

MOSS ADAMS LLP



The Yin & Yang of ILEC Cost Recovery

Moss Adams

- ◆ Firm Established in 1913
 - Serving Telecom Clients Since 1957
- ◆ The 11th largest Accounting & Consulting Firm in the U.S.
 - 250 Partners / 2,000 Staff
- ◆ Telecom Specialists based in Spokane, Stockton, Seattle & Vancouver

Yin & Yang



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Yin & Yang

- ◆ *“The concept of yin and yang (or earth and heaven) describes two opposing and, at the same time, complementary (completing) aspects of any one phenomenon (object or process) or comparison of any two phenomena.”* Wikipedia
- ◆ *“Opposite and complementary forces in Chinese thought, from Chinese words meaning “shaded” and “sunny.”* Encarta Encyclopedia

Yin & Yang

◆ The Yin & Yang of Loop Cost Recovery

- 3 primary means of loop cost recovery – we will focus on the first 2
 - ▶ Cost Separations – Part 36
 - NECA Settlements or Company Specific Tariff
 - EUCL/SLC + Interstate Common Line Support
 - ▶ High Cost Loop Support
 - ▶ Intrastate Revenues
 - Local Rates
 - Access
- Without one, cost recovery is not complete



Overview of Cost Separations

Part 36 – Cost Separations

Sample Telephone Company
Study Area: 123456
Study Year:

REVENUE REQUIREMENT SUMMARY

S-1

LINE	DESCRIPTION	SOURCE	TOTAL COMPANY (a)	INTERSTATE				INTRASTATE				LOCAL		
				InterLATA		IntraLATA		InterLATA		IntraLATA		EAS (j)	User Defined (k)	Other (l)
				MSG (b)	PL (c)	MSG (d)	PL (e)	MSG (f)	PL (g)	MSG (h)	PL (i)			
1	Net Telecom Plant	S-2,Ln46	6,583,485	2,416,368	237,680	-	-	-	-	978,062	53,378	1,033,153	347	1,864,497
3	RATE BASE	Ln1-2	6,583,485	2,416,368	237,680	-	-	-	-	978,062	53,378	1,033,153	347	1,864,497
4	Rate of Return	Records	10.5039%	11.2500%	11.2500%	11.2500%	11.2500%	10.0000%	10.0000%	10.0000%	10.0000%	10.0000%	10.0000%	10.0000%
5	RETURN ON RATE BASE	Ln3*4	691,524	271,841	26,739	-	-	-	-	97,806	5,338	103,315	35	186,450
7	NET RETURN	Ln5-6	691,524	271,841	26,739	-	-	-	-	97,806	5,338	103,315	35	186,450
8	Fixed Charges	S-10,Ln24	120,811	44,309	4,365	-	-	-	-	17,949	979	19,003	-	34,205
9	Amortization of Excess Def Taxes	S-10,Ln47	-	-	-	-	-	-	-	-	-	-	-	-
10	Capitalized Payroll Taxes	S-10,Ln50	-	-	-	-	-	-	-	-	-	-	-	-
11	Depreciation Adjustment	S-10,Ln53	-	-	-	-	-	-	-	-	-	-	-	-
12	FIT Allowances/Disallowances	S-14,Ln22	-	-	-	-	-	-	-	-	-	-	-	-
13	Inc Adj Alloc on 2001	S-10,Ln59+60	-	-	-	-	-	-	-	-	-	-	-	-
14	Inc Adj Alloc on Big 3 Exp	S-10,Ln61+62	-	-	-	-	-	-	-	-	-	-	-	-
15	Total Misc Inc Adjustment	S-10,Ln63	-	-	-	-	-	-	-	-	-	-	-	-
16	AFTER TAX INCOME	Note 1	570,713	227,532	22,374	-	-	-	-	79,858	4,359	84,312	35	152,244
17	State Income Tax	Ln52	45,511	18,144	1,784	-	-	-	-	6,368	348	6,723	3	12,141
18	State ITC Amortization	S-10,Ln45	-	-	-	-	-	-	-	-	-	-	-	-
19	Net Federal Income Tax	Ln43	294,004	117,213	11,526	-	-	-	-	41,139	2,245	43,433	18	78,429
20	Federal ITC Amortization	S-10,Ln44	-	-	-	-	-	-	-	-	-	-	-	-
21	Operating Expenses & Taxes	S-3,Ln17	2,880,493	1,113,786	103,631	-	-	-	-	428,775	23,752	396,800	7,896	805,853
22	Nonoperating Expenses	S-10, Ln17+18	-	-	-	-	-	-	-	-	-	-	-	-
23	Uncollectibles	S-10,Ln57	-	-	-	-	-	-	-	-	-	-	-	-
24	Other Adjustments (Net RR)	Records	-	-	-	-	-	-	-	-	-	-	-	-
25	NET REVENUE REQUIREMENT	Ln7+17..23-24	3,911,532	1,520,986	143,680	-	-	-	-	574,088	31,683	550,272	7,952	1,082,872
26	Gross Receipts Tax	Note 2	-	-	-	-	-	-	-	-	-	-	-	-
27	7340 Alw Fds Used Dur Constr	S-10,Ln15	1,000	355	37	-	-	-	-	151	8	160	-	289
28	REVENUE REQUIREMENT	Ln25+26-27	3,910,532	1,520,631	143,643	-	-	-	-	573,937	31,674	550,112	7,952	1,082,583
29	Distribution of Line 30	Ln28/28a	100.0000%	38.8855%	3.6732%	-	-	-	-	14.6767%	0.8100%	14.0674%	0.2033%	27.6838%

