

DECISION MEMORANDUM

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

FROM: GRACE SEAMAN

DATE: AUGUST 26, 2005

**RE: 2005 IDAHO UNIVERSAL SERVICE FUND ANNUAL REPORT AND
RECOMMENDATIONS**

On July 14, 2005, Alyson Anderson, the Administrator of the Idaho Universal Service Fund (USF), filed her Annual Report to the Commission for the period of July 1, 2004 through June 30, 2005. Staff has reviewed the calculations, supporting documentation and recommendations contained in the report.

Current USF monthly surcharge rates are \$.10 per residential line, \$.15 per business line, and \$.003 per MTS/WTS billed minute. Ms. Anderson reports surcharge revenue for the year in the amount of \$1,616,135. Local exchange services contributed \$830,052 (51%) and \$786,083 (49%) was contributed by MTS/WATS services. This is an increase in local surcharge revenue of approximately \$62,431 (from \$767,621 in 2004) and an increase in toll surcharge revenue of approximately \$67,914 (from \$718,169 in 2004).

Annual disbursements to the eight qualifying incumbent local exchange carriers (ILECs) increased slightly to \$1,973,671 as of June 30, 2005. For the next year beginning July 1, 2005, annual disbursements are expected to decrease slightly to \$1,943,524, assuming no changes are made to the USF draw. The ending fund cash balance as of June 30, 2004, after applying bank charges, administrative expenses, and interest received, was \$65,265.

Local Service

As of May 1, 2005, companies reported 485,612 residential lines and 192,947 business lines, for a total of 678,559 lines. This represents a net decrease in lines of 10,948 with residential lines declining by 3% and business increasing by 3% from the prior year.

The newly calculated statewide average rates and threshold rates are:

	2004 Current Weighted Average Rate	2005 Statewide Weighted Average Rate	125% Statewide Weighted Average Rate - 2004	125% Statewide Weighted Average Rate - 2005
Residential	\$17.53	\$17.65	\$21.92	\$22.06
Business Services	\$31.67	\$31.78	\$39.59	\$39.72

Switched Access Service

Local exchange companies reported MTS/WATS access minutes of 314,542,261 compared to 277,754,500 minutes in 2004, a 13% increase. Compared to a steady decline of billed minutes over the past three years, this represents a significant increase. Staff and the Administrator believe this is an anomaly that cannot be sustained into the next fiscal year. The Administrator noted the increase is impacted by the reports of 37 new companies that had not previously contributed or contributed minimally to the USF. Additionally, four major MTS/WATS service providers reported significant increases in billed minutes. These four companies reported a total combined increase in minutes of 70,594,561. These increases offset the decreases experienced by 56% of the MTS/WATS service providers. The statewide average switched access rate decreased to \$0.048 per minute from last year's average of \$0.0526.

Funding Adjustments Review

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 presented five funding options to meet the projected annual disbursements for the coming year. These options are as follows:

Option 1: Status Quo - Ms. Anderson stated that if current surcharge levels are maintained and the disbursements remain the same, the fund will have a negative balance of approximately \$22,886 by June 30, 2006.

Option 2: Increase Local Surcharge Rates Only - In this discussion, Ms. Anderson proposes to increase the monthly local surcharges to \$.15 per residential line, \$.27 per business line, and maintain the MTS/WATS rate at \$.003 per minute. If these surcharge levels are implemented, the fund balance on June 30, 2005 is estimated to be approximately \$546,324. MTS/WATS services would contribute approximately 38% of the surcharge revenue and local exchange services would contribute 62% of the surcharge revenue.

Option 3: Increase MTS/WATS Surcharge Rate Only - In this option, Ms. Anderson proposes to maintain the current monthly surcharge rates of \$.10 per residential line and \$.15 per business line, but increase the MTS/WATS surcharge rate to \$.0049 per minute. If this adjustment is made, Ms. Anderson projects an ending reserve balance of approximately \$571,011 by June 30, 2005. MTS/WATS service 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 - In this option, Ms. Anderson proposes an increase in each surcharge rate to \$.12 per residential line, \$.22 per business line and \$.004 per MTS/WATS minute. Under this proposal, the fund is estimated to have a reserve balance of \$568,313 by June 30, 2005. MTS/WATS service would contribute approximately 51% of the surcharge revenue and local exchange services would contribute 49% of the surcharge revenue.

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 \$.12 per residential line, \$.22 per business line and \$.004 per toll minute. Ms. Anderson also points out that Cambridge Telephone Company and Inland Telephone Company could slightly reduce access rates according to Rule 31.46.01.106. Under this proposal, Ms Anderson projects the fund would attain a reserve balance of \$552,958 by June 30, 2005. MTS/WATS services would contribute approximately 51% of the total surcharge revenue and local exchange services would contribute 49% of the total surcharge revenue.

ADMINISTRATOR'S RECOMMENDATION

Ms. Anderson recommends Option 5, which would increase the surcharge rates to \$.12 per residential line, \$.22 per business line per month and \$.004 per toll minute. Under this proposal, the fund is estimated to maintain an adequate reserve balance of \$552,958 by June 30, 2005.

STAFF ANALYSIS

In spite of this year's increase in MTS/WATS billed minutes, 56% of the companies reported a decline in billed minutes. Staff is cautious about increasing the per-toll-minute rate due to the continued competitive pressure and unstable toll minute inventories. This year's large and sudden increase in billed minutes should be viewed as an anomaly. Staff also understands that local exchange companies face increasing competition and shrinking line counts. Therefore, Staff continues to support an attempt to spread the needed increase as equitably as possible between the local and toll carriers.

Staff does not believe it is necessary to make the slight adjustments to the access rates of Cambridge and Inland Telephone companies at this time. Staff discussed this with both companies and they agree the slight changes may or may not have any distinguishable effect given the components of access revenue and the reporting cycles to the fund.

After reviewing the USF Annual Report, Staff discovered elements in company reports that merited further scrutiny. Staff requested additional information from Ms. Anderson and requested company reviews of information contained in the USF reports. Some issues have been clarified and some investigation of reported information continues. Receipt of additional information from company inquiries may potentially affect the statewide average threshold rates. Staff is also concerned about the 13% increase in billed minutes and believes it is prudent to expect the 2005 levels be the same or lower than the levels reported in the 2004 annual report. After assessing these concerns, Staff recommends the Commission adopt Option 4, which distributes the needed increase among the local and toll carriers and produces an adequate fund reserve balance that will provide an adequate cushion for changes in the funding thresholds. Staff believes the low end-of-year cash balance of \$65,265 must be addressed with a surcharge increase beginning on October 1, 2005. Additionally, the projected reserve balance estimated in Option 4 provides a cushion to address any downward adjustments in MTS/WATS billed minutes reported, and changes in the threshold levels that may occur as companies submit their reports.

COMMISSION DECISION

Does the Commission wish to adopt the Administrator's recommended Option No. 5 to increase the surcharge rates to \$0.12 for residential lines, \$0.22 for business lines and \$0.004 per

intrastate MTS/WATS minute? Does the Commission also approve an access rate decrease for Cambridge Telephone Co. and Inland Telephone Co. to the statewide threshold level and the corresponding changes in USF draws?

Does the Commission wish to adopt Staff's recommended Option No. 4 that increases the surcharge rates to \$0.12 for residential lines, \$0.22 for business lines and \$0.004 per MTS/WATS minute, but does not adjust the access rates of Cambridge and Inland Telephone Co.?

Does the Commission wish to adopt a different funding option?


Grace Seaman

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