THE BACK PAGE

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W i r e l i n e – W i r e l e s s – B r o a d b a n d - C a b l e – V i d e o

HELP!!! THE RURAL TELCO INDUSTRY HAS BEEN RIPPED OFF BY FCC RULES TO THE TUNE OF OVER $17 BILLION - I HAVE FOUND THE FIX BUT, ACHIEVING IT DEPENDS ON YOU

By Larry Dale

(Larry Dale is the founder of ITCS, Inc., a consulting firm that has served the rural telecom community for over 20 years)

By my count, over 1,100 small rural telecom companies have been ripped off by over $17,000,000,000 in deficient federal USF funds. And, this amount is increasing every year, and will continue to increase --- that is unless you do something to stop it.

For each of your companies the losses of the last twenty years has been significant. To illustrate, see below the losses for two companies for the year 2021 that I have calculated. Their loses for one year could have paid for getting the problem fixed several times over and they would still have money left over!

I have calculated that the annual losses for the rate of return carriers is over $131,000,000 for 2021. Unless something is done now, the losses will continue to increase until USF revenues will go to zero and either your subscriber will be faced with increased rates to cover the high cost of providing universal service in your service area, or your company will be hit with what might be an insurmountable financial challenge.

Under the principles of rate of return regulation (that are still applicable though too often forgotten or ignored), the regulated company has a right to recover its reasonable expenses, return of investment (depreciation) and a reasonable return on investment. Obviously, that principle has not been followed; if it had been, or there would not be the rip-off of over $17 Billion.

Assuming (and I think it may be a big assumption!) that the Federal Communications Commission did its job and fulfilled its responsibilities without prejudice or bias against any region or class of service providers, the resulting rules and regulations would be in accordance with law and generally accepted regulatory theory. As a result, there would be no continuing "haircut" reducing the rural telecom industry's recovery of the legitimate costs of providing universal service.

The only explanation I find for the ongoing and growing $17 Billion haircut is that some regulators and other industry players simply believe that the rural industry receives too much cost recovery from the USF. Like me, you've probably heard them throw around the term "waste, fraud and abuse" in applying it to the high-cost USF support mechanism – but, you've never seen them identify pervasive industry-wide "waste, fraud and abuse" that warrants the arbitrary "haircut." In terms of real "waste, fraud, and abuse," someone should research how much money and resources the FCC has used in auditing rural telecom carriers, searching for "waste, fraud, and abuse" – all of their effort and wasted resources uncovered only a very few isolated instances that the FCC sanctioned. That's because there is no systemic "waste, fraud and abuse" in the rural telecom industry.

My calculation of the growing $17 Billion "haircut" deficiency in USF is based on the information and data provided in company cost studies that calculated revenue requirements in accordance with the FCC's established rules. Is the cost study wrong, are the rules wrong, are the separations wrong, or does the Commission pull data, slogans and policy out of thin air?

I have urged others for several years to take the lead on addressing this issue, but obviously no one did. I suspect that some in a position to lead and take action fear that the people at the FCC won't like them or invite them "to the table" to talk about policy formation if they are challenged. I brought up the issue to NTCA the Governmental Affairs and Separations Committee Meeting and was laughed at. Then I waited several more years, before I followed the leading of the Lord to stay in the office and work through the issues to get to the source of the problem, and I have spent a considerable number of hours getting to the source of the problem.

The fact that no one else has pursued this problem that is sucking the life out of the small companies shows how difficult and complex it was to get to the answer. The issue was very cunningly written so as to hide it in plain sight. If any of you were praying about how to handle this issue, the answer has been found. Please consider joining with other companies to sponsor a project to address the wrong to the entire rural industry. We just need several companies to take it before the Commission to get it properly adjudicated, and, if necessary, to go before the courts to seek correction of the wrongful FCC policies that fail to provide rural telecoms with recovery of their costs.

We have the law, we have the facts, we have logic, and we have generally accepted regulatory principles as well as jurisdictional separations rules supporting this position. This request should not require any additional cost study work. The past and current cost studies have all been accepted by the Commission as fair just and reasonable, and are utilized for the determination of rates.

