Company Information

The full name and address of the company is Foothills Rural Telephone Cooperative Corporation, Inc. ("Foothills"), 1621 Kentucky Route 40 West / P.O. Box 240, Staffordsville, KY 41256-0240. Foothills was established in 1950 as a not-for-profit, member-owned cooperative to provide local telephone service to business and residential members within the exchanges of Blaine, Chapman, Fallsburg, Flat Gap, Royalton, Salyersville, and Staffordsville ("Service Territory"). Foothills is a rural incumbent local exchange carrier serving parts of Lawrence and Johnson counties and all of Magoffin county in eastern Kentucky. At year-end 2016, Foothills provided 11,114 residential lines and 1,777 business lines to its members.

Foothills is an eligible telecommunications carrier ("ETC") in the communities it serves. It is also the carrier of last resort ("COLR") in its Service Territory. The Universal Service Administrative Company reported that Foothills would receive $2,607,189 from the Universal Service Fund, including High Cost Loop Support ("HCLS"), to support its COLR responsibilities in its Service Territory for 2016 and $2.9M in calendar year 2017.[1] As a high cost company, all HCLS revenues are crucial for Foothills to continue to meet its COLR responsibilities and to continue bringing advanced services to the communities it serves. As discussed below, Foothills' receipt of its full HCLS support requires it to meet minimum pricing levels imposed by the Federal Communications Commission ("FCC").

A schedule of Foothills' quarterly Universal Service Support is provided in Attachment A of this Exhibit. Historic access line counts, as reported to the National Exchange Carrier Association, are provided in Attachment B.

[1] As of March 1, 2017: http://www.universalservice.org/about/tools/fcc/filings/default.aspx

Description and Reason for Filing

With this filing, Foothills proposes to increase its basic residential and business local service rates by $2.00 and $0.60, respectively, each to $20.00 per month. This filing is made in response to the FCC's November 18, 2011 order (the "Transformation Order")[2] mandating minimum local residential service rate levels as a condition to continued receipt of certain federal universal service support.

The FCC ordered that Local Exchange Carriers would remain eligible to receive their full HCLS in a study area only if their rates for residential local exchange service are at or above the rate floor on June 1 of every year, beginning in 2012.[3] Failure to meet the rate floor results in forfeiture of the HCLS that the carrier would have otherwise received for that year.[4] The rate floors were established as follows: $10.00, effective June 1, 2012; $14.00, effective June 1, 2013; $16.00, effective December 1, 2014; $18.00 effective June 1, 2016; and $20.00 effective June 1, 2017.[5]

Foothills has met the three previous rate floors by raising basic residential rates by $2.00.[6] In its 2013 filing[7] and 2014 filing,[8] Foothills offset the increases by adding calling

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[2] *In the Matter of Connect America Fund et al.*, Report and Order and Further Notice of Proposed Rulemaking, FCC 11-161 (Nov. 18, 2011).

[3] *See* Transformation Order; *Wireline Competition Bureau Announces Results of Urban Rate Survey for Voice Services; Seeks Comment on Petition for Extension of Time to Comply with New Rate Floor*, Public Notice, DA 14-384 (March 20, 2014) (establishing 2014 rate floor); Report and Order, Declaratory Ruling, Order, Memorandum Opinion And Order, Seventh Order On Reconsideration, and Further Notice of Proposed Rulemaking, FCC 14-54 (June 10, 2014) ("Reconsideration Order") (modifying 2014 rate floor to allow for a phase-in of the residential rate floor).

[4] Transformation Order at ¶ 239

[5] Reconsideration Order at ¶ 80.

[6] *See In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2013-00193; *In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2014-00328; *In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2016-00051.

[7] *See In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2013-00193.

[8] *See In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2014-00328.

features to its basic residential service. In its 2016 filing,[9] Foothills expanded local calling to targeted exchanges surrounding its Service Territory.

Proposed Revisions and Customer Impact

With this filing, Foothills proposes increasing its basic residential rates by $2.00 to $20.00, in order to meet the 2017 rate floor. Because its business rates are currently $19.40, absent a rate increase to that line rate, Foothills' business customers would pay less than its residential subscribers. Accordingly, Foothills proposes to raise its business rates by $0.60 to $20.00.

In order to help mitigate the effect of these rate adjustments, Foothills proposes to provide new value-added benefits to its subscribers by increasing the number of exchanges included as extended area service ("EAS"), similar to the expansion that accompanied its approved rate change to meet the rate floor in 2016. This new proposed change to Foothills' EAS would expand local calling (i.e., toll-free) to all rate centers in the 606 area code. In doing so, Foothills' residential and business subscribers will receive local calling to their primary community of interest and will no longer pay toll charges for calls to forty-three counties served by the 606 area code.

