

STATE OF ALASKA

THE ALASKA PUBLIC UTILITIES COMMISSION

Before Commissioners:

Sam Cotten, Chairman  
Alyce A. Hanley  
Dwight D. Ornquist  
Tim Cook  
James M. Posey

In the Matter of the Consider- )  
ation of Intrastate Universal )  
Service )  
 )  
\_\_\_\_\_ )

R-97-6  
ORDER NO. 10

**ORDER ISSUING NOTICE OF INQUIRY AND  
ESTABLISHING HEARING AND FILING SCHEDULE**

BY THE COMMISSION:

By previous Orders in this Docket, the Commission adopted rules governing the provision of universal service in Alaska. The adopted rules create an Alaska Universal Service Fund (AUSF) with two programs that went into effect on March 1, 1999: Lifeline and dial equipment minute (DEM) Weighting. Lifeline provides monthly support to subsidize local telephone service for low-income customers. DEM weighting, which is the focus of this Order, subsidizes the cost of switching equipment for certain telephone companies. DEM weighting support, by far the larger of the two programs (\$3,761,562), will account for approximately 91 percent of the AUSF (\$4,136,860) in 1999.<sup>1</sup>

---

<sup>1</sup>Other budget items comprising the AUSF include: Lifeline Support \$210,882 (5.1 percent) and administration \$164,416 (4.0 percent).

Prior to this year, DEM weighting support was paid by long distance companies to local exchange carriers (LECs) through charges for access to local networks when originating and completing long distance calls. The purpose of DEM weighting was to help keep local rates reasonable by subsidizing LECs that had high switching costs. However, the Federal Communications Commission (FCC) determined that collection of interstate DEM weighting support through interstate access charges constituted an implicit subsidy that is inconsistent with the federal Telecommunications Act of 1996<sup>2</sup> (The Act). This Commission found likewise with respect to intrastate DEM weighting and created the AUSF, in part, to continue this switching support in a competitively neutral manner consistent with The Act.

On March 23, 1999, the Commission Staff (Staff) submitted a memorandum (Report)<sup>3</sup> to the Commission questioning whether the entire amount of DEM weighting support (\$3,761,562) was necessary in order to maintain universal service. Staff noted that \$3,047,647 of the \$3,761,562 in 1999 DEM weighting support, or 81 percent of the total 1999 DEM weighting support, will go to five LECs with residential rates in the low to moderate range.<sup>4</sup>

---

<sup>2</sup>47 U.S.C. § 151 *et seq.*

<sup>3</sup>A copy of Staff's Report is attached to this Order as an Appendix.

<sup>4</sup>Specifically, the LECs (and amounts) in question include GTE Alaska Incorporated (\$957,744); Matanuska Telephone Association, Inc. (\$599,041); PTI Communications of Alaska, Inc. (\$535,836);  
(continued...)

Further, Staff noted that if intrastate DEM weighting support were eliminated for these five carriers, residential rates would still not exceed \$20 per month.<sup>5</sup> For example, Staff pointed out that if DEM weighting support were discontinued to TUA, local residential rates, currently \$9.49, would remain below the \$11 level.<sup>6</sup> In contrast, Bettles Telephone, Inc., which does not receive intrastate DEM weighting support, has local residential rates of \$27.90 per month.

Staff suggested that an intrastate universal service system that requires some customers paying \$27.90 per month to subsidize customers paying \$9.49 per month is not rational. However, Staff did not call into question the entire intrastate DEM weighting support program, noting that loss of support to United Utilities, Inc. (UUI), could possibly drive its local residential rate from \$19.23 per month to nearly \$30 per month.

Staff's Report recommended that the Commission issue a Notice of Inquiry in this Docket to investigate potential modifications to the DEM weighting portion of the AUSF.<sup>7</sup> Staff

---

<sup>4</sup>(...continued)  
Telephone Utilities of Alaska, Inc. [Juneau] (TUA) (\$411,716); and Telephone Utilities of the Northland, Inc. [Glacier State study area] (\$543,310).

