential telephone rates may be forced to increase local residential rates in order to earn a fair rate of return. The establishment of the TRAF could serve as a helpful mechanism to have in place in case the FCC mandates such drastic switched access reductions. The TRAF can better prepare RLECs and telephone Cooperatives to cope with such a change.

Access Rate Reduction to IXCs

As stated herein, the establishment of the TRAF will substantially lower rates paid by IXCs and perhaps some wireless carriers to RLECs and telephone Cooperatives for use of their networks to complete long distance calls. There is no language within the proposed legislation that requires such cost savings to be passed along to consumers in the form of lower rates. In 2001, the General Assembly determined that long distance markets were sufficiently competitive and therefore removed all rate regulation for intrastate long distance rates. Since that time, long distance competition has continued to flourish as evidenced not only by the sheer number of long distance providers,[8] but also in the various types of long distance communications available such as wireless, VoIP and e-mail services.

C. **Recommendations**

Broadband

Section 1(b) of the bill states in part that, "the TRAF is established to promote the widest possible deployment and adoption of telephone and broadband service…" While the Authority believes the TRAF will help to ensure affordable telephone service to rural areas by improving the financial condition of RLECs and telephone cooperatives, the TRA does not believe the fund can or should be used to promote broadband. Deployment of broadband support should be portable and should be funded by revenue sources other than

[8] There are over 100 CLECs and 168 long distance resellers registered with the Authority providing long distance services in Tennessee.

regulated revenues generated by local rates or intrastate access charges. There are other efforts presently being made to promote broadband deployment in rural areas. The American Recovery and Reinvestment Act of 2009 includes initiatives aimed at deploying broadband through the United States. While the primary goal of the Act was to create jobs, it also allocated almost $5 billion in funding to support deployment of broadband infrastructure in unserved and underserved areas. The program is titled the Broadband Technology Opportunities Program and is administered by the National Telecommunications and Information Administration ("NTIA"), which is in charge of evaluating and dispersing available funds to states for broadband initiatives. There are numerous funding requests pending at the NTIA for deploying broadband infrastructure throughout Tennessee. These grants should be announced during the first quarter of 2010.

Many RLECs and telephone Cooperatives offer broadband as an unregulated service offering, funded in part from low interest loans from the Rural Utility Services (RUS). Competitive providers in Tennessee also continue to expand broadband infrastructure mainly in the more densely populated areas of the State. Competition for users of broadband services is becoming more and more competitive especially in these areas and providing a subsidy to only one provider of broadband services could serve to chill, over time, the competitive alternatives that might otherwise develop. And while the establishment of the TRAF should improve the revenue streams and cash flows of the RLECs and telephone Cooperatives, the Authority has no jurisdiction to ensure that utilities will use these potential funds to deploy broadband. Additionally, the funds received from the TRAF would go on the regulated books of the RLECs and would not normally be used to support an unregulated service such as broadband. If funding were established for broadband services, the commensurate jurisdiction would also have to be delegated to the TRA to monitor deployment and rates charged for these unregulated services.

For these reasons, the Authority recommends broadband support be eliminated from this legislation and that the focus should remain on maintaining local telephone rates at their current levels. The Authority supports the enactment of separate legislation to address broadband deployment, support and regulation. A separate statute would enable the General Assembly to establish a competitively neutral fund tailored to the state regulation allowed by federal law. This approach would be consistent with that of the Federal Communication Commission, which is currently evaluating whether to establish a separate fund for broadband deployment and support.

<u>Benchmark Rate/Sunset Provision/Phase-Out</u>

The TRAF should not establish an RLEC minimum benchmark rate for local service to qualify for reimbursement from the fund. In order to establish a benchmark rate or end user cap based upon the cost of service, it would be necessary to conduct a local service study for each RLEC and telephone Cooperative. Based upon previous dockets before this Authority, it has been demonstrated by the RLECs that cost studies of this nature are very expensive and would therefore substantially increase the revenue needs of the RLECs and telephone Cooperatives. Additionally, time would be needed for each company to perform the cost of service study, thus delaying the implementation of any TRAF legislation. The Authority, therefore, recommends that no benchmark rate be established.

Some respondents to the Authority's data request stated that there should be an end-date to the subsidy provided by the TRAF. Further, they claim that if a provider receives assistance from the TRAF, and then elects "Market Regulation," that provider should no longer be eligible for assistance from the TRAF.