I want to offer you more background and facts. But, if you've read enough and you're ready to consider joining in an effort to address this, please email me at depta@itcsinc.com

Though none of us should be stuck in the past, history (together with law, rules and regulations that still exist) can be helpful in understanding and addressing the issue. Do you remember or know about the days prior to the divestiture of the Bell Operating Companies from AT&T (January 1, 1984) in regards to how cost studies and settlement were handled? During that time every cost company received there intrastate and interstate settlements at 100% from the Bell Operating Companies operating in that Bell Operating Company area. AT&T with the approval of the FCC set the interstate toll rates for the country based on the interstate revenue requirement for all of the companies. The non- AT&T companies did not deal with the FCC except on special occasions for special purposes. The companies only dealt with rate of return issues on an intrastate basis, dealing with the Bell Operating Companies for toll and the State Commission for local as the interstate was all handled by AT&T.

January 1, 1984 brought about the significant changes to settlements for toll by a novation of contract previously from a contract with AT&T to a contract with NECA on the behalf of the FCC. Here we need to go over the basics of monopoly regulation. In monopoly or rate of return regulation the governmental agency contracts with a private company to provide public services to customers at fair, just and reasonable rates. From a theoretical stand point these fair, just and reasonable rates should approximate the cost of the service if provided competitively. The reasonableness of the rates is determined by a third party or contractor to the process, the neutral regulating governmental agency, which is the regulatory commission. The end result is intended to produce reasonable rates for consumers and full investment and cost recovery and a fair return on investment for service providers. The fair return on investment is not guaranteed but is in the purview of the management of the private company to seek via a rate case to recover the appropriate return on investment.

Under this process, the regulator is not supposed to favor the customer or the company, or one class of companies over another, but it should be neutral in all cases.

With respect to whether the process has reflected neutrality or prejudice, however, we need to look no further than what happened with the divestiture of AT&T from the Bell Operating Companies. The Bell Operating Companies at the time of divestiture had a significant number of employees (hundreds and thousands) that under regulation were deemed necessary for proper operations but in a competitive environment (marked by price cap regulation replacing rate of return regulation for large companies at their urging), many of those employees were no longer needed. So, with the deregulation those employees were terminated, producing savings of millions of dollars for the large companies. Of course, that made for a great example for the need for deregulation of the large companies. But who couldn't make money under those circumstances if they serve densely populated areas where technology evolution enabled the realization of cost efficiencies?

This narrow focus that ignores the realities of serving rural America essentially became accepted as the competitive model for proving the so-called benefits for deregulation. When we look at the application of this way of thinking to the treatment of the small companies, one of the first things that happened after divestiture was that the corporate operations expense was capped without any meaningful factual basis of the cost needs of operating in rural areas. I think that from the outset, the rural telephone companies were handicapped in addressing the FCC challenges. Prior to divestiture, the small companies did not have much experience or reason to deal directly with the FCC. The needed responses required multi-disciplinary skills and experience: knowledge of all aspects of jurisdictional separations, changes in regulations, the effects of separations and regulation on day-to-day operations while at the same time working against the knowledgeable AT&T lobbyists who had no commission established cap on corporation operations expense.

Prior to the divestiture and through the 1996 Telecom Act until around the year 2001, many changes were made in the rules and regulation. The Part 67 jurisdictional Separations was transferred to Part 36 and Part 69 was implemented to allocate the interstate jurisdictionally separated costs to various elements. However, during this period, a pool was set up and rules written for Universal Service which included the large Bell Operating Companies. So, while the small companies were receiving settlements from NECA, the small companies had little knowledge of the inter working of the pool other than of their own interaction with NECA. The current payment of USF was always based on costs that were two-years old; and individual small rural telecoms had little knowledge of NECA's interaction with the large companies.

Finally in 2001 all of the large carriers were removed from the NECA and USF fund process applicable to the smaller companies. With the removal of the large companies, and their related cost and usage data that had been incorporated into the NECA processes, it was much easier to see what was happening to our companies because there were no large swings caused by the large companies. If I am not mistaken, one of the members of the Joint Board recommended that the FCC and NECA maintain a record by company and by year of the USF information. As a result, we can now see quite quickly how our revenue requirements are not being met. For example, each rate of return company prepares a jurisdictional separations study input for NECA to develop the USF information and interstate access rates. Based on the input to NECA we can develop the following management information to show the amount of USF that you should have received in the last year, and how much you were shorted. The amount utilized in calculating the USF amount is transferred from the state to interstate via the additional interstate expense allocation (AIEA). Based on the input to NECA in 2021 we can develop the following:

Revenue Requirement	Company A Annual Amounts	Company A Per Month Per Loop	Company B Annual Amounts	Company B Per Month Per Loop
USF Total Unseparated	$13,069,139	$273.44	$27,040,805	$153.21

State ROR/ Interstate USF/AIEA	$8,943,916	$187.13	$17,112,501	$96.96
Interstate Common Line	$3,267,285	$68.36	$6,760,201	$38.30
Exchange	$857,938	$17.95	$3,168,103	$17.95
`	$0		$0	
State ROR/ Interstate USF/AIEA	$8,943,916	$187.13	$17,112,501	$96.96
USF Payments	$5,367,230	$112.29	$8,409,058	$47.64
Unpaid USF/State Rev Req.	$3,576,686	$74.83	$8,703,443	$49.31

As I noted at the outset, the rural telco industry has been ripped off by the rules of the FCC. I have analysis that demonstrates that companies in the aggregate have lost over $17 Billion in federal USF funding over the last 21 years or since the large Telephone companies were removed from the high-cost fund and the rate-of-return company high-cost fund was dedicated to the rural telephone companies. I have underlying data available from public sources whereby we can calculate what each company's losses in Federal funding has been.

IS THE USF BROKEN?

The answer to that question differs depending on who is answering the question! If AT&T and the large companies were asked, the answer is probably that it is not broken but working more as it should, but still in need of further trimming. However, if the small companies were asked, the answer would have to be that it is broken and the disrepair will drive their companies to very high local rates or into bankruptcy.

IS THE UNIVERSAL SERVICE FUNDING GOING AWAY?

The answer to that question may likely depend on what are you willing to do? USF is headed to zero in the not-too-distant future unless changes are made. The only parties in the telecom industry interested in avoiding this outcome are each of your companies. It is management's responsibility to see that the company maintains a reasonable return on regulated investment. It is also management's responsibility to see that the customers are receiving good service at reasonable rates, and that the company stays viable so the customer will have good service after the current management is retired. It is the board of director's responsibility to ensure that the management is doing their job. Just because a telephone company may be a cooperative or customer owned utility does not mean that the investors are not entitled to a reasonable return on investment

The revenue requirements shown above were calculated by NECA using a return on investment of 9.75%. Given that the USF unseparated revenue requirement is such a large portion of your company total revenue requirement, your return on investment should also be very near 9.75%; if it is not, then something is broken. If you are unwilling to act, then Universal Service Support will continue to be broken. However, if you want to get your full funding again, then I have a solution to help you.

But. . . I NEED YOUR HELP AS I DO NOT HAVE STANDING BEFORE THE COMMISSION; UNLIKE YOU AND YOUR COMPANY, I HAVE NO LOSSES or UNPAID REVENUE REQUIREMENTS

That means that I don't have the right (or standing) to take independent action to address this wrong; but I have worked for over 30 years for rural telephone companies. I believe in what they do, I care about them, and I want to help address this issue.

If you remember that in court filings made in 2000, and again in 2010 the courts did not adjudicate our issues because there were no loses proven by the small companies. Now we have losses and can prove them. In addition, I have reviewed many court orders and those with the same underpinning as this issue has, and all been adjudicated with outcomes that would support a successful outcome. Of course, no one can guarantee a successful outcome, but I can guarantee that doing nothing will guarantee a bad outcome.

I'm looking for 10 or more companies willing to initiate funding of a joint effort to resolve this issue by filing a petition for a declaratory ruling to determine if the Commission is required to abide by the laws, rules and regulations in question. I have completed a lot of the research and each piece indicates the Commission remains subject to the law, rules and regulations that would serve your company. I am not an attorney, but most attorneys do not have experience or understanding of the details about how jurisdictional cost studies and revenue requirements relate to these statutory provisions, regulations and rules in a way that should benefit both your companies and the communities you serve. I am ready to help the attorney chosen to complete the petition; most of the analysis has already been done and can be utilized as support and attachments to the filing. This is a huge issue for rate of return companies and it could be to A-CAM companies as well depending on how it is presented. Right now, without changes, many of your companies are on a racetrack to bankruptcy.

What Do You Think?

Please let me know, and please help me find out what other rural telecom companies think by passing this on to others who may not be subscribers.

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