

DECISION MEMORANDUM

TO: COMMISSIONER KJELLANDER
COMMISSIONER SMITH
COMMISSIONER HANSEN
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL
WORKING FILE

FROM: DOUG COOLEY

DATE: AUGUST 11, 2004

RE: IDAHO UNIVERSAL SERVICE FUND – 2004 ANNUAL REPORT

On July 30, 2004, Alyson Anderson, the Administrator of the Idaho Universal Service Fund, filed her Annual Report to the Commission for the period of July 1, 2003 through June 30, 2004. Staff has reviewed the calculations and recommendations in this report and finds them to be accurate and comprehensive. Once again, Staff commends Ms. Anderson for her continued service as Administrator of this fund.

Ms. Anderson reports surcharge revenue for the year in the amount of \$1,485,790 of which \$767,621 (52%) was contributed by local exchange services and \$718,169 (48%) was contributed by MTS/WATS services. This is a decrease in local surcharge revenue of approximately \$134,000 (from \$902,422 in 2003) and a decrease in toll surcharge revenue of approximately \$34,000 (from \$752,894 in 2003). These decreases are due largely to a decrease in inventory.

Annual disbursements to the eight qualifying incumbent local exchange carriers (ILECs) remained at \$1,898,303 as of June 30, 2004. For the fiscal year beginning July 1, 2004, annual disbursements are currently scheduled to be \$1,943,524. The ending fund cash balance at June 30, 2004 after applying bank charges, administrative expenses, and interest received was \$136,311; additionally, investments carry a cash value of \$300,000 with staggered maturity dates through September 30, 2004.

Local Service

As of May 1, 2004, companies reported 501,853 residential lines and 187,654 business lines, for a total of 689,507 lines. This represents a net decrease in lines of 4% with residential declining 3% and business decreasing 6% from the prior year.

The newly calculated statewide average rates and threshold rates are:

	2003 Current Weighted Average Rate	2004 Statewide Weighted Average Rate	125% Statewide Weighted Average Rate - 2003	125% Statewide Weighted Average Rate - 2004
Residential	\$17.58	\$17.53	\$21.98	\$21.92
Business Services	\$31.52	\$31.67	\$39.40	\$39.59

Switched Access Service

Toll access minutes reported by the local exchange companies were 277,754,500 representing almost no change from the 278,681,411 minutes reported in 2003. The new statewide average switched access rate has increased to \$0.0526 per minute from last year's average of \$0.0525.

Staff also reviewed the residential, business, and access rates of the recipient companies in accordance with Rule 31.46.01.106. Of the eight companies receiving Universal Service funds, Staff recommends that no adjustments to residential, business, or access rates be made at this time.

ADMINISTRATOR'S OPTIONS

The Administrator has presented five funding options for the coming year. These options are as follows:

Option 1: Status Quo - Ms. Anderson stated that if current surcharge levels are maintained and no additional funding is needed, the fund will decrease to a negative balance of approximately \$51,807 by June 30, 2005.

Option 2: Increase Local Surcharge Rates Only - In this discussion, Ms. Anderson proposes to increase the local surcharges to \$.13 per residential line per month, \$.24 per business line, and maintain the MTS/WATS rate at \$.0025 per minute. If these surcharge levels are

implemented and no additional funding is needed, the fund is estimated to increase to an adequate reserve balance of approximately \$497,008 by June 30, 2005.

Option 3: Increase MTS/WATS Surcharge Rate Only - In this option, Ms. Anderson proposes to maintain the current surcharge rates of \$.08 per residential line and \$0.13 per business line but increase the MTS/WATS surcharge rate to \$0.0045 per toll minute. If this adjustment is made, Ms. Anderson projects an ending balance of approximately \$503,702 by June 30, 2005.

Option 4: Increase All Surcharge Rates - In this option, Ms. Anderson proposes an increase in each surcharge rate to \$0.10 per residential line, \$0.18 per business line and \$0.0035 per toll minute. Under this proposal, the fund is estimated to have an adequate reserve balance of \$458,984 by June 30, 2005.

