

**BEFORE THE  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554**

In the matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
A National Broadband Plan for our Future	)	GN Docket No. 09-51
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337

**COMMENTS OF GVNW CONSULTING, INC.**

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## TABLE OF CONTENTS

Executive Summary	3
Introduction	5
NOTICE OF INQUIRY ISSUES	6
<u>National Broadband Plan Model</u>	6
<u>Tribal and Hawaiian Home Lands need for separate treatment</u>	7
NOTICE OF PROPOSED RULEMAKING ISSUES	9
<i>Controlling the Size of the High-Cost Program</i>	10
<u>We oppose capping. If capping occurs, it should be initialized at 2012 levels in order to allow carriers to finish current projects</u>	10
<u>The attachments included with this filing show the damaging impact of any capping of USF amounts on both a per-line as well as a total company study area basis</u>	10
Data sample used	11
Description and results of per-line freeze price out	12
Description and results of study area freeze price out	13
Attachments for this comment filing	13
<i>Specific Steps to Cut Legacy High-Cost Support</i>	15
<u>Rural carriers should continue to be regulated via rate-of-return regulation</u>	15

## ATTACHMENTS

Four files in PDF format, with Excel version to be provided to FCC WCB Staff under separate cover

## **EXECUTIVE SUMMARY**

We recognize that the Commission desires comprehensive USF reform and seeks to redirect legacy USF support to supporting broadband infrastructure deployment in unserved areas, or to areas “that depend on universal service support for the maintenance of existing broadband service.” We respectfully submit that a prudent public policy outcome will fully recognize providing this type of maintenance support to rural carriers in order to maintain the cornerstone of rural broadband infrastructure.

We anticipate supporting the comments addressing the Model that will be filed by the joint rural wireline association effort. We find it necessary, however, to offer one initial comment at this time. Because the Commission posture surrounding the NBP stressed transparency, the public should be given access to the actual model the Commission used for testing and analysis.

We believe that the special circumstances involved in providing service to the Hawaiian Home Lands require an alternative approach. The provider for the Hawaiian Home Lands (HHL) is Sandwich Isles Communications, Inc. (SIC). SIC faces some extreme challenges in providing service on the HHL.

We have provided four attachments that provide detailed price out information based on **publicly-available data** for 822 companies. The purpose of these price outs is to provide illustrative results of the FCC proposals using historical data that has been filed with the FCC by the Universal Service Administrative Company (USAC). The price out illustrates how the FCC’s proposed approach works contrary to certain of the Commission’s goals. The effects of the FCC’s proposed approach create winners and losers in an effort where it will take all winners to successfully deploy broadband in rural

America. It also raises several policy issues that need to be addressed and resolved prior to the FCC taking any action.

In the last decade, ROR carriers have begun to deploy broadband infrastructure in rural areas and price cap carriers have not. And now, the proposal is to shift away from a successful regulatory scheme to one that does not incent building infrastructure. The proposed CAF mechanism appears to have only a short-term focus for rural carriers with the proposed 4Mbps target. Absent significant changes, the proposed recommendations of the FCC will eliminate the companies who have already invested to achieve the goals of universal broadband under a rate of return regulatory regime.

Rural carriers have in fact deployed the foundation for the broadband platform in rural America. In order to do this, it has been necessary to borrow funds and commit to making timely payments to lenders such as the United States Department of Agriculture Rural Utilities Service as well as private lenders such as CoBank and RTFC. The applause for the rural carriers must also be shared with these lenders who provided the debt funding that enabled the broadband plant to be built, based in part on the assurance that rate of return regulated companies in high cost to serve areas would meet their loan obligations.

We respectfully request that as this important universal service reform is developed, the circumstances related to meeting the needs of customers in high cost to serve rural areas are carefully evaluated and factored into any reform effort.

## INTRODUCTION

With this Notice of Inquiry (NOI) and Notice of Proposed Rulemaking (NPRM), the Commission has taken an initial step toward crafting a national broadband universal service strategy. We recognize that the Commission desires comprehensive USF reform and seeks to redirect legacy USF support to supporting broadband infrastructure deployment in unserved areas, or to areas “that depend on universal service support for the maintenance of existing broadband service.”<sup>1</sup> We respectfully submit that a prudent public policy outcome will fully recognize providing this type of maintenance support to rural carriers in order to maintain the cornerstone of rural broadband infrastructure.