<sup>5</sup>See, Staff Report, Table, p. 5.

<sup>6</sup>This assumes that loss of DEM support would be spread evenly between residential and business customers and that TUA is currently earning at its authorized rate of return.

<sup>7</sup>On March 25, 1999, UUI filed a petition in Dockets R-97-5  
(continued...)

further recommended that the Commission seek comment on four specific alternatives to the current system or any other feasible alternative.<sup>8</sup> The four alternatives include:

- modifying the existing DEM weighting program;
- replacing DEM weighting with support based upon an affordability standard;
- replacing DEM weighting with support based upon a utility's historic cost;
- replacing DEM weighting with support based upon a utility's forward-looking cost.

#### **Modify Existing DEM Weighting Program**

Staff suggested that the simplest and quickest fix to the problems associated with DEM weighting would be to leave the existing program substantially in place but to add criteria for receiving benefits. For example, rules could be adopted that would prevent an LEC from receiving intrastate DEM support unless it could show that local rates would, without support, exceed some

---

<sup>7</sup>(...continued)

and R-97-6 requesting that the scope of this Notice of Inquiry include the issue of the double counting of local minutes in the DEM calculation. UUI contended that the double counting of local minutes in the DEM results in an implicit subsidy to the inter-exchange carriers and overstates the amount of support shifted to the AUSF and requested that the Commission invite comment on the double-counting issue. By this Order, the Commission issues its Notice of Inquiry on potential modifications to the DEM weighting portion of the AUSF. The Commission invites comment on the four specific alternatives discussed in Staff's March 23, 1999, Report and any other feasible alternative and invites commentors to address the double-counting issue raised by UUI.

<sup>8</sup>Staff recommended that the Commission encourage commentors to include draft regulations along with their proposals.

predetermined benchmark rate level. Alternatively, the Commission could limit intrastate DEM support to LECs with fewer than 10,000 access lines. Staff noted that either of these changes could be accomplished with fairly simple changes to existing regulations.

### **Affordability**

Staff's second alternative involves adoption of an affordability standard. Affordability of rates is one of the universal service principles established by The Act,<sup>9</sup> and has previously been proposed as a standard for providing intrastate universal service support in Alaska. In October 1997, the Rural Coalition outlined such a plan in response to the Commission's initial Notice of Inquiry in this Docket.<sup>10</sup> The main features of the Rural Coalition's proposal were summarized by Staff as follows:

Under the Rural Coalition's plan benchmark levels would be set for both residential as well as simple or single-line business rates. The benchmarks could be based upon a national average with adjustments for affordability factors such as the higher cost of living in Alaska. The business benchmark would be some multiple of the residential rate (e.g., 150%). For example, the Rural Coalition used a hypothetical \$25 residential benchmark with a business benchmark of \$37.50.

The benchmark would establish a rate ceiling above which eligible LECs would not be allowed to

---

<sup>9</sup>"Quality services should be available at just, reasonable, and affordable rates." Section 254(b)(1), Telecommunications Act of 1996.

<sup>10</sup>Joint Reply Comment of the Rural Coalition, Dockets R-97-5/-R-97-6, October 22, 1997.

charge. Qualifying LECs would be eligible for intra-state universal service support for the amount above this level. In order to encourage efficiency the LEC would be limited to some percentage (e.g., 80%) of the amount [above] the benchmark. The Rural Coalition also proposed that eligible LECs be required to justify their costs through a rate proceeding before obtaining state universal service funding. In addition, in order to maintain the integrity of the system, the Rural Coalition proposed that the Commission 'require annual filings from companies receiving universal service funding to determine whether their costs are still sufficient to justify the funding or whether a new funding level is required.'<sup>11</sup>

### **Embedded Cost Model**

The DEM weighting system is based on factors that are applied to a utility's minutes data to increase the allocation of costs to state access. The existing formula assigns support regardless of the actual costs of the utility receiving support. As an alternative, the Commission could provide support based on whether an LEC's historic (embedded) costs were some percentage above the Alaskan average or based on some other formula.