Market Regulation was enacted to allow providers unfettered pricing flexibility in competitive markets. Market Regulation is permitted by statute because it was determined that certain exchanges are competitive. Because a carrier operating pursuant to Market Regulation can adjust its rates to respond to competition, the need for specific subsidies such as that from the TRAF would become unnecessary. Therefore it is appropriate to cease such TRAF assistance if the carrier elects Market Regulation. Of course, a carrier under Market Regulation can always re-elect Price Regulation, and would thereby be allowed access to the TRAF.

The Authority believes it is appropriate to continuously review the need for the TRAF. Alternative technologies within the communications market are rapidly changing and as the demand from rural customers for these alternatives increases, competition should develop in these markets in the near future. As competition eases its way into the rural areas it would be prudent to conduct a review of the TRAF to determine its continued viability. The usefulness of the fund may over time lose its relevance. A provision could be added to the legislation establishing a sunset provision and requiring the Authority to provide a report to the General Assembly prior to its consideration to sunset the TRAF. The report would contain a recommendation as to whether the TRAF should be continued and, if so, any recommended prospective changes. One additional safeguard should be added to require the TRA to establish a cap on the fund based upon the initial determination of the size of the fund. This cap would prevent growth of the fund.

Regulatory Accountability

The telecommunications industry in Tennessee is a mixture of carriers consisting of both regulated and unregulated entities. The regulated entities are required to provide or contribute to certain social and safety services including Lifeline, Link Up, Telecommunications Relay Services for the deaf and hard of hearing, the Telecommunications Devices Assistance Program for deaf, hard of hearing, speech impaired and other disabilities requiring technology assistance to use a telephone, and E-911 access. Telecommunication service providers outside of the Authority's jurisdiction, including telephone Cooperatives, also provide these services. A statutory requirement that these programs be provided would help ensure that all providers, whether regulated or unregulated, provide the same social services with similar quality to all Tennessee consumers. Therefore, the TRAF legislation should include a requirement that all companies receiving funds from the TRAF provide certain social and safety services.

Additionally, the legislation, as proposed, includes language that RLECs and telephone Cooperatives receiving support from the fund will be deemed “carriers of last resort for each provider’s respective service area.” As previously stated, the revenue stream provided to RLECs and telephone Cooperatives from this fund will make them financially stronger and should greatly assist in maintaining the existing levels of local rates. In return for receiving support from the fund, RLECs and telephone Cooperatives should be considered as carriers of last resort unless otherwise ordered by the Authority. For these reasons, this language should remain in the TRAF legislation.

Universal Contributions

The proposed legislation mandates that “Each provider that contributes to the Federal Universal Service Fund and provides services for a fee in Tennessee shall contribute to the TRAF.” Since all carriers should benefit from intrastate switched access reductions and/or general accessibility to the public switched network, this language should remain in the bill. Furthermore, Section 254(d) of the 1996 Federal Telecommunications Act requires “every telecommunications carrier that provides telecommunications services to contribute on an equitable and nondiscriminatory basis…to preserve and advance universal service.”[9] Therefore, the Authority recommends that if this legislation is enacted, all providers that contribute to the Federal Universal Service Fund should also contribute to Tennessee Rural Affordability Fund.

[9] 47 USCA, Section 254(d)

The current law, however, gives no jurisdiction to the Authority over wireless providers or local carriers under “Market Regulation” to collect data and assess TRAF fees. Further, there is no authority to impose fines on wireless providers or local carriers under “Market Regulation” for noncompliance. The Authority therefore recommends that this legislation be amended to include language providing this jurisdiction and authority for the limited purpose of assessing and collecting fees.

Existing Universal Service Statute

As previously mentioned, Tenn. Code Ann. § 65-5-107 provides the Authority with the ability to create a universal service fund in the event that the affordability of local service becomes threatened. The proposed TRAF legislation removes any jurisdiction granted to the Authority to establish a state USF. As proposed, the TRAF legislation changes the statute in such a way as to limit its coverage only to the consumers who are served by RLECs and Cooperatives. Since these providers represent only approximately twelve percent (12%) of Tennessee’s wireline consumers, the remaining eighty-eight percent (88%) would no longer have the protection of any statute providing for a state universal service fund.

As previously discussed, the Authority, when providing certification of ETCs to the Federal Communication Commission, continually monitors the affordability of rates and carrier of last resort obligations. Additionally, any mandated federal access reduction could place a burden on the local rates of telecommunication providers. For these reasons, it is recommended that should the proposed legislation establishing a TRAF be enacted, the current language contained in Tenn. Code Ann. § 65-5-107 should be retained; this language leaves in place the ability to maintain affordable rates for all Tennessee consumers.