Option 5: Adjust Funding to meet Statewide Averages and Increase All Surcharge Rates - In this option, Ms. Anderson proposes an increase in each surcharge rate to \$0.10 per residential line, \$0.18 per business line and \$0.0035 per toll minute. In addition, Ms. Anderson points out that Cambridge Telephone shows a need to slightly reduce its access rates while Midvale Telephone shows a need to slightly increase its access rates according to Rule 31.46.01.106. Ms Anderson recommends that only Cambridge adjust its access rates and estimates that, under this proposal, the fund would attain an adequate reserve balance of \$451,422 by June 30, 2005.

ADMINISTRATOR'S RECOMMENDATION

Ms. Anderson recommends Option 5, which would increase the surcharge rates to \$0.10 per residential line, \$0.18 per business line per month and \$0.0035 per toll minute. Under this proposal, the fund is estimated to maintain an adequate reserve balance of \$451,422 by June 30, 2005. Although Staff is concerned about increasing the per-toll-minute rate because of growing competitive pressure and shrinking toll minute inventories, Staff also understands that local exchange companies also face increasing competition and shrinking line counts. Therefore, Staff supports an attempt to spread the needed increase among the local and toll carriers. However, Staff believes that making very slight adjustments to the access rates of Cambridge Telephone or Midvale Telephone is not necessary at this time. Staff discussed this with Cambridge Telephone and Midvale Telephone and the companies agree that very slight changes may or may not have

any distinguishable effect given the components of access revenue and the reporting cycles to the fund. Therefore, Staff is more inclined to recommend Option 4 which also spreads the needed increase among the local and toll carriers and produces an adequate fund reserve balance for 2005.

COMMISSION DECISION

Does the Commission wish to adopt the Administrator's recommended Option No. 5 to increase the surcharge rates to \$0.10 for residential lines, \$0.18 for business lines and \$0.0035 per toll minute? Does the Commission approve an access rate decrease for Cambridge telephone to the statewide threshold level and the corresponding changes in USF draws?

Does the Commission wish to adopt Staff's recommended Option No. 4 which also increases the surcharge rates to \$0.10 for residential lines, \$0.18 for business lines and \$0.0035 per toll minute but does not adjust the access rates of Cambridge Telephone?



Doug Cooley

Attachment

udmemos/usf 2004

**ADMINISTRATOR'S REPORT
IDAHO UNIVERSAL SERVICE FUND
YEAR ENDED -- JUNE 30, 2004**

SURCHARGE REVENUES

Surcharge revenues collected during the year totaled \$1,485,790 of which \$767,621, or 52% was assessed on local exchange services and \$718,169, or 48%, was assessed on MTS/WATS services. Current monthly surcharge rates are \$.08 per residential line, \$.13 per business line, and \$.0025 per MTS/WATS billed minute.

DISBURSEMENTS

COMPANIES RECEIVING DISBURSEMENTS

Authorized disbursements to Local Exchange Companies during the year ended June 30, 2003 totaled \$1,898,303 (page 11). Effective October 1, 2003, Order Number 29324 directed ATC Communications, Fremont Telecom, and Midvale Telephone Exchange to reduce switched access rates and increase disbursements from the Idaho Universal Service Fund. The IUSF did not make changes to the disbursements for these companies until the 2004-05 fiscal year. The following table shows the Local Exchange companies authorized by the Idaho Public Utilities Commission to receive disbursements from the Idaho Universal Service Fund.

Company Name	Original IPUC Order Authorizing Disbursement	Current Authorized Annual Disbursement
ACT Communications	22718 & 22128	\$528,352
Cambridge Telephone	22131	\$167,381
Fremont Telecom	28085 & 28166	\$123,894
Inland Telephone Co	23838	\$43,161

Midvale Telephone Exc.	22377	\$379,660
Direct Comm Rockland	22132	\$221,847
Rural Telephone Co	22414 & 26598	\$316,128
Silver Star Telecom	22237 & 22370	\$163,101
Total		\$1,943,524

ADMINISTRATIVE FEES AND EXPENSES

Administrative fees and expenses for the year ended June 30, 2004 were \$12,534. Administrative expenses include bank and broker charges of \$345. Administrative expenses payable at June 30, 2004 are \$762.

INVESTMENTS AND FUNDS

CASH

At June 30, 2004, the Idaho Universal Service Fund had a cash balance of \$136,311. The following is a table showing the beginning, ending, and quarterly fund cash balances for the year ended June 30, 2004.