GVNW Consulting, Inc. (GVNW) is a management consulting firm that provides a wide variety of consulting services, including regulatory and advocacy support on issues such as universal service, intercarrier compensation reform, and strategic planning for communications carriers in rural America. We are pleased to see the formulation of a unified rural wireline industry position and anticipate supporting the comments that will be filed by this group on or around July 12, 2010.

In a May, 2010 telecommunications conference<sup>2</sup>, Senator Byron Dorgan clearly captured the rural challenge by noting that rural America is “*often left behind*” by policies implemented by the federal government and added that: “*America is not about two cities where a plane takes off and another one lands. There is a lot of country in between.*” In the attachments we have included with this filing, we demonstrate the impacts on the companies that serve “the country in between” those two big cities. It is important for

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<sup>1</sup> Federal Communications Commission, *Connecting America: The National Broadband Plan*, released March 16, 2010, (National Broadband Plan – NBP), at 144.

<sup>2</sup> Conference sponsored by the Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO) and the Western Telecommunications Alliance (WTA), Washington, D.C., May 18, 2010.

policymakers to understand the impact on the individual providers that are serving the rural and remote customers. As noted in the May 3, 2010 joint association<sup>3</sup> letter to

Congress:

*Since the early 20<sup>th</sup> century, many of the industry's largest telecom providers chose not to invest in facilities to provide basic telephone service in the geographic areas of the United States that are the most economically challenging to serve. These areas consist of the most rural, insular, and sparsely populated areas of the nation, such as the Northern Plains, Appalachian and Rocky Mountains, Southwestern Deserts, Central and Mid-Western farmlands, Native American reservations and the frozen tundra of Alaska.*

We respectfully request that as this important universal service reform is developed, the circumstances related to meeting the needs of customers in high cost to serve rural areas are carefully evaluated and factored into this reform effort.

## **NOTICE OF INQUIRY ISSUES**

The Commission is utilizing a Notice of Inquiry approach to begin an analysis of what type of modeling is appropriate for the universal service reform effort.

### National Broadband Plan Model

We anticipate supporting the comments addressing the Model that will be filed by the joint rural wireline association effort. We find it necessary, however, to offer one initial comment at this time. Although the Commission's posture surrounding the NBP stressed transparency, the Commission's actual model has not been released to the public for testing and analysis. The Commission's model needs to be released to the public.

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<sup>3</sup> National Telecommunications Cooperative Association (NTCA), OPASTCO and WTA letter to Congressional delegation, May 3, 2010. page 1.

Tribal and Hawaiian Home Lands need for separate treatment

In the Notice of Inquiry section at paragraph 13, the Commission asks in part:

*“and specifically ask whether there are any unique circumstances in Tribal lands that would necessitate a different approach. (Cite fn46) Similarly, we request comment on whether there are any unique circumstances in insular areas that would necessitate a different approach. Similarly, we request comment on whether there are any unique circumstances in insular areas that would necessitate a different approach.”*

In the last sentence at the referenced footnote 46, the Commission states:

*“Although Native Hawaiians are not currently members of federally-recognized Tribes, we also seek comment on whether there are any unique circumstances that would warrant an alternative approach in Native Hawaiian Homelands.”*

We believe that the special circumstances involved in providing service to the Hawaiian Home Lands (HHL) require an alternative approach. The story of providing service to the HHL is nine decades in the making. The Hawaiian Homes Commission Act (HHCA) of 1920 reserved slightly over 200,000 acres of public lands in the Territory of Hawaii for homesteading by native Hawaiians. Known today as the HHL, these 69 non-contiguous parcels are located on the six major Hawaiian Islands. Founded in 1995, the communications provider for the Hawaiian Home Lands (HHL) is Sandwich Isles Communications, Inc. (SIC). SIC was formed to provide modern communications infrastructure and services in an environment where GTE had previously required significant contributions in aid of construction to offer basic services.