Administration / Rulemaking

As previously recommended, the legislation should be amended to include language providing the Authority with jurisdiction for the limited purpose of collecting data, assessing and collecting fees, and disbursing the funds. In order to perform these functions, the Authority would need to establish procedures and criteria for the collection of data. Also, procedures and criteria would be necessary in order to assess, collect and disburse the funds. To enable the Authority to orderly and promptly carry out these duties, the legislation should provide specific rulemaking authority to the TRA for the purpose of establishing procedures and criteria for assessing, collecting and dispersing fees, and for monitoring the operation of the TRAF. The Authority would also need to have rules in place outlining the responsibilities of all companies, whether they are contributors or recipients. The Authority would then need to convene a rulemaking hearing and adopt rules to enable it to comply with any statutory mandate in the most timely and efficient manner. For these reasons, the effective date of significant parts of any legislation that may be enacted, other than rulemaking authority, should be delayed approximately one year to enable the Authority to establish, conduct and complete a rulemaking setting forth the procedures and criteria for the TRAF.

Attachment A

FILED
Date ____________
Time ____________
Clerk ____________
Comm. Amdt. ______

Amendment No.______________

____
Signature of Sponsor

AMEND Senate Bill No. 2147 House Bill No. 2117*

by deleting all language after the enacting clause and by substituting instead the following:

SECTION 1. Tennessee Code Annotated, Section 65-5-107, is amended by deleting subsections (b) through (e) and by substituting instead the following:

(b) The Tennessee Rural Affordability Fund ("TRAF") is established by this section in order to promote and assure the widest possible deployment and adoption of telephone and broadband service at rates that are affordable, and provide for reasonably comparable services and rates between rural and urban areas. The TRAF is critically important to preserving universal service and maintaining carrier of last resort obligations in rural areas of Tennessee. The TRAF shall be established and administered by the authority.

(c) The authority's jurisdiction over providers under this section is limited to the enforcement of the provisions as stated in this section, and not to be construed as granting additional regulatory authority over the contributing telecommunications and information service providers.

(d) The TRAF shall provide funding to the local exchange carrier serving as carrier of last resort provider using its own facilities within its study areas existing on January 1, 2009. Unless otherwise ordered by the authority, rural telephone cooperatives and incumbent local exchange carriers are deemed carriers of last resort for each provider's respective service area as of January 1, 2009.

(e) Affordable service shall consist of residential basic local exchange telephone service defined as the primary line servicing the end user customer premise, touchtone,

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access to 911, telecommunications relay system, toll presubsription, operator services and directory assistance, at affordable rates.

(f) Each provider that contributes to the Federal Universal Service Fund and provides services for a fee in Tennessee shall contribute to the TRAF.

(g) The authority shall determine the manner of contribution using either one or a combination of the following:

(1) A charge for each working telephone number; or

(2) A proportionate amount based on each provider's gross intrastate retail end user telecommunications revenues.

(h) The contributing providers may pass on a surcharge to their end user customers to recover the TRAF charge paid by the provider.

(i) The authority shall implement and administer the necessary processes and procedures for the administration of the TRAF including the determination of the assessment amount, collection of contributions and distribution of fund amounts. The costs of administering the TRAF shall be included in the fund amount. The authority has the power to require telecommunications service providers, voice over Internet protocol (VOIP) providers and domestic cellular radio service providers which contribute to the Federal Universal Service Fund to provide information to the authority necessary to establish and administer the TRAF. The authority has the power to fix charges levied by any telecommunications service provider for carrier access provided in this state and may order changes in such charges, subject to this section. The authority shall not require a telecommunications service provider to reduce its lawful rates for carrier access in effect on the effective date of this section except on revenue neutral basis, and any resulting rate changes necessary to comply with this section.

(j) The authority shall require the incumbent small local exchange carriers with less than one million (1,000,000) access lines and cooperatives to adjust intrastate (carrier common line and switched access) rates to their billed interstate rate levels in effect on December 31, 2009.

(k) The initial TRAF amount shall be determined by the difference between intrastate access rates in effect on December 31, 2009 and the interstate access rate levels in effect on December 31, 2009 multiplied by the intrastate access minutes for the twelve (12) month period ending December 30, 2008. Such rates shall include an administrative expense.