FCC Rules – Part 36

- ◆ Outlines procedures to separate costs between state and interstate jurisdictions
 - ILECs use same plant to provide both state and interstate services
 - Separation is necessary to delineate federal and state regulatory authority and cost recovery

FCC Rules – Part 36

◆ Overall separations concept

- Telecommunications plant, in general, can be segregated into 2 broad categories
 - ▶ Interexchange plant – used primarily to provide toll services
 - ▶ Exchange plant – used primarily to provide local services, separated based on traffic and work time studies

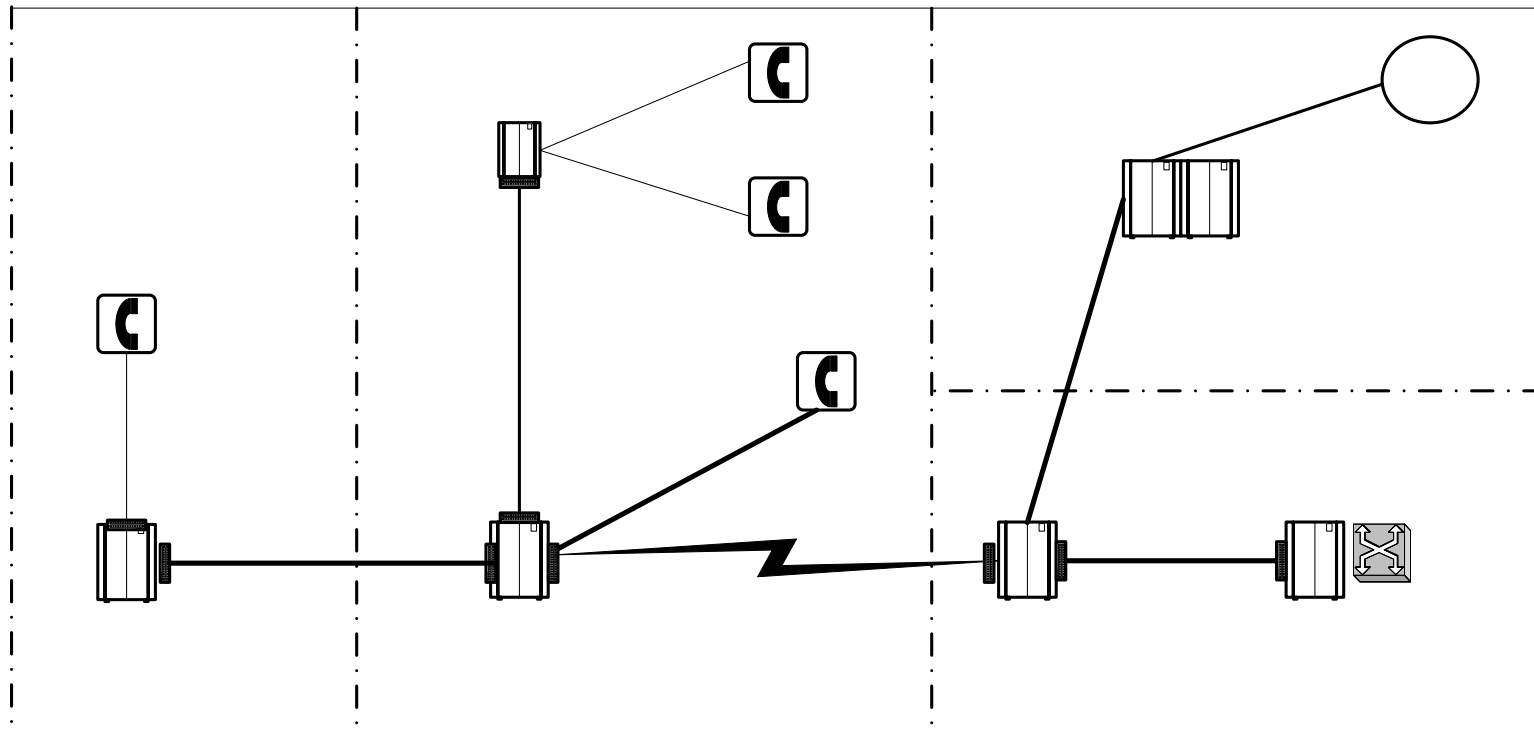
FCC Rules – Part 36

- ◆ Certain types of plant are assigned to categories, to better define the cost of services provided
 - Central Office Equipment (2210/2220/2230)
 - Cable and Wire Facilities (2410)
- ◆ Each category contains equipment that is used in the provision of similar services

Part 36 - Cost Categorization

- ◆ Loop costs are primarily broken into 2 specific categories
 - Central Office Equipment Category 4.13 – Subscriber Circuit Equipment
 - ▶ Loop concentration equipment
 - Cable & Wire Facilities Category 1 – Exchange Line Excluding Wideband
 - ▶ Subscriber loops (non-wideband)

Part 36 – Plant Categorization



Part 36 – Jurisdictional Separations

- ◆ Costs are separated between jurisdictions, using traffic and work time studies
 - Each cost is separated on the appropriate factor, or follows a related plant or expense account
 - ▶ COE Cat. 4.13 – Subscriber Plant Factor (SPF)
 - 25% Interstate by Rule
 - ▶ C&WF Cat. 1 – Subscriber Plant Factor (SPF)
 - 25% Interstate by Rule