Beginning Balance 6/30/03	Balance 9/30/03	Balance 12/31/03	Balance 3/31/04	Ending Balance 6/30/04
\$154,721	\$235,865	\$125,174	\$138,422	\$136,311

INTEREST

Interest earned on funds for the year ended June 30, 2004 totaled \$23,523. Coupon payments from investments in US Treasury Notes totaled \$22,330 and interest earned on funds held in a Merrill Lynch CMA-Government Securities Fund account, with a current yield of .46%, totaled \$1,193.

INVESTMENTS

The Idaho Universal Service Fund currently has investments in US Treasury Notes (Page 10). The T-Notes are valued at \$300,592 (face value \$300,000) have staggered maturity dates through September 30, 2004.

INVENTORIES

Total residential and business lines at May 1, 2004 were 501,853 and 187,654 respectively (pages 33 and 34). This represents a 3% decrease in residential lines and a 6% decrease in business lines from the prior year. Total MTS/WATS billed minutes of use for the year ended December 31, 2003 were 277,754,500 (page 38), a .33% decrease from the prior year.

STATEWIDE WEIGHTED AVERAGE RATES

A schedule summarizing the total funding eligibility for the local exchange companies is shown on page 11.

ONE-PARTY, SINGLE LINE SERVICE

The statewide weighted average rates for one-party single-line residential and business services are shown on pages 23 and 32. The following table shows the statewide weighted averages for one-party, single line service.

	STATEWIDE WEIGHTED AVERAGE RATE	IUSF THRESHOLD 125% STATEWIDE WEIGHTED AVERAGE RATE
RESIDENTIAL SERVICES	\$17.53	\$21.92
BUSINESS SERVICES	\$31.67	\$39.59

TOLL SWITCHED ACCESS

The statewide weighted average revenue per MTS/WATS access minute is shown on page 14. The statewide weighted average revenue is \$.0526 per minute.

FUNDING OPTIONS

GENERAL INFORMATION

OPTION 1: STATUS QUO

If current surcharge levels (\$.08 per residential line, \$.13 per business line, and \$.0025 per intrastate MTS/WATS billed minute) are maintained and no additional IUSF funding is authorized, the fund will decrease by approximately \$188,118 (page 39). MTS/WATS services would continue to contribute approximately 47% of the surcharge revenue and local exchange services would contribute 53% of the surcharge revenue, however the fund would have a negative balance of approximately (\$51,807) at June 30, 2005.

OPTION 2: INCREASE LOCAL SURCHARGE RATES

Due to the significant competition and the continual decline of MTS/WATS intrastate traffic, it could be prudent to increase only the local surcharge rates. If local surcharge levels are increased to \$.13 per residential line, \$.24 per business line, the MTS/WATS billed minute remains at \$.0025 per minute, and no additional IUSF funding is authorized, the fund will increase by approximately \$360,697 (page 39). The fund would have a balance of approximately \$497,008 at June 30, 2005, thus, providing an adequate

reserve balance. MTS/WATS services would contribute approximately 34% of the surcharge revenue and local exchange services would contribute 66% of the surcharge revenue.

OPTION 3: INCREASE MTS/WATS SURCHARGE RATES

This year shows an overall decline in local access lines, it could be argued that local access is facing as much competition and only the MTS/WATS surcharge rate should be increased. If the MTS/WATS surcharge rate is increased to \$.0045 per minute, and the local surcharge rates remain at \$.08 per residential line, \$.13 per business line, and no additional IUSF funding is authorized, the fund will increase by approximately \$367,391 (page 40). The fund would have a balance of approximately \$503,702 at June 30, 2005, thus, providing an adequate reserve balance. MTS/WATS services would contribute approximately 62% of the surcharge revenue and local exchange services would contribute 38% of the surcharge revenue.

OPTION 4: INCREASE ALL SURCHARGE RATES

If current surcharge rates are increased to \$.10 per residential line, \$.18 per business line, and \$.0035 per intrastate MTS/WATS billed minute, and no additional IUSF funding is authorized, the fund will increase by approximately \$322,673 (page 40). The fund would have a balance of approximately \$458,984 at June 30, 2005, thus, providing an adequate reserve balance. MTS/WATS services would contribute approximately 49% of the surcharge revenue and local exchange services would contribute 51% of the surcharge revenue.