(l) Future intrastate access rate adjustments shall mirror the providers billed interstate access rate levels. The December 30, 2008 intrastate access minutes shall be the frozen base amount to which the access rate difference shall be applied. Such access rates shall include administrative expenses and shall be adjusted annually.

(m) The amount that each carrier of last resort provider as set forth in subsection (d) shall receive is based on the fund amount of intrastate switched access reductions made.

(n) The authority shall not require or conduct a rate case, earnings review or cost analysis in connection with the revenue recovery of the access rate reductions.

(o) To implement the fund, there is established a special reserve account in the state's general fund to be funded and allocated in accordance with the provisions of this section and rules promulgated by the authority. Such fund shall be known as the Tennessee Rural Affordability Fund. Moneys from the fund may be expended in accordance with such universal service program. Any moneys deposited in the fund shall remain in such account until expended for purposes consistent with such program and shall not revert to the general fund on any June 30. Any interest earned by deposits in such account shall not revert to the general fund on any June 30 but shall remain in such account until expended for purposes consistent with the universal service program.

SECTION 2. This act shall take effect upon becoming a law, the public welfare requiring it.

Current Residential Rates for RLECs and telephone cooperatives with less than 1 Milllion access lines in Tennessee

CENTURYTEL OF ADAMSVILLE

Exchange		Residential One party
Adamsville	$	12.67
Enville		12.67
Milledgeville		12.67
Shiloh		12.67
Touchtone		1.65

ARDMORE TELEPHONE COMPANY

Exchange		Residential One party
Ardmore	$	9.61
Mcburg		9.61
Minor Hill		9.61
Touchtone		1.00

CITIZENS TELECOMMUNICATIONS OF TENNESSEE OF TENNESSEE B/D/A FRONTIER

Exchange		Residential One party
Cookeville	$	10.25
Crossville		10.25
Dresden		10.25
Latham		10.25
Martin		10.25
McMinnville		10.25
Monterey		10.25
Palmersville		10.25
Pleasant Hill		10.25
Sharon		10.25
Sidonia		10.25
Sparta		10.25
Tansi		10.25
Touchtone		0.55

CITIZENS TELECOMMUNICATIONS OF THE VOLUNTEER STATE d/ba FRONTIER

Exchange	Residential One party
Claxton	$ 11.85
Powell	11.85
Rutledge	9.85
Tate Springs	9.85
Washburn	9.85
Touchtone	1.25

CENTURYTEL OF CLAIBORNE

Exchange	Residential One party
New Tazewell	$ 13.90
Sharps Chapel	14.90
Touchtone	1.75

CONCORD TELEPHONE COMPANY

Exchange	Residential One party
Concord	$ 11.85

Touchtone – Included as part of basic local exchange rate.

CROCKETT TELEPHONE COMPANY

Exchange	Residential One party
Alamo	$ 5.79
Friendship	5.79

Touchtone – Included as part of basic local exchange rate.

HUMPHREYS COUNTY TELEPHONE COMPANY

Exchange	Residential One party
New Johnsonville	$ 5.25

Touchtone – Included as part of basic local exchange rate.

LORETTO TELEPHONE COMPANY

Exchange	Residential One party
Ethridge	$ 13.35
Leoma	13.35
Loretto	13.35
St. Joseph's	13.35
Five Points	13.35
Touchtone	1.50

MILLINGTON TELEPHONE COMPANY

Exchange	Residential One party
Millington	$ 13.15
Rosemark	13.15
Shelby Forest	13.15
Drummonds	13.15
Mason	13.15
Munford	13.15
Stanton	10.15
Touchtone	1.50

CENTURYTEL OF OOLTEWAH-COLLEGEDALE

Exchange		Residential One party
Apison	$	11.85
Collegedale		11.85
Ooltweah		11.85
Touchtone		2.00

PEOPLES TELEPHONE COMPANY

Exchange		Residential One party
Erin	$	1.91
Henry		1.91
Tennessee Ridge		1.91

Touchtone -- Included as part of basic local exchange rate.

TELLICO TELEPHONE COMPANY

Exchange		Residential One party
Ball Play	$	11.95
Coker Creek		11.95
Niota		11.95
Riceville		11.95
Tellico Plains		11.95
Vonore		11.95
Englewood		12.85

Touchtone -- Included as part of basic local exchange rate.