Part 36 - COE Separation

Sample Telephone Company
Study Area: 123456
Study Year:

CENTRAL OFFICE EQUIPMENT

S-5
Sheet 1 of 3

LINE	DESCRIPTION	SOURCE	TOTAL COMPANY (a)	INTERSTATE TOLL				INTRASTATE TOLL				LOCAL				
				InterLATA		IntraLATA		InterLATA		IntraLATA		EAS (j)	User Defined (k)	Other (l)		
				MSG (b)	PL (c)	MSG (d)	PL (e)	MSG (f)	PL (g)	MSG (h)	PL (i)					
25	2210 Central Office Switching															
31	Cat 3-Local Switching - TS	Ln31a*9	1,572,893	1,336,959	-	-	-	-	78,645	-	78,645	-	-	78,645	-	-
32	Cat 3-Local Switching - NTS	Ln32a*9	-	-	-	-	-	-	-	-	-	-	-	-	-	-
33	Direct Assignment	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
34	Total Cat 3	Ln31..33	1,572,893	1,336,959	-	-	-	-	78,645	-	78,645	-	-	78,645	-	-
35	Distribution of Line 34	Ln34/34a	100.0000%	85.0000%	-	-	-	-	5.0000%	-	5.0000%	-	-	5.0000%	-	-
36	TOTAL COE-SWITCHING	Ln28+34	1,572,893	1,336,959	-	-	-	-	78,645	-	78,645	-	-	78,645	-	-
37	Distribution of Line 36	Ln36/36a	100.0000%	85.0000%	-	-	-	-	5.0000%	-	5.0000%	-	-	5.0000%	-	-
COE CATEGORY 4 SEPARATION																
44	2230 Central Office - Transmission															
45	Cat 4.1-Exchange Circuit															
46	4.11 Wideband-Line	Ln46a*38	-	-	-	-	-	-	-	-	-	-	-	-	-	-
47	Direct Assignment	Direct	110,370	-	109,001	-	-	-	-	1,369	-	-	-	-	-	-
48	4.12 Exch Trunk - EAS	Direct	95,717	-	-	-	-	-	-	-	95,717	-	-	-	-	-
49	Ex Trk x/WB - Basic	Ln49a*40	-	-	-	-	-	-	-	-	-	-	-	-	-	-
50	Ex Trk x/WB - Basic DA	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
51	Ex Trk WB	Ln51a*39	-	-	-	-	-	-	-	-	-	-	-	-	-	-
52	Exch Trk WB - Direct Assignment	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
53	4.13 Ex Line x/WB															
54	Joint MSG	Ln64b*41	710,294	177,573	-	-	-	-	71,029	-	106,544	-	-	355,147	-	-
55	PL & Local	Ln64c..i	11,791	-	8,703	-	-	-	-	3,088	-	-	-	-	-	-
56	Direct Assignment - Basic/Special	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
57	Cat 4.2-Interexchange															
59	4.22 Wideband															
60	Joint MSG	Ln60a*43	-	-	-	-	-	-	-	-	-	-	-	-	-	-
61	PL	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
62	Direct Assignment	Direct	20,001	-	16,606	-	-	-	-	3,395	-	-	-	-	-	-
67	4.23 All Other															
68	Joint MSG	Ln82*64	192,689	105,979	-	-	-	-	86,710	-	-	-	-	-	-	-
69	PL, TWX & Local	Ln82c..i	34,523	-	24,889	-	-	-	-	9,634	-	-	-	-	-	-
70	Direct Assignment - Nonaccess	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
71	Cat 4.3-Host/Remote MSG															
72	Joint (x/WATS)	Ln72a*66	616,722	215,853	-	-	-	-	215,853	-	154,180	-	-	30,836	-	-
73	WATS	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
74	Direct Assignment	Direct	-	-	-	-	-	-	-	-	-	-	-	-	-	-
75	Total Cat 4	Ln46..62+67..74	1,792,107	499,405	159,199	-	-	-	373,592	17,487	356,441	-	-	385,983	-	-
76	TOTAL COE-TRANSMISSION	Ln75	1,792,107	499,405	159,199	-	-	-	373,592	17,487	356,441	-	-	385,983	-	-
77	Distribution of Line 76	Ln76/76a	100.0000%	27.8669%	8.8834%	-	-	-	20.8465%	0.9758%	19.8895%	-	-	21.5379%	-	-
78	TOTAL CENTRAL OFFICE EQUIP	Ln23+36+76	3,365,000	1,836,364	159,199	-	-	-	452,237	17,487	435,086	-	-	464,628	-	-
79	Distribution of Line 78	Ln78/78a	100.0000%	54.5725%	4.7310%	-	-	-	13.4394%	0.5197%	12.9297%	-	-	13.8077%	-	-

Part 36 - CWF Separation

Sample Telephone Company
Study Area: 123456
Study Year:

CABLE AND WIRE FACILITIES

S-7
Sheet 1 of 2

SOURCE	TOTAL COMPANY (a)	INTERSTATE TOLL				INTRASTATE TOLL				LOCAL		
		InterLATA		IntraLATA		InterLATA		IntraLATA		EAS	User Defined	Other
		MSG (b)	PL (c)	MSG (d)	PL (e)	MSG (f)	PL (g)	MSG (h)	PL (i)	(j)	(k)	(l)
SEPARATIONS FACTORS												
1 Gross Allocator Pct (Trans SPF)	Records	100.0000%	25.0000%							15.0000%		50.0000%
2 REL MOU's - Exchange Trunk	Records	-										
3 WB Line	Records	-										
4 MOU Pct-Ex Trk WB	Records	-										
C&WF CAT 1-2 SEPARATION												
5 2410 Cable & Wire Facilities												
6 Cat 1-Exch Line x/WB												
7 1.1 Intra PL & WATS	Ln22e.i	22,184						22,184				
8 1.2 Inter PL & WATS	Ln22c.d	62,518	62,518									
9 1.3 Jointly Used	Ln22b*1	5,102,283	1,275,571					510,228		765,342		2,551,141
10 Direct Assignment	Direct	-										
11 Total Category 1	Ln7..10	5,186,985	1,275,571	62,518				510,228	22,184	765,342		2,551,141
12 Cat 2-WB & Exch Trunk												
13 Ex Trk - joint message	Ln13a*2	-										
14 Ex Trk - EAS	Direct	131,310								131,310		
15 Ex Line WB	Ln15a*3	-										
16 WB Line	Direct	58,376		47,201					11,175			
17 WB Trunk	Ln17a*4	-										
18 WB Trunk DA	Direct	-										
19 Total Category 2		189,685		47,201					11,175	131,310		
23 Interexchange Trk WB	Records	-										
24 CMM Pct-IX x/WB	Records	100.0000%	55.0000%					45.0000%				
25 C&WF TWX Connect Min Miles Pct-IT	Records	100.0000%	55.0000%					45.0000%				
26 C&WF TWX Connect Min Miles Pct-Rmt	Records	100.0000%	55.0000%					45.0000%				
27 Host/Remote MOU Miles Pct	Records	100.0000%	35.0000%					35.0000%		25.0000%		5.0000%
C&WF CAT 3-4 SEPARATION												
28 Cat 3-Interexchange C&WF												
29 WB PL - Direct Assignment	Direct	75,627		60,081					15,547			
30 WB - Joint Message	Ln30a*23	-										
31 Joint MSG x/WB	Ln48b*24	269,940	148,467					121,473				
32 PL, TWX & Local x/WB	Ln49c.i	89,980		67,485					22,495			
33 Joint TWX-IT	Ln49j*25	-										
34 Joint TWX-Rmt	Ln49k*26	-										
35 Direct Assignment - Nonaccess	Direct	-										
36 Total Category 3	Ln28..35	435,548	148,467	127,566				121,473	38,042			
37 Cat 4-Host/Remote C&WF												
38 Joint (x/WATS)	Ln38a*27	1,520,783	532,274					532,274		380,196		76,039
39 WATS	Direct	-										
40 Direct Assignment	Direct	-										
41 Total Category 4	Ln38..40	1,520,783	532,274					532,274		380,196		76,039
42 TOTAL CABLE & WIRE FACILITIES	Ln11+19+36+41	7,333,000	1,956,312	237,284				1,163,975	71,400	1,276,848		2,627,180

Part 36 – Expense Separation

Expense Account	Account Description	Allocation Basis
6110	Network Support	Account 2110 – Land and Support Assets
6120	General Support	Account 2110 – Land and Support Assets
6210	Switching	Accounts 2210, 2220, and 2230 <u>combined</u> – Central Office Equipment
6220	Operator	Accounts 2210, 2220, and 2230 <u>combined</u> – Central Office Equipment
6230	Transmission	Accounts 2210, 2220, and 2230 <u>combined</u> – Central Office Equipment
6310	Information	Account 2310. Typically non-regulated. If so, remove from study.
6410	Cable & Wire	Account 2410 – Cable and Wire Facilities
6510	Other PP&E	Account 2001 – Total Telecommunications Plant in Service
6530	Network Ops.	Accounts 2210, 220, 2230, 2310 and 2410 <u>combined</u>
6540	Access	Directly assigned to the appropriate jurisdiction
6560	Depreciation	Associated primary plant account or related category
6610	Marketing	Analysis of current billing (currently frozen)
6620	Services	Analysis of job functions (Work Time Study), broken into more specific expense categories
6710	Exec. & Planning	Big 3 Expenses (Plant Specific, Plant Non-Specific & Customer Operations, excluding 6110, 6120, 6510, 6540 & 6560)
6720	Gen. & Admin.	Big 3 Expenses (Plant Specific, Plant Non-Specific & Customer Operations, excluding 6110, 6120, 6510, 6540 & 6560)
7200	Operating Taxes	Approximate Net Income, Direct Assignment, and/or Account 2001 – Total Telecommunications Plant in Service

Part 69 – Cost Recovery

Sample Telephone Company
Study Area: 123456
Study Year:

REVENUE REQUIREMENT SUMMARY

A-1

LINE	DESCRIPTION	SOURCE	INTERSTATE										
			JURIS TOTAL (a)	Special Access			Local Switching (e)	Transport		Carrier Common Line		B&C	
				Chan Term (b)	CM-Term (c)	CM-Facil (d)		Transmissior (i)	Tandem Sw (j)	Pay (k)	BFP (l)	Record (m)	Process (n)
1	Net Telecom Plant	A-2, Ln44	2,654,048	136,745	25,204	75,866	949,433	600,331	-	-	866,468	-	-
3	RATE BASE	Ln1-2	2,654,048	136,745	25,204	75,866	949,433	600,331	-	-	866,468	-	-
4	Rate of Return	Records	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%	11.2500%
5	RETURN ON RATE BASE	Ln3*4	298,580	15,384	2,835	8,535	106,811	67,537	-	-	97,478	-	-
7	NET RETURN	Ln5-6	298,580	15,384	2,835	8,535	106,811	67,537	-	-	97,478	-	-
8	Fixed Charges	A-10, Ln25	48,675	2,642	482	1,482	15,534	11,649	-	-	16,884	-	-
15	Total Misc Inc Adjustment	A-10, Ln61	48,675	2,642	482	1,482	15,534	11,649	-	-	16,884	-	-
16	AFTER TAX INCOME	Note 1	249,906	12,741	2,353	7,053	91,277	55,888	-	-	80,593	-	-
17	State Income Tax	Ln59 less ITC	19,929	1,016	188	562	7,279	4,457	-	-	6,427	-	-
18	State ITC Amortization	A-10, Ln45	-	-	-	-	-	-	-	-	-	-	-
19	Net Federal Income Tax	Ln50	128,739	6,564	1,212	3,633	47,021	28,791	-	-	41,518	-	-
20	Federal ITC Amortization	A-10, Ln44	-	-	-	-	-	-	-	-	-	-	-
21	Operating Expenses & Taxes	A-3, Ln24	1,217,418	62,980	14,045	26,106	437,022	259,404	-	-	373,119	22,292	22,135
22	Uncollectibles	A-10, Ln57	-	-	-	-	-	-	-	-	-	-	-
23	Other Adjustments (Net RR)	Records	-	-	-	-	-	-	-	-	-	-	-
24	NET REVENUE REQUIREMENT	Ln7+19..23-24	1,664,666	85,944	18,281	38,837	598,133	360,189	-	-	518,541	22,292	22,135
25	Gross Receipts Tax	Note 2	-	-	-	-	-	-	-	-	-	-	-
26	7340 Alw Fds Used Dur Constr	A-10, Ln15	392	21	4	12	125	94	-	-	136	-	-
27	SUBTOTAL REVENUE REQUIREMENT	Ln24+25-26	1,664,274	85,923	18,277	38,825	598,008	360,095	-	-	518,406	22,292	22,135
28	Local Switching Support	LSS Algorithm	395,487				395,487						
29	6540 Access Expense - Federal Support	A-12, Ln22	15,000							15,000			
30	Adjusted Revenue Requirement x/LSS & 6540	Ln27-28-29	1,253,787	85,923	18,277	38,825	202,521	360,095	-	-	503,406	22,292	22,135
31	Transfer 30% of Local Sw Rev Req to CL	Ln30e*30%	-				(60,756)			60,756			
32	Interstate TIC Revenues	Records	(100,000)					(100,000)	-	-			
33	Revised Rev Req prior to TIC Reallocation	Ln30+31+32	1,109,361	85,923	18,277	38,825	141,765	260,095	-	-	564,162		
34	Distribution	Ln33/33a	100.0000%	7.7452%	1.6475%	3.4997%	12.7790%	23.4455%	-	-	50.8547%		
35	Interstate TIC Reallocation	Ln32a*34	100,000	7,745	1,648	3,500	12,779	23,445	-	-	50,855		
36	TOTAL REVENUE REQUIREMENT	Ln27+31-32+35	1,664,274	93,668	19,924	42,325	550,031	283,540	-	-	630,017	22,292	22,135

FCC Rules – Part 69

- ◆ Part 69 specifies how interstate costs are recovered through specific rate elements
 - 1 rate element applies to subscriber loop plant
 - ▶ Carrier Common Line
 - Costs between local switch and customer
 - » COE Category 4.13 – 100% assigned to CCL
 - » CWF Category 1 – 100% assigned to CCL
 - 2 primary sources of cost recovery
 - » EUCL/SLC assessed on end users
 - » Interstate Common Line Support

Part 69 – COE Recovery

Sample Telephone Company
 Study Area: 123456
 Study Year:

CENTRAL OFFICE EQUIPMENT

A-5
 Page 2 of 3

LINE	DESCRIPTION	SOURCE	INTERSTATE										
			JURIS TOTAL (a)	Special Access			Local Switching (e)	Transport		Carrier Common Line		B&C	
				Chan Term (b)	CM-Term (c)	CM-Facil (d)		Transmission (i)	Tandem Sw (j)	Pay (k)	BFP (l)	Record (m)	Process (n)
APPORTIONMENT FACTORS													
COE APPORTIONMENT													
32	2230 Central Office - Transmission												
33	Cat 4.1-Exchange Circuit												
34	4.11 Wideband Line	Direct	-	-									
35	Direct Assign-MSG	Direct											
36	-PL	Direct	109,001	109,001									
37	4.12 Ex Trk x/WB - Basic	Direct											
38	Direct Assign-MSG	Direct											
39	-PL	Direct											
43	4.13 Ex Line x/WB												
44	Joint MSG	Direct	177,573							-	177,573		
45	PL & Local	Direct	8,703	8,703									
46	Direct Assign-MSG	Direct											
47	-PL	Direct											
48	Cat 4.2-Interexchange												
51	4.22 Wideband												
52	Jt MSG-Access	Direct											
53	-Nonaccess	Direct											
54	PL TWX-Access	Direct											
55	-Nonaccess	Direct											
56	Direct Assign-MSG	Direct											
57	-PL	Direct	16,606	16,606									

Part 69 – CWF Recovery

Sample Telephone Company
 Study Area: 123456
 Study Year:

CABLE AND WIRE FACILITIES

LINE	DESCRIPTION	SOURCE	INTERSTATE											
			JURIS TOTAL (a)	Special Access			Local Switching (e)	Transport		Carrier Common Line		B&C		
				Chan Term (b)	CM-Term (c)	CM-Facil (d)		Transmission (i)	Tandem Sw (j)	Pay (k)	BFP (l)	Record (m)	Process (n)	
APPORTIONMENT FACTORS														
1	Cat 1.3 Equip Inter Loops Pct	Records	100.0000%								-	100.0000%		
C&WF CAT 1-2 APPORTIONMENT														
2	2410 Cable & Wire Facilities													
3	Cat 1-Exch Line x/WB													
4	1.1 Intra PL & WATS	Direct	-	-										
5	1.2 Inter PL & WATS	Direct	62,518	62,518										
6	1.3 Jointly Used	Direct	1,275,571								-	1,275,571		
7	Direct Assign-MSG	Direct	-								-	-		
8	-PL	Direct	-	-										
9	Total Category 1	Ln4..8	1,338,089	62,518	-	-	-	-	-	-	-	1,275,571	-	-
10	Cat 2-WB & Exch Trunk													
11	Ex Trk x/WB - joint message	Direct	-											
12	Ex Line WB - PL	Direct	-	-										
13	WB Line - MSG	Direct	-											
	-PL	Direct	47,201	47,201										
14	WB Trunk-MSG	Direct	-											
15	WB Trk Direct Assign-MSG	Direct	-											
16	-PL	Direct	-											
17	Total Category 2	Ln11..16	47,201	47,201	-	-	-	-	-	-	-	-	-	-



Overview of High Cost Loop Support

Federal USF

◆ 4 Separate Funds

- High Cost

- ▶ High Cost Loop/Model Support
 - Safety Net & Safety Valve
- ▶ Interstate Common Line/Access Support
- ▶ Local Switching Support

- Schools & Libraries

- Rural Health Care

- Low Income

◆ Supported through 1 end user surcharge

◆ Defined in §36 and §54 of the FCC's Rules

Federal USF

- ◆ High Cost Loop Support (§36.601)
 - Supports loop costs above the National Average Cost Per Loop
 - Capped as of 6/30/01 + the percentage increase in working loops each year since
 - NACPL is adjusted up or down to ensure that the fund does not exceed the cap
 - ▶ Frozen NACPL = \$240.00
 - ▶ NACPL Currently ≈ \$360

Federal USF

◆ High Cost Loop Support

- Every change to the cost study will have a corresponding change to the Federal USF and the NACPL
 - ▶ Support is not netted with interstate revenue requirement
- 2-Year payment lag
 - ▶ Annual submission (2008-1) based on costs from the previous year (2007) and support begins the following year (2009)

Federal USF

◆ High Cost Loop Support

- Separations Costs Not Included in HCLS

- ▶ General Support Facilities (2110)

- Associated Depreciation Reserve, Depreciation Expense and Deferred Taxes

- ▶ Plant Under Construction (2003)

- ▶ Access Expense/USF Expense (6540)

- Direct assigned to interstate in the cost study

- ▶ Customer Operations Expense (6610/6620)

Federal USF

◆ High Cost Loop Support

- Investments & Expenses that Increase HCLS
 - ▶ C&WF Category 1
 - ▶ COE Category 4.13
 - ▶ Expenses assigned to C&WF Category 1 and COE Category 4.13
- Investments & Expenses not assigned to these categories actually reduce HCLS

Federal USF

◆ High Cost Loop Support

● Corporate Operations Expense Cap

▶ Amount of Corporate Operations Expense allowed in Federal USF is capped

– 0-6000 Loops = Greater of

» $\$33.31 - (\$0.00246 * \text{Working Loops})$ per Loop/Month

» $\$50,000 / \text{Working Loops}$ per Loop/Month

– 6,000-18,005 Loops \approx $\$8.74$ - $\$18.57$ per Loop/Month

» $\$3.83 + \$88,429 / \text{Working Loops}$

– 18,006+ Loops \approx $\$8.74$ per Loop/Month

▶ Cap grows by the annual GDP-CPI

Federal USF

◆ High Cost Loop Support

- Study Area Cost Per Loop (SACPL)
 - ▶ Expenses assigned to CWF Category 1 and COE Category 4.13
 - ▶ Return on Investment @ 11.25% for C&WF Category 1 and COE Category 4.13
 - ▶ Divided by Total Working Loops = SACPL
 - USF supports only Category 1.3 Loops

Federal USF

◆ High Cost Loop Support

- Support Between NACPL & SACPL

- ▶ SACPL between 100-115% of the NACPL = 0%
- ▶ SACPL between 115-150% of the NACPL = 65%
- ▶ SACPL above 150% of the NACPL = 75%
- ▶ For Example:
 - SACPL of \$600 & NACPL of \$360
 - » Support = \$126.90 per Loop/Year



**Yin & Yang:
The Two Become One**

Yin & Yang - Investments

- ◆ Inverse relationship between cost recovery from separations and USF for investments and associated expenses
 - COE Switching – high cost study/low USF
 - COE Transmission
 - ▶ Subscriber Circuit – low cost study/high USF
 - ▶ Other – high cost study/low USF
 - CWF
 - ▶ Subscriber Line – low cost study/high USF
 - ▶ Other – high cost study/low USF