Financial Impact

As a consequence of expanding its EAS calling scope, Foothills will forego two sources of revenue previously billed to interexchange carriers on routes it will convert from toll to EAS: (1) originating switched access revenues; and (2) billing and collections services. Additionally, to terminate the traffic to these exchanges, Foothills will pay a contracted interexchange carrier

[9] *See In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative*, Ky. P.S.C. Case No. 2016-00051.

as its underlying service provider. Hence, the terminating charges and the lost interexchange carrier revenues are costs Foothills expects to incur in expanding its EAS calling.

Foothills proposes to extend the EAS benefit to both its business and residential subscribers. Depending on their individual communities of interest and toll charges they will avoid with the expanded EAS, Foothills expects that, for many of its subscribers, particularly its business subscribers, the expanded local calling will mitigate the local rate increase and may actually offer savings.

As described in Attachment C of this Exhibit, Foothills estimates that its local rate increases minus the costs associated with its expanded calling area will create a net impact of approximately $13,486 per year. Even without the expanded EAS offset, however, as shown in the financial support section of this Exhibit, the impact of the FCC's Transformation Order warrants the rate increase proposed in this filing.

Financial Support for Filing

The FCC's Transformation Order included two requirements that had an immediate impact on state revenues and local service. First, the Transformation Order imposed financial penalties on companies that fail to meet the annual residential rate floor. Second, the Transformation Order capped and reduced charges associated with state access and reciprocal compensation. Combined, these items reduced state revenues and introduced additional potential losses that put pressure on Foothills to raise its local service rates to meet the FCC's rate floor.

Beginning in June 2017, companies that fail to meet the 2017 rate floor will lose a dollar in HCLS funding for every dollar they are below the residential rate floor. Foothills is seeking to increase its residential local exchange rates by $2.00 to meet the rate floor and avoid a reduction in its HCLS. As shown below, raising its residential rates allows Foothills to avoid losing

$266,736 per year in HCLS, which constitutes approximately 9.3% of its total anticipated Universal Service Support.

	Subscribers	Current Rate	FCC Floor	Retained HCLS
Residential Based on year-end 2016	11,114	$ 18.00	$ 20.00	$ 266,736
2017 Universal Service Support (See Attachment A)				$2,859,474
Universal Service Support at risk absent a rate increase				9.3%

Included in the FCC's Transformation Order is a requirement that carriers cap and reduce their reciprocal, state, and interstate inter-carrier compensation rates ("Access Cap"). The initial Access Cap was based on fiscal year 2011 revenues.[10] As mandated by the FCC, the Access Cap is reduced by 5% *each year*. As shown in the step-down of Eligible Access Recovery (as depicted in the following table), the cumulative FCC-mandated reduction in Foothills' access revenue recovery through the upcoming fiscal period ending June 2018 is [redacted]

	Access Cap	Incremental Reduction	Cumulative Reduction	Percent Lost
FY2011 10/1-9/30	[redacted]			
7/2012 - 6/2013	[redacted]	[redacted]	[redacted]	-5%
7/2013 - 6/2014	[redacted]	[redacted]	[redacted]	-10%
7/2014 - 6/2015	[redacted]	[redacted]	[redacted]	-14%
7/2015 - 6/2016	[redacted]	[redacted]	[redacted]	-19%
7/2016 - 6/2017	[redacted]	[redacted]	[redacted]	-23%
7/2017 - 6/2018	[redacted]	[redacted]	[redacted]	-26%
Six-year Aggregate Reduction			[redacted]	

This is the fourth residential rate increase, and first business increase, filed by Foothills in response to the FCC's rate floor. In its June 1, 2013 filing, Foothills forecast an increase in revenues of $23K per year. In its December 1, 2014 and June 1, 2016 filings, Foothills forecast

[10] October 1, 2010 through September 30, 2011.

an annual net increase in revenues of $28K, and $158K, respectively. This filing expands the definition of local calling to be state-wide, creating net revenues of $13K per year. As shown above, however, Foothills' aggregate net revenue increases resulting from its four filings remain well below the cumulative reduction in access revenues.

Summary

The FCC's Transformation Order continues to dramatically change the revenue sources that have been historically available to high cost rural telephone companies like Foothills and which have been used to meet their COLR obligation and to expand the availability of advanced broadband services to their customers. Unfortunately, for many of these affected companies, doing so requires upward pressure on local service rates. Because Foothills faces competition and is a not-for-profit, member-owned cooperative, the company would not have chosen to impose rate increases on its subscribers absent compelling pressure from the FCC. As shown in this documentation, Foothills has no realistic options except to meet the FCC's 2017 rate floor, and it is proposing reasonable measures to mitigate the effects of the rate change. For these reasons, Foothills respectfully requests that its tariff revisions be approved.

Attachments to this Exhibit:

Attachment A:	Foothills Quarterly Universal Service Support 2016-2017
Attachment B:	National Exchange Carrier Association Report of Access Lines
Attachment C:	Rate Design Analysis