OPTION 5: ADJUST FUNDING TO MEET STATEWIDE AVERAGES & INCREASE ALL SURCHARGE RATES

Idaho Universal Service Fund rule 106.02 indicates that to continue receiving IUSF funding after the first year of eligibility, the company may need to revise rates to meet the statewide threshold rates. If the rate is below the statewide threshold rate, and difference between the rates are greater than 3% and \$6,000, the company must revise it's rates to equal or exceed 100% of the statewide average for MTS/WATS access service and

125% of the statewide average for local exchange service. The following applies rule 106 to each company currently drawing from the IUSF. All of the companies drawing IUSF funds have had rate proceedings during the past several years, and the Commission has already reviewed and approved the rates for local access service. Therefore, I think it is unnecessary to adjust the local rates to meet the statewide average.

- ◆ ATC Communications does not need to adjust access rates, or the IUSF draw at this time.
- ◆ Cambridge Telephone Company shows a need to reduce access rates, thereby increasing the draw from the IUSF by \$7,562.
- ◆ Direct Communications Rockland does not need to adjust access rates, or the IUSF draw at this time.
- ◆ Fremont Telecom does not need to adjust access rates, or the IUSF draw at this time.
- ◆ Inland Telephone Company does not need to adjust access rates, or the IUSF draw at this time.
- ◆ Midvale Telephone Company shows a need to increase access rates, and decrease the IUSF draw by \$6,672. In 2003, Midvale was ordered to reduce access rates and thereby increase the IUSF draw. It does not seem prudent to reverse that action at this time, thus causing Midvale's access rates to fluctuate back and forth.
- ◆ Rural Telephone Company does not need to adjust access rates, or the IUSF draw at this time.
- ◆ Silver Star Telecom does not need to adjust access rates, or the IUSF draw at this time.

The 2004-2005 IUSF disbursements, including the adjustments to funding for Cambridge Telephone Company, per rule 106, will be \$1,951,086. If current surcharge levels are increased to \$.10 per residential line, \$.18 per business line, and \$.0035 per intrastate MTS/WATS billed minute, the fund will maintain an adequate reserve balance of approximately \$451,422 (page 41). At these rates, MTS/WATS services would contribute 49% of the total surcharge revenue and local exchange services would contribute 51% of the total surcharge revenue, with a projected income of \$315,111.

ADMINISTRATOR'S RECOMMENDATION

I recommend that the Commission adopt Option 5, increasing the current surcharge rates to \$.0035 per MTS/WATS billed minute, \$.10 per residential line, and \$.18 per business line. Additionally, the access rates and funding for Cambridge Telephone Company should be adjusted. This option should allow the fund to meet its obligations, as well as provide an adequate reserve balance. The fund will continue investing unused balances in US Treasuries. This option approximates a 50-50 contribution of surcharge revenues from local exchange services and MTS/WATS services. The fund balance at June 30, 2005 should be approximately \$451,422.

IDAHO UNIVERSAL SERVICE FUND OPTIONS

8/11/2004

OPTION 1 - STATUS QUO

	RATE		FUND CHANGE	
BANK BALANCE 7/1/04			\$136,311	
ANNUAL INVENTORY				
RESIDENTIAL LINES	501,853	0.08	\$481,779	33% OF TOTAL SURCHARGE REVENUE
BUSINESS LINES	187,654	0.13	292,740	20% OF TOTAL SURCHARGE REVENUE
TOLL MINUTES	277,754,500	0.0025	694,386	47% OF TOTAL SURCHARGE REVENUE
TOTAL IUSF FUNDING FOR YEAR			1,468,905	
US TREASURIES REDEEMED			300,000	
ESTIMATED INTEREST INCOME			5,000	
ESTIMATED IUSF DISBURSEMENTS			(1,943,524)	
ESTIMATED ADMINISTRATIVE EXPENSES			(18,500)	
TOTAL ESTIMATED EXPENSES			(1,657,024)	
PROJECTED INCOME/(DRAWDOWN)			(188,118)	
PROJECTED BALANCE 6/30/05			(\$51,807)	