### **Forward-Looking Cost Model**

Rather than using historic costs, the Commission could also determine a utility's costs, for universal-service purposes, on a forward-looking basis. This approach involves the use of a proxy model to estimate a utility's cost based certain factors such as size, location, access lines, etc. Proxy models also assume the use of current technology. The FCC has determined that

---

<sup>11</sup>Joint Reply Comment of the Rural Coalition, Dockets R-97-5/-R-97-6, October 22, 1997, p. 27.

forward-looking cost models are its preferred method for developing the amount of federal support that will be provided to eligible telecommunications carriers for universal service.<sup>12</sup> Staff notes that unless the State separately develops its own proxy model for Alaska, the use of proxy models for the distribution of universal service support is not likely to be available in the near term. As Staff stated in its March 23, 1999, Report:

As experience at the federal level has shown, development of a proxy model is not a simple task. Most of the effort to date, by the FCC, has been focused on developing a model for use with large urban LECs, not rural LECs (particularly not Alaska's rural LECs). This is not to suggest that no models have been developed for rural areas. Ben Johnson Associates has provided Staff with a proxy model prepared for use in Idaho. Staff has not reviewed this model to determine how much time and effort would be required to adapt it for use in Alaska. In any case this alternative, like the second alternative, is not likely to be a short term fix for the DEM weighting problem discussed above.

#### Discussion

At its March 24, 1999, Public Meeting the Commission considered the issues raised in Staff's Report. The Commission believes that Staff has raised valid concerns about continuing the current intrastate DEM weighting support system without modification. The Commission therefore seeks comment on the alternatives outlined by Staff's March 23, 1999, Report and any other feasible

---

<sup>12</sup>The Federal State Joint Board in CC Docket No. 96-45 has recommended that federal support be based upon some percentage of the difference between a benchmark level and a carrier's forward looking economic cost (assuming the carrier's costs exceed the benchmark level) with added support going to states based on need.

alternative. Parties recommending an alternative are encouraged to also submit draft regulations along with their comments.

### **Format of Filings**

The Commission requests that commentors provide an electronic copy of the comments (on diskette or by E-mail to apuc@apuc.state.ak.us) in Adobe Acrobat format (.pdf) format.

### **ORDER**

THE COMMISSION FURTHER ORDERS:

1. By 4 p.m., June 15, 1999, interested persons may file with the Commission written comments<sup>13</sup> on alternatives to the current intrastate DEM weighting universal service support program, as further discussed in the body of this Order.

2. By 4 p.m., July 15, 1999, interested persons may file with the Commission written comments in response to the comments filed pursuant to Ordering Paragraph No. 1 above.

3. Those individuals wishing to present oral comment at the public hearing scheduled below are requested to notify the Commission of their intent by 4 p.m., July 15, 1999.

---

<sup>13</sup>Since this is a regulation proceeding, commentors are not required to serve their comments on the other entities set out on the service list of this Order. However, interested persons may request copies of such from the Commission's Records & Filing Section at the address reflected in the left margin hereof.

4. A public hearing<sup>14</sup> in this proceeding is scheduled to convene at 9 a.m., August 9, 1999, in the Commission's hearing room at 1016 West Sixth Avenue, Suite 305, Anchorage, Alaska, for the purpose of taking public comment on alternatives to the current intrastate DEM weighting universal service support program, as further discussed in the body of this Order.

DATED AND EFFECTIVE at Anchorage, Alaska, this 30th day of April, 1999.

BY DIRECTION OF THE COMMISSION

( S E A L )

---

<sup>14</sup>If you are a person with a disability who may need a special accommodation, auxiliary aid, or service or alternative communication format in order to participate in this hearing, please contact Diane Hunt at 1-907-276-6222 or TDD 1-907-276-4533 at least two weeks before the hearing to make the necessary arrangements.