Yin & Yang - Investments

- ◆ Comparative impacts of \$100,000 investment assigned to different categories
 - DSL Equipment – 100% Interstate
 - ▶ Depreciation Rate = 10.00%
 - Switching Equipment – Weighted DEM \leq 85.00%
 - ▶ Depreciation Rate = 10.00%
 - Subscriber Circuit Equipment – SPF = 25%
 - ▶ Depreciation Rate = 10.00%
 - Subscriber Cable & Wire Facilities – SPF = 25%
 - ▶ Depreciation Rate = 4.00%
 - General Support Facilities \approx 40.00%
 - ▶ Depreciation Rate = 20.00%

Separations Impact

Sample Telephone Company Incremental Investment Analysis

	DSL		Switching		Subscriber COE		Subscriber C&WF		GSF	
	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2
Interstate Investment (100%/85%/25%/25%/40%)	\$ 50,000	\$ 100,000	\$ 42,500	\$ 85,000	\$ 12,500	\$ 25,000	\$ 12,500	\$ 25,000	\$ 20,000	\$ 40,000
Interstate A/D (10%/10%/10%/4%/20%)	\$ (2,500)	\$ (10,000)	\$ (2,125)	\$ (8,500)	\$ (625)	\$ (2,500)	\$ (250)	\$ (1,000)	\$ (2,000)	\$ (8,000)
Interstate Rate Base Impact	\$ 47,500	\$ 90,000	\$ 40,375	\$ 76,500	\$ 11,875	\$ 22,500	\$ 12,250	\$ 24,000	\$ 18,000	\$ 32,000
Interstate Rate of Return	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%
Interstate Return on Rate Base	\$ 5,344	\$ 10,125	\$ 4,542	\$ 8,606	\$ 1,336	\$ 2,531	\$ 1,378	\$ 2,700	\$ 2,025	\$ 3,600
Interstate Tax Gross Up (.34/.66)	\$ 2,753	\$ 5,216	\$ 2,340	\$ 4,434	\$ 688	\$ 1,304	\$ 710	\$ 1,391	\$ 1,043	\$ 1,855
Interstate Depreciation Expense	\$ 5,000	\$ 10,000	\$ 4,250	\$ 8,500	\$ 1,250	\$ 2,500	\$ 500	\$ 1,000	\$ 4,000	\$ 8,000
Interstate Revenue Requirement	\$ 13,097	\$ 25,341	\$ 11,132	\$ 21,540	\$ 3,274	\$ 6,335	\$ 2,588	\$ 5,091	\$ 7,068	\$ 13,455
2-Year Settlement Impact		\$ 38,438		\$ 32,672		\$ 9,609		\$ 7,679		\$ 20,523

Separations + HCLS Impact

Sample Telephone Company Incremental Investment Analysis

	DSL		Switching		Subscriber COE		Subscriber C&WF		GSF	
	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2
Interstate Investment (100%/85%/25%/25%/40%)	\$ 50,000	\$ 100,000	\$ 42,500	\$ 85,000	\$ 12,500	\$ 25,000	\$ 12,500	\$ 25,000	\$ 20,000	\$ 40,000
Interstate A/D (10%/10%/10%/4%/20%)	\$ (2,500)	\$ (10,000)	\$ (2,125)	\$ (8,500)	\$ (625)	\$ (2,500)	\$ (250)	\$ (1,000)	\$ (2,000)	\$ (8,000)
Interstate Rate Base Impact	\$ 47,500	\$ 90,000	\$ 40,375	\$ 76,500	\$ 11,875	\$ 22,500	\$ 12,250	\$ 24,000	\$ 18,000	\$ 32,000
Interstate Rate of Return	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%	11.25%
Interstate Return on Rate Base	\$ 5,344	\$ 10,125	\$ 4,542	\$ 8,606	\$ 1,336	\$ 2,531	\$ 1,378	\$ 2,700	\$ 2,025	\$ 3,600
Interstate Tax Gross Up (.34/.66)	\$ 2,753	\$ 5,216	\$ 2,340	\$ 4,434	\$ 688	\$ 1,304	\$ 710	\$ 1,391	\$ 1,043	\$ 1,855
Interstate Depreciation Expense	\$ 5,000	\$ 10,000	\$ 4,250	\$ 8,500	\$ 1,250	\$ 2,500	\$ 500	\$ 1,000	\$ 4,000	\$ 8,000
Interstate Revenue Requirement	\$ 13,097	\$ 25,341	\$ 11,132	\$ 21,540	\$ 3,274	\$ 6,335	\$ 2,588	\$ 5,091	\$ 7,068	\$ 13,455
2-Year Settlement Impact		\$ 38,438		\$ 32,672		\$ 9,609		\$ 7,679		\$ 20,523
2-Year USF Impact (2-Year Lag)		\$ (10,731)		\$ (10,731)		\$ 43,386		\$ 27,270		\$ (8,420)
Total Revenue Impact		\$ 27,707		\$ 21,941		\$ 52,995		\$ 34,949		\$ 12,103

Yin & Yang Expenses

- ◆ Comparative impacts of expenses booked to different accounts
 - \$10,000 Expense
 - ▶ COE
 - ▶ C&WF
 - ▶ GSF
 - ▶ Corporate Operations – Executive