TENNESSEE TELEPHONE COMPANY

Exchange		Residential One party
Bruceton	$	11.60
Clifton		11.60
Collinwood		11.60
Cornersville		11.60
Darden		11.60
Decaturville		11.60
Halls Crossroads		11.85
LaVergne		15.70
Linden		11.60
Lobelville		11.60
Mt. Juliet		15.70
Parsons		11.60
Sardis		11.60
Scotts Hill		11.60
Waynesboro		11.60

Touchtone – Included as part of basic local exchange rate.

UNITED TELEPHONE COMPANY

Exchange		Residential One party
Belfast	$	8.44
Chapel Hill		8.44
College Grove		8.44
Estill Springs		10.44
Flat Creek		8.44
Fosterville		8.44
Nolensville		13.94
Unionville		8.44
Touchtone		1.00

UNITED TELEPHONE SOUTHEAST d/b/a EMBARQ

Exchange		Residential One Party
Baileyton	$	17.95
Blountville		17.95
Bluff City		17.95
Bristol		17.95
Butler		17.95
Church Hill		17.95
Elizabethton		17.95
Erwin		17.95
Fall Branch		17.95
Greeneville		17.95
Hampton		17.95
Johnson City		17.95
Jonesborough		17.95
Kingsport		17.95
Limestone		17.95
Midway - Sullivan Co.		17.95
Midway - Washington Co.		17.95
Mosheim		17.95
Mountain City		17.95
Roan Mountain		17.95
Stoney Creek		17.95
Sullivan Gardens		17.95

1/ Includes Touchtone and LATA-Wide Toll Free Calling.

WEST TENNESSEE TELEPHONE COMPANY

Exchange		Residential One party
Atwood	$	1.11
Bradford		1.11
Rutherford		1.11
Trezevant		1.11

Touchtone -- Included as part of basic local exchange rate.

BEN LOMAND COOPERATIVE

Exchange		Residential One Party
Beech Grove	$	11.70
Beersheba-Altamount		11.70
Bon Decroft		11.70
Centertown		11.70
Dibrell		11.70
Doyle		11.70
Hillsboro		11.70
Laager		11.70
Mcminnville Rural		11.70
Monteagle		11.70
Old Zion		11.70
Pelham		11.70
Rock Island		11.70
Sparta Rural		11.70
Spencer		11.70
Tracy City		11.70
Viola		11.70

Touchtone - Included as part of basic local exchange rate.

BLEDSOE COOPERATIVE

Exchange		Residential One Party
College Station	$	11.70
Dunlap		11.70
Fall Creek Falls		11.70
Nine Mile		11.70
Pikeville		11.70

Touchtone - Included as part of basic local exchange rate.

DCT COMMUNICATIONS (Formerly Dekalb Cooperative)

Exchange		Residential One Party
Alexandria	$	12.75
Auburntown		12.75
Gordonsville		12.75
Liberty		12.75
Milton		12.75
Norene		12.75
Smithville		12.75
Temperance Hall		12.75
Woodbury		12.75
Woodland		12.75
Touchtone		1.50

HIGHLAND COOPERATIVE

Exchange		Residential One Party
Deer Lodge	$	9.73
Huntsville		9.73
Oakdale		9.73
Oneida		9.73
Petros		9.73
Robbins		9.73
Sunbright		9.73
Wartburg		9.73
Touchtone		0.95

NORTH CENTRAL COOPERATIVE

Exchange	Residential One Party
Bethpage	$ 14.90
Defeated	14.90
Green Grove	14.90
Hillsdale	14.90
Lafayette	14.90
Oak Grove	14.90
Pleasant Shade	14.90
Red Boiling Springs	14.90
Westmoreland	14.90
Scottsville Rural (KY)	14.90

Touchtone - Included as part of basic local exchange rate.

TWIN LAKES COOPERATIVE

Exchange	Residential One Party
Baxter	$ 10.50
Byrdstown	10.50
Celina	10.50
Chestnut Mound	10.50
Clarkrange	10.50
Cookeville South	10.50
Crawford	10.50
Gainesboro	10.50
Granville	10.50
Highland	10.50
Jamestown	10.50
Livingston	10.50
Moss	10.50
North Springs	10.50
Rickman	10.50

Touchtone - Included as part of basic local exchange rate.

WEST KENTUCKY COOPERATIVE

Exchange		Residential One Party
Cottage Grove	$	14.56
Cypress		14.56
Puryear		14.56

Touchtone - Included as part of basic local exchange rate.

YORKVILLE COOPERATIVE

Exchange		Residential One Party
Brazil	$	14.56
Mason Hall		14.56
Trimble		14.56
Yorkville		

Touchtone - Included as part of basic local exchange rate.