SIC faces some extreme challenges in providing service on the HHL. The geographic areas served by Sandwich Isles Communications are non-contiguous and insular characterized by rugged terrain – volcanic rock, coral, and sand, which makes terrestrial and submarine fiber placement a significant challenge. Hawaii is home to over

50% of the nation's endangered species which require specific and very expensive Federal and State mandated mitigation measures. Additionally, the tropical climate adds costly challenges to the ongoing operations and maintenance of a communications system.

The high cost of insular transport has been particularly problematic for Sandwich Isles. As noted in its 2006 filing<sup>4</sup>: *“Just the high cost of transporting communications services to consumers in remote areas of Hawaii and Alaska has the potential to make telephone service either unaffordable or unavailable. A lack of quality communications infrastructure will perpetuate an isolated existence for consumers residing in these remote areas. It will slow economic development and lessen overall quality of life, including access to healthcare and education. It will also threaten personal safety during periodic times of natural crises, which might include ...tropical hurricanes. In sum, without quality infrastructure, a connection to the broader community, and most certainly a global community, will be absent, taking away the opportunity for Hawaiian and Alaskan communities to grow and develop through participation.*

*In addition, the strategic location of these states makes availability of a robust communications network critically important to national security. The nation can ill afford to short-change the deployment of some of the nation's most critical infrastructure. A broadband communications network in Hawaii and Alaska must be available to drive our nation's defense systems.”*

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<sup>4</sup> Comments of Sandwich Isles Communications, Inc., TelAlaska, Inc., Yukon Telephone Company, Inc., et al, CC Docket No. 96-45 and WC Docket No. 05-337, March 27, 2006, pages 18-19.

## NOTICE OF PROPOSED RULEMAKING (NPRM) ISSUES

The NPRM seeks comment on what the Commission calls “common-sense reforms to cap growth” in the legacy high-cost support mechanisms in order to shift savings toward broadband communications. What is as important as to what will be discussed in this NPRM is what is not being discussed at this juncture. For instance, issues such as comparably defining broadband access for both urban and rural areas, whether we as a nation, both urban and rural, will continue to enjoy carrier-grade service and the inherent 99.999% reliability<sup>5</sup>, are not raised.

In addition, intercarrier compensation issues that from a rural carrier viewpoint are intertwined with USF reform have been deferred to later in the process. In its July 17, 2008 petition<sup>6</sup> at page 28, what AT&T offered as a foundational basis for assessing access charges is the fact that one of the Commission’s primary objectives with respect to access policy, in place for nearly two decades, “*has been to assess access charges on all users of exchange access, irrespective of their designation...*”<sup>7</sup> Access charges assist in paying for the infrastructure<sup>8</sup> that everyone<sup>9</sup> uses.

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<sup>5</sup> See, for example, Associated Press news story of May 25, 2010; Widespread outage for AT&T’s digital phone lines: “*AT&T’s new digital home phone service failed across the country Tuesday, illustrating continuing reliability issues with Internet-based phone service.*”

<sup>6</sup> This particular petition generated the comment and reply process in WC Docket No. 08-152.

<sup>7</sup> 6 FCC Rcd 4524, paragraph 54.

<sup>8</sup> One of the reasons that universal service is working today is that virtually all customers are accounted for within some eligible carrier’s service territory. These “carriers of last resort” (COLR) stand ready to serve even the most remote and isolated customers. But, this universally available service comes with a cost. Specifically for rural carriers, in a rate-of-return regulatory environment, the overarching principle that the Commission should adhere to is that rate-of-return carriers are entitled, as a matter of law, to a full recovery of their costs in providing interstate (access) services.

<sup>9</sup> The mobility provider depends on the wireline provider in its call completion architecture. Current wireless, VoIP, and satellite networks require a backhaul fiber connection to land line infrastructure to provide full functionality. This network reality is documented in *Wireless Needs Wires: The Vital Role of*

### ***Controlling the Size of the High-Cost Program***

We oppose capping. If capping occurs, it should be initialized at 2012 levels in order to allow carriers to finish current projects

Our review of the language in Chapter 8 of the National Broadband Plan indicates an understanding of the need for an adequate transition from legacy USF support:

- Page 141: *“The reforms must be achieved over time to manage the impact on consumers, who ultimately pay for universal service.”*
- Page 142: *“...should recognize that ICC revenue is an important part of the picture for some providers.”*
- Page 143: *“No flash cuts. New rules should be phased in over a reasonable time period. Policymakers must give service providers and investors time to adjust to a new regulatory regime.”*
- Page 151: *“The FCC’s ability to shift funds from existing programs to broadband assumes that shifting the identified money from voice service to broadband will not negatively impact company operations or future deployment strategies.”*

The attachments included with this filing show the damaging impact of any capping of USF amounts on both a per-line as well as a total company study area basis

We are pleased to be part of the unified rural wireline industry effort which will soon place specific numerical data into this record. This process involves an extensive data request to individual carriers, many of which are our client companies. In the course

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*Rural Networks in Completing the Call*, published by the Foundation for Rural Service in March, 2006. This paper states in part: *Without thoughtful consideration by policymakers of the challenges of providing wireless services in rural America, as well as the dependence of wireless services on wireline networks, portions of the nation are likely to remain underserved . . . Most importantly, one must recognize that without the underlying wireline network, wireless networks could not exist in their current form. In spite of this obvious fact, large wireless carriers and policymakers alike continue to pursue practices and policies that will in fact undermine the critical wireline network. While discussions on how to modify reciprocal compensation, access charges, and universal service continue, attention must be placed on ensuring these mechanisms are capable of maintaining the fiscal health of that wireline network.*

of preparing for these data requests, our clients have posed several questions<sup>10</sup> to us that have created the need to develop the data included in the four attachments to this filing. This data serves as only an initial data point, and is meant to complement the projected data that we expect to be filed in July in the joint industry filing.

At paragraph 52 of the NPRM, the question is posed: “*Should the Commission freeze per-line support for each carrier at 2010 levels?*” This paragraph also seeks comment as follows: “*Alternatively, should the Commission freeze the total amount of support a carrier receives in a particular study area at 2010 levels?*” The purpose of these price outs is to provide illustrative results of this approach using actual data that has been filed with the FCC by USAC. We believe the price outs illustrate how each of these approaches work contrary to certain of the Commission’s goals and how it creates winners and losers. It also raises several policy issues that need to be addressed prior to the adoption of this type of action.

### **Data Sample Used**

In order to illustrate the potential impact of the NPRM recommendations, we used publicly-available USAC filed data from 2003 and 2008. The sample data was derived from the HC-01 schedule for the support amounts for each of the years. The fourth quarter monthly support amounts for High Cost Loop (HCL), Local Switching Support (LSS), and Interstate Common Line Support (ICLS) were annualized for purposes of this price out. The loop counts for each year were taken from the fourth quarter HC-05. The price out was performed on the study areas that were identified as rural carriers on a cost

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<sup>10</sup> Questions have included, but are not limited to: “How will I determine whether my projected data compares to what would have happened if the rules had been in effect for the prior five years?”; “Will the data presented to the FCC be responsive to the request that I have heard at industry conventions this spring from WCB personnel for the data to be shown on a per company basis?”

basis of settlement. The price out only included those companies that appeared in the report for both 2003 and 2008. A separate price out was made for each of the three mechanisms (HCL, LSS and ICLS), and then a summary was created combining the three mechanisms. The data for 822 companies was then sorted by line size groups as follows:

Under 10,000 loops	593 Companies
10,001 to 20,000 loops	106 Companies
20,001 to 50,000 loops	68 Companies
Over 50,000 loops	55 Companies

Within each group, the companies were sorted based on their loss or (gain) per loop.

**Description and results of per-line freeze Price Out**

The 2003 support per line (loop) was calculated for each carrier in the sample. The support per line was then multiplied by the number of loops for 2008. The resulting support amount was then compared to the annualized support reported by USAC for the fourth quarter of 2008. The loss or (gain) from the adoption of the frozen amount per line was then shown on both a total study area basis and on an annual per loop basis.