OPTION 2 - INCREASE LOCAL SURCHARGE RATES

	RATE		FUND CHANGE	
BANK BALANCE 7/1/04			\$136,311	
ANNUAL INVENTORY				
RESIDENTIAL LINES	501,853	0.13	\$782,891	39% OF TOTAL SURCHARGE REVENUE
BUSINESS LINES	187,654	0.24	540,444	27% OF TOTAL SURCHARGE REVENUE
TOLL MINUTES	277,754,500	0.0025	694,386	34% OF TOTAL SURCHARGE REVENUE
TOTAL IUSF FUNDING FOR YEAR			2,017,720	
US TREASURIES REDEEMED			300,000	
ESTIMATED INTEREST INCOME			5,000	
ESTIMATED IUSF DISBURSEMENTS			(1,943,524)	
ESTIMATED ADMINISTRATIVE EXPENSES			(18,500)	
TOTAL ESTIMATED EXPENSES			(1,657,024)	
PROJECTED INCOME/(DRAWDOWN)			360,697	
PROJECTED BALANCE 6/30/05			\$497,008	

IDAHO UNIVERSAL SERVICE FUND OPTIONS

8/11/2004

OPTION 3 - INCREASE MTS/WATS SURCHARGE RATES

		RATE	FUND CHANGE	
BANK BALANCE 7/1/04			\$136,311	
ANNUAL INVENTORY				
RESIDENTIAL LINES	501,853	0.08	\$481,779	23% OF TOTAL SURCHARGE REVENUE
BUSINESS LINES	187,654	0.13	292,740	15% OF TOTAL SURCHARGE REVENUE
TOLL MINUTES	277,754,500	0.0045	1,249,895	62% OF TOTAL SURCHARGE REVENUE
TOTAL IUSF FUNDING FOR YEAR			2,024,414	
US TREASURIES REDEEMED			300,000	
ESTIMATED INTEREST INCOME			5,000	
ESTIMATED IUSF DISBURSEMENTS			(1,943,524)	
ESTIMATED ADMINISTRATIVE EXPENSES			(18,500)	
TOTAL ESTIMATED EXPENSES			(1,657,024)	
PROJECTED INCOME/(DRAWDOWN)			367,391	
PROJECTED BALANCE 6/30/05			\$503,702	

OPTION 4 - INCREASE ALL SURCHARGE RATES

		RATE	FUND CHANGE	
BANK BALANCE 7/1/04			\$136,311	
ANNUAL INVENTORY				
RESIDENTIAL LINES	501,853	0.10	\$602,224	30% OF TOTAL SURCHARGE REVENUE
BUSINESS LINES	187,654	0.18	405,333	21% OF TOTAL SURCHARGE REVENUE
TOLL MINUTES	277,754,500	0.0035	972,141	49% OF TOTAL SURCHARGE REVENUE
TOTAL IUSF FUNDING FOR YEAR			1,979,697	
US TREASURIES REDEEMED			300,000	
ESTIMATED INTEREST INCOME			5,000	
ESTIMATED IUSF DISBURSEMENTS			(1,943,524)	
ESTIMATED ADMINISTRATIVE EXPENSES			(18,500)	
TOTAL ESTIMATED EXPENSES			(1,657,024)	
PROJECTED INCOME/(DRAWDOWN)			322,673	
PROJECTED BALANCE 6/30/05			\$458,984	

IDAHO UNIVERSAL SERVICE FUND OPTIONS

8/11/2004

OPTION 5 - ADJUST FUNDING LEVELS PER RULE 106 & INCREASE ALL SURCHARGE RATES

		RATE	FUND CHANGE	
BANK BALANCE 7/1/04			\$136,311	
ANNUAL INVENTORY				
RESIDENTIAL LINES	501,853	0.10	\$602,224	30% OF TOTAL SURCHARGE REVENUE
BUSINESS LINES	187,654	0.18	405,333	21% OF TOTAL SURCHARGE REVENUE
TOLL MINUTES	277,754,500	0.0035	972,141	49% OF TOTAL SURCHARGE REVENUE
TOTAL IUSF FUNDING FOR YEAR			1,979,697	
US TREASURIES REDEEMED			300,000	
ESTIMATED INTEREST INCOME			5,000	
ESTIMATED IUSF DISBURSEMENTS			(1,951,086)	REFELCTS INCREASED FUNDING TO CAMBRIDGE
ESTIMATED ADMINISTRATIVE EXPENSES			(18,500)	
TOTAL ESTIMATED EXPENSES			(1,664,586)	
PROJECTED INCOME/(DRAWDOWN)			315,111	
PROJECTED BALANCE 6/30/05			<u>\$451,422</u>	