Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 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
	)	
Establishing Just and Reasonable Rates for Local Exchange Carriers	))	WC Docket No. 07-135
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Developing a Unified Intercarrier Compensation Regime	))	CC Docket No. 01-92

COMMENTS
of
CENTRAL TEXAS TELEPHONE COOPERATIVE

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Introduction and Summary

The Federal Communications Commission's (Commission) NPRM[1] in the above-captioned proceeding requests comment on proposed rules intended to modify the existing rules on the Universal Service Fund (USF) and Intercarrier Compensation (ICC).

Central Texas Telephone Cooperative[2] (Central Texas) submits these comments for the FCC's consideration. Central Texas is a rural telecommunications provider serving 6,892 voice access lines and 4,696 broadband customers in the state of Texas. The following characteristics are true of Central Texas:

- Central Texas is the Carrier of Last Resort designated by the Public Utility Commission of Texas, which legally obligates the company to provide telecommunications service to all requesting customers within its service territory.

- Central Texas is the Eligible Telecommunications Carrier (ETC) determined by the Public Utility Commission of Texas to provide universal service within the company's designated service territory.

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[1] *Connect America Fund*, WC Docket No. 10-90, *A National Broadband Plan for Our Future*, GN Docket No. 09-51, *Establishing Just and Reasonable Rates for Local Exchange Carriers*, WC Docket No. 07-135, *High-Cost Universal Service Support*, WC Docket No. 05-337, *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Lifeline and Link-Up*, WC Docket No. 03-109, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, FCC 11-13 (rel. Feb. 9, 2011) (*NPRM*).

[2] Central Texas Telephone Cooperative is located in the geographic center of Texas. The terrain varies significantly throughout the 3,000 mile serving area. There is a small portion that is relatively flat farm land but the majority of the serving area is hills. There are many residents that are very remote and several miles from their closest neighbor or town. Central Texas is 80-100 miles from any significant population center. There are no significant economic drivers in the Central Texas area. The farming and agriculture business employees few people and at a very low pay rate. Recreational hunting brings in a lot of people to the area throughout the year but does not necessarily create jobs.

- Central Texas receives High Cost Support from the Federal Universal Service Fund. This support totaled $7,367,049 in 2010 and comprised over 48.17% of Central Texas revenues in 2010. Support came from the following sources:

    - High Cost Loop Support (HCLS) $4,621,533
    - Interstate Common Line Support (ICLS) $2,371,656
    - Local Switching Support (LSS) $373,860

- Central Texas generates substantial revenues from providing intrastate switched access services. In 2010 intrastate switched access revenues totaled $1,279,431.

- Central Texas provides voice and broadband services to schools, libraries, rural health care facilities, governmental agencies, and other anchor institutions within its service territory. Central Texas has worked with 8 schools in the service area providing distance learning and connectivity to a college for over 15 years. This helps the schools to share teaching resources and offer college credit classes to high school students.

- Central Texas is one of the, if not the, largest employers in the company's rural service territory, providing jobs and financial stability in rural areas of Central Texas. In 2010, Central Texas employed 70 people and provided combined payroll and benefits of $4,755,000. A good example as to the importance of Central Texas as an employer in the community happened recently, where a job posting for one Customer Service Representative, one of the lowest paid positions in the Cooperative, had 48 applicants from the area.

- Central Texas has deployed substantial financial and human resources to provide voice and broadband services under the existing rate of return rules prescribed by the FCC and by the Public Utility Commission of Texas. In 2010, Central Texas had:

  - Regulated rate base $25,042,445
  - Long term debt $10,953,404
  - Annual debt payments $2,238,922
  - Net income $1,976,601

- In 2010 Central Texas had financial results that produced the following financial ratios, which are key drivers of the company's ability to borrow additional funds and the terms and interest rates under which existing loans must be repaid:

  - Debt service coverage ratio[3] 0.61
  - Times interest earned ratio[4] 4.86
  - Debt/EBITDA ratio[5] 1.12

- Central Texas would not have had the financial resources to deploy and maintain either voice or broadband services without rate of return regulation and the support of the Universal Service Fund.

In these comments, Central Texas outlines the impacts that adoption of the short term USF and ICC rules, as written in the NPRM, would have on its financial results.