Following is a quick recap of the losers<sup>11</sup> and winners by group:

<b>Company Size - Loops</b>	<b>Number of Losers</b>	<b>Number of Winners</b>
Under 10,000	463	130
10,001 – 20,000	75	31
20,001 – 50,000	32	36*
Over 50,000	23	32**

- \* Includes 3 companies that break even
- \*\* Includes 13 companies that break even

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<sup>11</sup> Under current rules and regulations, all of the federal support from HCL, LSS, and ICLS go to the recovery of costs that are assigned to the interstate jurisdiction. The recovery of the costs associated with the loss in support must be addressed and the mechanism must be consistent with Congressional and Commission policy. Is the Commission going to attempt to shift the burden of recovery of the lost support to the state jurisdiction by way of changes to the Jurisdictional Separations process? Since many states are in the process of trying to bring certain rates down, how will the states be able to handle the additional burden of the cost shifts to the state jurisdiction?

In the group of companies with fewer than 10,000 loops, there are 18 companies that experience a loss of cost recovery in excess of \$100 per loop per month.

**Description and results of study area freeze Price Out**

The 2003 support was calculated for each carrier in the sample. The resulting support amount was then compared to the annualized support reported by USAC for the fourth quarter of 2008. The loss or (gain) from the adoption of the frozen amount per study area was then shown on both a total study area basis and on an annual per loop basis. A separate price out was made for each of the three mechanisms, and then a summary was created combining the three mechanisms.

Following is a quick recap of the losers and winners by group:

<b>Company Size - Loops</b>	<b>Number of Losers</b>	<b>Number of Winners</b>
Under 10,000	419	174
10,001 – 20,000	67	39
20,001 – 50,000	23	45*
Over 50,000	21	34**

\* Includes 3 companies that break even

\*\* Includes 13 companies that break even

In the group of companies with less than 10,000 loops, there are 20 companies that experience a loss of cost recovery in excess of \$100 per loop per month.

**Attachments for this comment filing**

We have included four of our ten price outs with this comment filing, two related to the analysis of the freezing USF on a per line basis and two related to the analysis of the alternative of freezing USF on a study area basis. A price out of freezing each of the three USF mechanisms was computed, and two summary files were calculated. The first summary file contains the combined impact of freezing the three mechanisms sorted by line size and impact per line, and the second summary file includes the same information

as the first but is sorted by state in the same manner as the HC-01 and HC-05. File names of the attachments to this filing are noted below:

<u>Per Line analysis</u>	<u>Per Study Area Analysis</u>
<b>Summary Sorted.pdf</b>	<b>Study Area HCL LSS ICLS Sorted.pdf</b>
<b>Combined HCL LSS ICLS.pdf (by state)</b>	<b>Study Area Summary HCL LSS ICLS.pdf (by state)</b>

In the charts above, we have identified companies as winners and losers. The winners are those companies whose support at the frozen level is more than sufficient to handle the support requirement as identified under current rules **in the single year analyzed**. These companies would not have to seek rate increases for other interstate services to make up for the loss in support for that particular year. The losers are companies whose loss in support causes a shortfall in interstate revenue that must be made up through increasing other interstate rates. With rural rate of return companies, the investment is generally “lumpy.” In other words, investment to upgrade facilities occurs over a short period of time, and then remains in service for a long period of time. Therefore, there are spikes in the investments over the years. If a company has made its major investments just prior to the freeze, they might not be impacted until their next plant upgrade. In some cases, companies that are in need of upgrades will have a lower frozen support level which will be insufficient to make the needed investments.

### ***Specific Steps to Cut Legacy High-Cost Support***

In the last decade rate-of-return (RoR) carriers have begun to deploy broadband infrastructure in rural areas and price cap carriers have not. And now, after the rural RoR carriers' initiative, the FCC proposes to shift away from a successful regulatory scheme to one that does not incent building infrastructure and that will put many rural carriers out of business. The proposed CAF mechanism appears to have only a short-term focus for rural carriers with the proposed 4Mbps target which simply exacerbates the digital divide.