ATTACHMENT C

BILLED ACCESS MINUTES OF USE
2000 THROUGH 2008

TELEPHONE COMPANY A/		2004	2005	2006	2007	2008	
Ardmore	B/	5,078,039	5,224,010	5,117,574	4,972,633	4,260,173	
Century-Adamsville		15,676,445	12,699,457	11,272,386	11,504,590	12,232,598	
Century-Claiborne		16,045,492	14,943,336	14,287,489	13,342,470	12,433,504	
Century-Ooltewah-Collegedale		6,378,376	6,586,414	6,586,874	6,556,060	7,381,369	
Citizens of TN d/b/a Frontier		248,541,197	136,616,705	107,997,266	106,808,629	195,595,081	
Citizens-Vol St. d/b/a Frontier		42,034,084	23,876,256	28,122,035	32,873,108	28,653,624	
Concord		27,183,874	26,439,266	19,030,472	16,817,575	16,817,575	C/
Crockett		20,193,578	20,342,329	19,065,899	16,038,777	12,893,800	
Humphreys County		7,351,986	7,257,225	6,574,938	5,970,018	5,496,699	
Loretto		16,056,611	11,977,469	10,230,936	9,282,352	8,232,301	
Millington		22,920,024	21,940,232	21,994,026	22,227,623	19,352,717	
Peoples		20,952,128	23,479,294	26,458,906	22,819,583	20,171,156	
Tellico		27,014,563	24,979,472	21,052,404	16,323,341	16,323,341	C/
Tennessee Telephone		138,146,759	135,696,554	100,401,176	89,871,214	72,493,549	
United Telephone		39,845,499	34,525,591	32,978,411	39,359,872	36,203,338	
West Tennessee		18,034,567	18,367,852	17,349,463	14,392,377	8,116,682	
Total		671,453,222	524,951,462	448,520,255	429,160,222	476,657,507	

Source: Annual Reports filed with the TRA.

A/ Telephone cooperative data not available.
B/ Percentage of Ardmore, TN access lines to Ardmore, AL access lines * total switched access minutes.
C/ 2007 Data used.

ATTACHMENT D

ESTIMATED PAYMENTS RECEIVED FROM TRAF PER RESIDENTIAL LINE

TELEPHONE COMPANY A/		PAYMENT PER LINE RESIDENTIAL	ANNUAL PAYMENT
Humphreys County		$ 29.14	$ 426,660
Peoples Telephone		24.23	1,128,153
Crockett Telephone		17.92	590,394
United Telephone		10.80	1,695,728
West Tennessee		9.91	366,809
Tennessee Telephone		7.97	4,067,056
Loretto		7.96	423,206
Century Telephone Ooltewah-Coll.		7.91	471,633
Tellico		7.63	663,708
Concord		7.13	962,836
Century Telephone of Claiborne		6.94	540,385
Century Telephone of Adamsville		6.90	449,939
Citizens of TN d/b/a Frontier	B/	6.18	3,334,526
Citizens of the Vol State d/b/a/ Frontier		4.94	818,405
Ardmore		4.86	129,241
Millington		0.51	113,526
Total			$ 16,182,205

NOTE: Lost revenues and access lines based upon information contained in annual reports and other sources on file with the Tennessee Regulatory Authority.

A/ Data from cooperatives unavailable.
B/ 2007 data used.

ATTACHMENT E

ESTIMATED REVENUE LOSS PER RESIDENTIAL LINE BY REDUCING INTRASTATE ACCESS RATES TO INTERSTATE LEVELS

TELEPHONE COMPANY A/	Revenue Loss Per Res. Line
Humphreys County	$ 29.14
Peoples Telephone	24.23
Crockett Telephone	17.92
United Telephone	10.80
West Tennessee	9.91
Tennessee Telephone	7.97
Loretto	7.96
Century Telephone Ooltewah-Coll.	7.91
Tellico	7.63
Concord	7.13
Century Telephone of Claiborne	6.94
Century Telephone of Adamsville	6.90
Citizens of TN d/b/a Frontier	6.18 B/
Citizens of the Vol State d/b/a/ Frontier	4.94
Ardmore	4.86
Millington	0.51

NOTE: Lost revenues and access lines based upon information contained in annual reports and other sources on file with the Tennessee Regulatory Authority.

A/ Data from cooperatives unavailable.
B/ 2007 data used.