Separations Ratios

DISTRIBUTION RATIOS FOR RATE BASE AND EXPENSES

ALLOCATION RATIOS	A/C Category	Total	INTERSTATE TOLL				INTRASTATE TOLL				LOCAL		
			InterLATA		IntraLATA		InterLATA		IntraLATA		EAS	User Defined	Other
			MSG (b)	PL (c)	MSG (d)	PL (e)	MSG (f)	PL (g)	MSG (h)	PL (i)	(j)	(k)	(l)
Operating Expenses and Taxes Summary													
Network Support	6110	100.0000%	35.3489%	4.0239%	-	-	-	-	14.8689%	0.9103%	16.0561%	-	28.7918%
General Support	6120	100.0000%	35.3489%	4.0239%	-	-	-	-	14.8689%	0.9103%	16.0561%	-	28.7918%
Central Office	6210	100.0000%	54.2665%	5.5862%	-	-	-	-	12.7210%	0.8256%	13.1560%	-	13.4448%
Information Orig/Term	6310	-	-	-	-	-	-	-	-	-	-	-	-
Cable and Wire Facilities	6410	100.0000%	25.4029%	7.8939%	-	-	-	-	15.1024%	0.9042%	16.5622%	-	34.1344%
Other Plant	6510	-	-	-	-	-	-	-	-	-	-	-	-
Network Operations	6530	100.0000%	35.3489%	4.0239%	-	-	-	-	14.8689%	0.9103%	16.0561%	-	28.7918%
Access Charge	6540	-	-	-	-	-	-	-	-	-	-	-	-
Federal Support	6540	100.0000%	100.0000%	-	-	-	-	-	-	-	-	-	-
Marketing	6610	100.0000%	36.1991%	8.1448%	-	-	-	-	27.1493%	1.3575%	-	-	27.1493%
Customer Service	6620	100.0000%	35.3980%	1.2056%	-	-	-	-	18.7926%	1.2419%	0.0523%	-	43.3097%
Corporate Operations - Executive and Planning	6710	100.0000%	36.9157%	5.7794%	-	-	-	-	14.9264%	0.9343%	12.7885%	-	28.6557%
Corporate Operations - General and Administrative	6720	100.0000%	39.6945%	5.5248%	-	-	-	-	14.2689%	0.8931%	12.2252%	-	27.3935%
Subtotal Operations Expense		100.0000%	38.2636%	5.3350%	-	-	-	-	14.6498%	0.9181%	13.5301%	-	27.3034%
Depreciation and Amortization	6560	100.0000%	39.0238%	4.6532%	-	-	-	-	14.6214%	0.9215%	15.6309%	-	25.1492%
Other Operating	7240	100.0000%	35.6811%	4.0032%	-	-	-	-	14.7925%	0.9057%	15.9736%	-	28.6439%
Equal Access		-	-	-	-	-	-	-	-	-	-	-	-
Fixed Charges	7500	100.0000%	36.7312%	3.9325%	-	-	-	-	14.6049%	0.8867%	15.7571%	-	28.0875%
Rent Revenue	5240	100.0000%	35.3489%	4.0239%	-	-	-	-	14.8689%	0.9103%	16.0561%	-	28.7918%
Total Operating Expense and Tax		100.0000%	38.1773%	5.2904%	-	-	-	-	14.6545%	0.9177%	13.6119%	-	27.3482%
Nonoperating Expense	7370												
Abandoned Construction		-	-	-	-	-	-	-	-	-	-	-	-
Contributions		100.0000%	38.7091%	5.6151%	-	-	-	-	14.5021%	0.9077%	12.4249%	-	27.8411%
Other Nonoperating		-	-	-	-	-	-	-	-	-	-	-	-
Allowance for Funds Used During Construction	7340	100.0000%	35.3489%	4.0239%	-	-	-	-	14.8689%	0.9103%	16.0561%	-	28.7918%
Other Income Adjustments	XXXX	-	-	-	-	-	-	-	-	-	-	-	-

Separations Impact

Sample Telephone Company Incremental Expense Analysis

	COE	CWF	GSF	Executive		Customer
				Uncapped	Capped	
Regulated Expense	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000
Part 36 Interstate Allocation Factor	59.85%	33.30%	39.37%	42.70%	42.70%	36.60%
Part 36 Revenue Requirement Impact	\$ 5,985	\$ 3,330	\$ 3,937	\$ 4,270	\$ 4,270	\$ 3,660
Part 69 Access Allocation Factor	100.00%	100.00%	99.00%	87.72%	87.72%	46.01%
Interstate Expense Recovery	\$ 5,985	\$ 3,330	\$ 3,898	\$ 3,745	\$ 3,745	\$ 1,684

Separations + HCLS Impact

Sample Telephone Company Incremental Expense Analysis

	COE	CWF	GSF	Executive		Customer
				Uncapped	Capped	
Regulated Expense	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000
Part 36 Interstate Allocation Factor	59.85%	33.30%	39.37%	42.70%	42.70%	36.60%
Part 36 Revenue Requirement Impact	\$ 5,985	\$ 3,330	\$ 3,937	\$ 4,270	\$ 4,270	\$ 3,660
Part 69 Access Allocation Factor	100.00%	100.00%	99.00%	87.72%	87.72%	46.01%
Interstate Expense Recovery	\$ 5,985	\$ 3,330	\$ 3,898	\$ 3,745	\$ 3,745	\$ 1,684
Annual USF Impact (2-Year Lag)	\$ 1,573	\$ 5,218	\$ 3,594	\$ 3,594	\$ -	\$ -
Total Revenue Impact	\$ 7,558	\$ 8,548	\$ 7,492	\$ 7,339	\$ 3,745	\$ 1,684

Separations & HCLS



A close-up photograph of fiber optic cables, showing the glowing ends of the fibers in shades of purple, yellow, and orange against a dark background.

Questions?

Thank You!