[3] Debt Service Coverage = Net Operating Income / (Principal + Interest on Long Term Debt)

[4] Times Interest Earned = (Net Income + Interest on Long Term Debt + Income Tax) / Interest on Long Term Debt

[5] Debt/EBITDA = Long Term Debt / Earnings Before Interest, Taxes, Depreciation, and Amortization

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I. Analysis Performed by Central Texas

In order to provide relevant financial context to the FCC in these comments, Central Texas engaged Moss Adams LLP[6] to perform a detailed financial analysis of the impacts of the NPRM. Their analysis primarily focused on the impacts of the proposed rules identified in Appendices A-C of the NPRM, which outline short term modifications to Universal Service Funding. They also analyzed the potential impacts of shifting intrastate access rates to an

[6] Moss Adams LLP (Moss Adams) is the 11th largest accounting and consulting firm in the United States, with more than 225 partners and 1,800 staff. Moss Adams' Telecom Group has served the telecommunications industry since 1957. Today, they provide audit, tax, and consulting services to more than 80 small and mid-sized telecommunications carriers throughout the United States and its territories.

average interstate switched access rate[7] or $0.0007. This analysis was performed using Central Texas recently submitted 2011 National Exchange Carrier Association (NECA) cost study forecast, which is utilized by NECA in establishing tariff rates for its annual access tariff filing with the FCC, and other information generally available from Central Texas as the basis. The following assumptions were used in the analysis of the impacts of these proposed changes in USF support and intercarrier compensation:

- 2011 forecasted costs were held constant for the 4 year analysis (2011 – 2014). Given the uncertainty in regulation and drastic reductions in USF support proposed in the NPRM. Central Texas will finish the projects for 2011 and cease future broadband upgrade projects until decisions are made regarding USF. Central Texas will continue to look at its entire network to determine broadband needs of its customers and have a plan in place for when the details are worked out to be able to move forward.

- All proposed changes to the calculation of High Cost Support were analyzed on an individual and aggregate basis. For example, for High Cost Loop Support, Moss Adams individually calculated the impacts of the phase out of Corporate Operations Expense and the reduction in support from 65% and 75% to 55% and 65%, and then calculated the combined impacts of these proposals.

- For ICLS, Moss Adams performed a standalone analysis of the impacts of phasing out Corporate Operations Expense without considering the impact that changes to LSS have

[7] The interstate switched access for each company varies based on participation in the National Exchange Carrier Association (NECA) FCC Tariff No. 5, NECA rate band, and transport miles and billing percentages included in the calculation of the composite rate. These composite switched access rates range from $0.010598 to $0.099349 per minute of use.

on the calculation of ICLS.[8] In addition, Moss Adams performed an analysis that included both the impacts of phasing out Corporate Operations Expense and the impacts of changes to LSS.

- Intrastate switched access minutes of use were held constant at their 2010 levels. While access minutes have been steadily declining, it was assumed that minutes will stabilize if the switched access rates decline to a composite interstate rate or $0.0007, and these savings are passed on to consumers by interexchange carriers.

- Voice access lines were held constant over the life of the analysis. While Central Texas has consistently lost access lines over the past several years, it is difficult to forecast the level of continuing decline. Maintaining consistency is a conservative approach, which may actually understate the overall negative financial impacts of the NPRM over the life of the analysis.

- Beyond intrastate switched access, all intrastate revenues were held constant over the life of the analysis. This includes local service revenue, special access, and state universal service funding. Again, given the consistent annual losses in voice access lines, maintaining consistency is a conservative approach, which may actually understate the overall negative financial impacts of the NPRM over the life of the analysis.

Using a wide variety of data and the assumptions identified above, the following analyses were performed based on the 2011 NECA forecast data and actual 2010 financial results:

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[8] Part 69.306(d)(2) of the FCC's rules requires a shift of the local switching revenue requirement (typically 30%), after the local switching revenue requirement has been reduced for LSS, to the common line revenue requirement. As a result, reductions in LSS will increase the local switching revenue requirement. This increased local switching revenue requirement is then shifted (30%) to the common line revenue requirement. The increase in the common line revenue requirement, increases the amount of ICLS necessary to recover the common line revenue requirement.

- The effect of phasing out Corporate Operations Expense over 3 years (2012-2014) on High Cost Loop Support (HCLS).