### **Rural carriers should continue to be regulated via rate-of-return regulation**

In his statement that accompanied this instant NPRM, Commissioner Copps offered the following observation:

*While we often rightly complain about the lapses, we should also recognize the achievements. Regardless of where the funding comes from, I commend those providers who have made broadband deployment a priority. For example, a lot of small rural telcos often went where others feared to tread and brought broadband to some pretty remote places. Their efforts should be not only recognized, but applauded.*

“Applause” is not adopting measures that will put rural carriers who had already started their own broadband initiative out of business. Rural carriers have in fact deployed the foundation<sup>12</sup> for the broadband platform in rural America. In order to do this, it has been necessary to borrow funds and commit to making timely payments to lenders such as the United States Department of Agriculture Rural Utilities Service as well as private lenders such as CoBank and RTFC. The applause for the rural carriers must also be shared with these lenders who provided the debt funding that enabled the

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<sup>12</sup> If the determination is made that embedded investments which were made under rate of return regulation are not to be supported under a new regulatory (incentive regulation) regime, what plans are going to be put in place to allow companies to recover their costs incurred under the rate of return regime which limited the recovery periods?

broadband plant to be built, based in part on the assurance that rate of return regulated companies in high cost to serve areas would meet their loan obligations.

Concomitant with these loan obligations, rural carriers have contractually committed to meeting certain financial ratios for the term of their loan. These financial ratios include, but may not be limited to: current ratio; debt service coverage ratio<sup>13</sup> (DSC); leverage ratio; minimum net worth test<sup>14</sup>; and times interest earned ratio (TIER).

The TIER test is one of the most common, and perhaps easiest to explain. The TIER is calculated for each year by comparing (a) total net income or margins plus interest expense payable for any year divided by (b) interest expense payable for each year. The minimum TIER that is required is equal to at least 1.0. In some cases, the TIER may be at a level of 1.0 for the first several years of the loan, and then increase to 1.35 for a short period of time, with then being at a level of 1.5 in each period for the balance of the loan. Simply stated, the lender requires the borrower to have a net income or net margin to avoid defaulting on the loan.

We are preparing an attachment for later submission that shows the impact for a sample of companies of removing current legacy USF support on the interstate TIER. Early data gathered so far indicates that unless these carriers are able to transition seamlessly to the CAF support system or some other recovery system, the majority of them will be in technical default on their loans within the first full year of implementing

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<sup>13</sup> Debt service coverage ratio for any year typically means (a) total net income or margins plus depreciation and amortization expense and interest on long-term debt for such year, divided by (b) principal and interest on long-term debt payable in such year, as calculated on a consolidated basis for the Borrower and all of its subsidiaries. This is often set at 1.25 to 1.

<sup>14</sup> Minimum Net Worth Test shall be calculated on a consolidated basis for the Borrower and all its subsidiaries, and shall mean an equity to total asset ratio of at least forty percent (40%). Equity shall be determined by subtracting total liabilities from total assets.

the CAF and others will go into default and fail later. In this scenario, there are no winners, but only losers.

We do not believe that this is a sound public policy result. It would appear that at least part of the desire of the NPRM proposal to shift rural carriers to incentive regulation (specifically price cap) is offered in order to provide a legal basis to freeze ICLS, delink access rates from revenue requirements, and possibly reduce any payments offsetting reductions in access charges. An FCC price cap regulation<sup>15</sup> approach traditionally bases price changes on a factor reflecting estimated productivity gains offset by generalized cost increases reflected by some form of price index. It is difficult to understand how rural carriers serving high-cost-to-serve territory<sup>16</sup> will be able to deliver quality broadband services while at the same time meeting price cap productivity targets. Incentive regulation for rural carriers would incent minimal levels of capital deployment, maintenance, and customer service.

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<sup>15</sup> The current incentive in the rate of return regime is that a company is allowed the opportunity to recover its expenses and earn a reasonable return on its investment. If the Commission reneges on this incentive by forcing the replacement of the current incentives with an alternative incentive plan, how much confidence will there be in the FCC's commitment to follow through with any incentives offered?

<sup>16</sup> If an incentive regulatory plan is to be adopted, what actions are going to be incented? Price Caps provide an incentive to limit investment in rural areas. As can be seen from the record, this spurred many of the price cap companies to sell off their high cost rural areas or simply not keep their equipment up-to-date with current technology.

GWNW Consulting, Inc.  
Comments in WCD No. 10-90, GND No. 09-51, WCD No. 05-337  
June 3, 2010

Respectfully submitted,

*Submitted via ECFS*

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