Kansas Senate Utilities Committee
Rural Local Exchange Carrier Presentation
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Good afternoon, Mr. Chairman and members of the Committee. My name is Catherine Moyer. I am the General Manager and CEO of Pioneer Communications, headquartered in Ulysses, Kansas. I am here today on behalf of the 35 rural local exchange carriers (RLECs) in the State of Kansas. I plan to give a brief overview of the RLEC industry in Kansas.

The 35 Kansas RLECs provide service in 104 of the 105 counties in the State of Kansas (Wyandotte County is the exception). Collectively, Kansas RLECs serve more than 50% of the geographic area of Kansas and less than 10% of the telephone customers in Kansas. The areas the Kansas RLECs serve are the rural, sparsely populated part of the State.

In my company's service area, Pioneer serves approximately 12,000 access lines over about 5,000 square miles. Our largest population center is Ulysses, which has a population of about 6,300 people. Our population centers decline in population from there. We provide wireline phone service to communities like Hugoton, Lakin, Johnson, Syracuse, Kendall, Richfield and Rolla. Pioneer is on the larger size for Kansas RLECs, but all RLECs generally serve the same type of area—rural, sparsely populated, and very small towns.

To illustrate the areas the RLECs serve, I will give you a few more facts about Pioneer's service area. Using just the number of access lines we serve and the square miles we serve, we have just over 2 subscribers per square mile. However, when taking into account that 81% of our customers live in our population centers, our rural subscribers per square mile drops just under 0.5. Another way to look at service area is to look at that 81%--they reside in approximately 15 square miles of our 5,000 square miles. The remaining 19% of customers reside in the other 4,985 square miles. In actual network route miles, the 81% utilizes 375 route miles (14% of our route miles), and the 19% utilizes 2,325 route miles (86% of our route miles).

The cost to serve these areas is much higher than the cost to serve urban areas. If more customers are connected to the network, there are more people to which to spread the cost of the network. In some rural areas there will be several miles of network that connect only a customer or two, making the deployment and maintenance of a network an expensive proposition.

In addition to providing service to a sparsely populated part of the state, Kansas RLECs are also Carriers of Last Resort, or COLRs. COLRs are required by law to provide service to any customer in that RLECs service area that requests service, regardless of whether it is economically viable to provide service at the prevailing service rate. COLR obligations were established to provide service to low population areas because competition by itself cannot ensure access to telephone service; to ensure access where a business model by itself does not make sense.

In exchange for accepting the regulatory requirements of being a COLR, as well as other regulatory requirements, Kansas RLECs receive Federal Universal Service Fund (USF) support. Additionally, most Kansas RLECs also receive Kansas Universal Service Fund (KUSF) support. In 1996 the Kansas Legislature passed the Kansas Telecommunications Act. Among other things, the legislation required reductions in intrastate access rates that the local telephone companies charge to interexchange carriers for long distance calls that originate and terminate within the State of Kansas. Before the reductions, the intrastate access rates were based on the actual costs to the local telephone company to provide access to their customers for the interexchange carriers. In return for this intrastate access rate reduction that benefited interexchange carriers, the Kansas Legislature created the KUSF. The purpose of the KUSF was to compensate local telephone companies that serve the rural and high cost areas of Kansas for the loss in intrastate access rate revenue.

The Kansas RLECs continue to use KUSF support like they used intrastate access rate revenue—to deploy and maintain the network used to serve customers in the rural, sparsely populated parts of Kansas.

Another result of the 1996 Kansas Telecommunications Act was an increase of local rates for local telephone service. A minimum average local rate was established and all companies that were below that rate began to move towards that rate in small increments. The increase in local rate revenue was offset by concurrent reductions in KUSF support received, making it revenue neutral to the local telephone companies.

In 2002 the Kansas Legislature again passed telecommunications legislation. Based on a Kansas Corporation Commission proceeding, the Kansas Legislature established a target local telephone service rate, and provided a roadmap to move local telephone service rates to that target rate. Every two years the KCC establishes a statewide average rate and local telephone companies increase local service rates to the average rate. As with the 1996 legislation, any increase in local rate revenue is offset by concurrent reductions in KUSF support received.

There are many states that do not have state universal service funds, or do not have state universal service funds that have offset a reduction in intrastate access rates. In most of those states, intrastate access rates remain at a high level, and local rates remain at a low level. In those states, interexchange carriers are still paying rates that are based on the actual costs to the local telephone company to provide access to their customers for the interexchange carriers. Those states will still need to deal with the hard issues of intrastate access rate rebalancing and local rate increases at some point in the near future.

The Kansas RLECs are rate of return regulated. The Kansas Corporation Commission has performed intense audits of all RLECs and has set an intrastate rate of return specific to each company. This rate varies, and is dependent on the company's debt/equity structure, as well as dependent on when the rate was set based on outside influences of the market. Contrary to popular belief rate of return carriers have no guaranteed profit; only a right to a revenue structure providing the reasonable opportunity to earn a modest profit if they operate efficiently. The KCC's job is to review all costs and determine whether they are reasonable. The RLECs are also rate of return regulated on the Federal level.

In exchange for this level of regulation, as well as in exchange for accepting COLR responsibilities, RLECs receive USF and KUSF support. RLECs use this support to deploy and maintain their networks and provide affordable service, at a level set by the KCC, to their customers. Without support, the RLECs local rates would most likely reach an unaffordable level. At an unaffordable level, a decrease in connected subscribers would occur, ultimately making the entire worldwide network less valuable. In Pioneer's service area our local service rate, without all other taxes and surcharges, will move to $18.25 per month on March 1st. If Pioneer received no USF or KUSF, the rate to provide telephone service would increase to just more than $150.00 per month.

In addition to providing local telephone service to our customers, RLECs also provide service to enterprise customers. Enterprise customers are customers to which we are selling connectivity. In some cases these are wireless companies, where the RLEC is connecting towers back to the wireline network, carrying voice calls and data from the cell tower to its destination. In other cases these are wireless internet service providers, again connecting towers back to the wireline network and carrying the data to its destination. Without these wired connections, other providers would not have access to the wired network.

The RLECs are also regulated at the Federal level. The Federal Communications Commission has recently started an overhaul of the USF mechanism. Over the next several years the FCC will institute many new rules and regulations that will have an effect on the Kansas RLECs. Most RLECs will need to examine business plans and make changes to adapt to new rules and regulations. While these adaptations take place, the Kansas RLECs are advocating a Kansas regulatory environment that continues to operate as it has in the recent past and not add to uncertainty at the Federal level.

Thank you for the opportunity to appear here today. I am happy to stand for questions.