- The effect of phasing out Corporate Operations Expense over 3 years (2012-2014) on Interstate Common Line Support (ICLS).

- The effect of phasing out Corporate Operations Expense over 3 years (2012-2014) on Local Switching Support (LSS).

- The effect of reducing the HCLS support levels from 65% and 75% to 55% and 65% at once, starting in 2012.

- The effect of phasing out SNA over a 4-year period (2012-2015).

- The effect of phasing out LSS over a 3-year period (2012-2014).

- The effect of capping total High Cost Support (HCS) at $3,000 per line per year.

- The effect of transitioning intrastate switched access rates to the composite interstate switched access rate or $0.0007 per minute of use.[9]

- The combined effect of these proposed rule changes on net income.

- The combined effect of these proposed rule changes on the ability to repay existing debt, as measured by three key financial ratios, Debt Service Coverage (DSC), Times Interest Earned Ratio (TIER), and Debt/EBITDA.[10]

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[9] While there is a proposed calculation of support under Phase 2 of the Connect America Fund (CAF) that could include recovery of certain lost intrastate revenues, the NPRM does not ensure that this intrastate revenue loss will be recovered through the CAF or some other mechanism. As a result, Moss Adams included the proposed reductions in intrastate access revenues as potential lost revenues under the NPRM.

- The combined effect of these proposed rule changes on local customer rates.[11]

II. Financial Results and Findings of Moss Adams' NPRM Analysis

The results of the analyses and assumptions outlined above can be summarized for Central Texas as follows:

- The phase out of Corporate Operations Expense alone[12] reduces HCLS by $926,017, ICLS by $334,176, and LSS by $67,748 for a total impact of $1,327,941. This is a reduction in total High Cost Support of 17.25% over 3 years.

- The reduction in HCLS support from 65% of the Study Area Cost Per Loop (SACPL) above 115% of the National Average Cost Per Loop (NACPL) up to 150% of the NACPL and 75% of the SACPL above 150% of the NACPL to 55% and 65% respectively, alone reduces HCLS by $613,481. This is a reduction in total High Cost Support of 7.97% over 3 years.

- The phase out of LSS eliminates support of $257,110. This is a reduction in total High Cost Support of 3.34% over 3 years.

- The overall result of the proposed USF rule changes is a reduction in net income of $1,931,887, from $1,976,601 to $44,714. This results in a significant reduction in the financial ratios included in many loan covenants. The TIER ratio is reduced from 4.86 to

[10] Banks that traditionally lend to the rural telecommunications industry mandate loan covenants on borrowers, which usually include TIER, DSC, and/or Debt/EBITDA ratios. While these covenants can vary between borrowers and lenders, our covenants are with TIER ratios between 1.50% and 1.75%, DSC ratios at 1.25%, and Debt/EBITDA between 2.0 and 4.5.

[11] Presumably, increases in local rates will be the only way to recover lost USF revenues and potentially lost intrastate access revenues, as it is not clear that the Connect America Fund (CAF) will cover lost intrastate revenues.

[12] This does not include the impact of any other proposed rule changes.

1.12, the DSC ratio is reduced from 0.61 to (0.25), and Debt/EBITDA ratio increases from 1.12 to 1.40. In addition, the return on regulated rate base declines precipitously from 7.89% to 0.18%[13].

- The reduction of intrastate switched access rates to a composite interstate switched access rate or $0.0007 per minute of use reduces intrastate revenue by $374,911 and $1,268,310 respectively. This is a reduction of 29.30% and 99.13% respectively.

- The combined impact of these proposed rule changes has a devastating impact on the company's net income. In 2010, net income was $1,976,601. The result of the proposed USF rule changes, and intrastate switched access rates at the composite interstate rate, is a reduction in net income of $2,306,798 for a resulting net loss of $330,197. If intrastate switched access rates are further reduced to $0.0007, and there is no support for this lost revenue under the CAF or some other mechanism, net income is reduced by $3,200,197 for a resulting net loss of $1,223,596. There is no need to recalculate the financial ratios given these changes, as both the TIER and DSC ratios would be negative.

- As a result of these substantial reductions in revenue, with no apparent offset in support, Central Texas would have to raise end user rates, or reduce costs, to maintain long term financial viability. In order to recover the lost High Cost Support, Central Texas would need to increase end user rates, or reduce costs, by an estimated $23.36 per line per month. Residential rates for supported voice services currently average $7.83 per line per month today. This is an increase of more than 298.33% from today's average rates.

[13] The interstate rate of return authorized by the FCC is 11.25%. Intrastate rates of return vary by state and by company, but typically fall in the range of 8% to 12%.

- If the CAF, or some other mechanism does not support lost intrastate access revenues, end user rates would need to increase by an additional $4.53 with intrastate access rates reduced to the composite interstate rate per minute of use, or $15.34 with intrastate access rates reduced to $0.0007 per minute of use. Combined with the reductions in High Cost Support outlined above, end user rates would need to increase by as much as $38.70 to recover the lost revenues. This is an increase of more than 494% and brings the average rate for basic local service to a staggering $46.53 per month, not including the Federal Subscriber Line Charge, calling features, and taxes and surcharges.

III. Central Texas' Ability to Generate Cost Savings Through Increased Efficiency

As the designated Carrier of Last Resort in our regulated service territory, we are obligated to provide service to all requesting customers. As a result of this obligation, our ability to reduce capital investments is limited. If a customer requests service, we must build the facilities to that customer, pursuant to state and federal tariffs. In order to meet the expectations of our customers that we provide services that are reasonably comparable to those available in urban areas, we must continually maintain and upgrade our network.

In addition to the capital costs discussed above, many of our operating expenses are fixed, and certainly are not discretionary as the NPRM would suggest. The majority of our operating expenses are driven by employee salaries and benefits and depreciation expense. These employees install service, maintain the network, provide customer service, and perform administrative and management functions.

Certainly the installation of service and maintenance of the network are not discretionary functions, as the Public Utility Commission of Texas maintains service installation and quality of service standards. In order to reduce these costs significantly, we would need to reduce staff, which would in turn negatively affect the quality of service that we are able to provide our customers.

Customer service representatives are responsible for assisting customers with: understanding and ordering services, solving service problems, understanding and paying bills, and many other customer facing functions. Many of these customer service functions are mandated by the Public Utility Commission of Texas and/or the FCC. In order to reduce these costs significantly, we would need to reduce staff, which would in turn negatively affect our ability to assist customers in understanding services and rates.

Corporate operations expenses primarily include administrative functions, such as: regulatory accounting and auditing, legal and regulatory requirements, general management, and other administrative requirements. Many of these functions are mandated by the Public Utility Commission of Texas and/or the FCC, or lenders that provide necessary capital to build the network. In order to reduce these costs significantly, we would need to reduce staff, which in turn would negatively affect our ability to manage the company and to meet many of our regulatory obligations.

Our staffing levels are designed to maintain compliance with all regulatory and customer service standards, including meeting customer and network demand and allowing for reasonable work schedules, including sick and vacation time. We believe that it would be very difficult to significantly reduce these expenses, while still maintaining the quality of service, customer responsiveness and regulatory requirements mandated by the Public Utility Commission of Texas and the FCC. Central Texas has added much more responsibility and workload to its employees over the last several years in order to be as efficient as possible. The total employee base is lower than it was 8 years ago even though the total customer base has increased. Central Texas feels its employees are its greatest asset for taking care of the obligations it has and it would not be possible without them.

IV. Conclusions

If these financial impacts do take place it will be impossible to continue making the investments that will be required just to maintain our broadband and communications network. The area Central Texas serves is very rural but the customers still have needs and demands for communications and broadband services. Central Texas has been committed to serving this rural area for over 60 years. Without the high cost support, many areas will not receive service and it will be impossible to borrow funds for construction to these remote areas without a way to pay back the debt. Central Texas has worked hard to reduce its debt over the last several years and at the same time continue investing in infrastructure to better serve the needs of its customers. With the financial uncertainty these proposed changes create, future investment will halt. It will also be unfeasible to maintain the 70 jobs even though Central Texas is still obligated to serve the customers.

Central Texas has used high cost support for its intended purpose by maintaining good service and expanding broadband and communications services throughout rural central Texas. The rules changes as proposed would erase the gains we have made over the years and significantly damage the Cooperative, its members and the community.

Respectfully submitted,

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