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Arizona Corporation Commission

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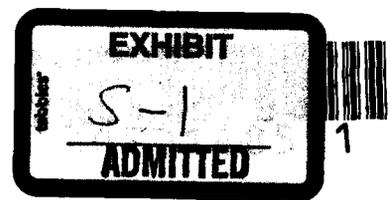
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Docket #(s): T-01923A-13-0229

Exhibit #: SL, A1

ORIGINAL



MEMORANDUM
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TO: Docket Control

2013 SEP 27 P 2:58

FROM: Steven M. Olea
Director
Utilities Division

AZ CORP COMMISSION
DOCKET CONTROL

Date: September 27, 2013

RE: IN THE MATTER OF THE APPLICATION OF SOUTH CENTRAL UTAH TELEPHONE ASSOCIATION, INC. FOR A HEARING TO DETERMINE THE EARNINGS OF THE COMPANY, THE FAIR VALUE OF THE COMPANY FOR RATEMAKING PURPOSES, AND TO INCREASE RESIDENTIAL RATES AS NECESSARY TO COMPENSATE FOR THE RATE IMPACTS OF THE FCC'S USF/ICC TRANSFORMATION ORDER (DOCKET NO. T-01923A-13-0229)

Attached is the Staff Report for South Central Utah Telephone Association dba South Central Communications' ("SCC" or "Applicant") Application to increase residential rates to compensate for the rate impacts of the Federal Communications Commission's Universal Service Fund/Intercarrier Compensation ("FCC's USF/ICC") Transformation Order.

Staff recommends approval of South Central Utah Telephone Association's request to increase its monthly residential local exchange service rate from \$11.00 to \$14.00 for customers in SCC's Colorado City base rate area, and from \$13.18 to \$14.00 for customers in SCC's Fredonia base rate area, effective December 1, 2013.

SMO:PJG:red\MAS

Originator: Pamela J. Genung

Attachment: Original and Thirteen copies

Arizona Corporation Commission

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SEP 27 2013

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**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

**SOUTH CENTRAL UTAH TELEPHONE ASSOCIATION, INC.
DOCKET NO. T-01923A-13-0229**

**IN THE MATTER OF THE APPLICATION OF SOUTH CENTRAL UTAH TELEPHONE
ASSOCIATION, INC. FOR A HEARING TO DETERMINE THE EARNINGS OF THE
COMPANY, THE FAIR VALUE OF THE COMPANY FOR RATEMAKING PURPOSES,
AND TO INCREASE RESIDENTIAL RATES AS NECESSARY TO COMPENSATE FOR
THE RATE IMPACTS OF THE FCC'S USF/ICC TRANSFORMATION ORDER**

SEPTEMBER 27, 2013

EXECUTIVE SUMMARY
SOUTH CENTRAL UTAH TELEPHONE ASSOCIATION INC.
DBA SOUTH CENTRAL COMMUNICATIONS
DOCKET NO. T-01923A-13-0229

On July 1, 2013, South Central Utah Telephone Association, Inc., dba South Central Communications ("SCC" or "Applicant") filed an Application for a determination of its earnings and the fair value of its investment and requested that its residential rates be increased as necessary to compensate for the rate impacts of the Federal Communication Commission's ("FCC's") November 18, 2011, USF/ICC Transformation Order ("USF/ICC Order") pursuant to Arizona Revised Statute ("A.R.S.") § 40-250 and the Arizona Corporation Commission's ("Commission") rules, Arizona Administrative Code ("A.A.C.") R14-2-103.

Staff recommends that the SCC monthly residence local exchange rate increase from \$11.00 to \$14.00 for customers in SCC's Colorado City base rate area, and from \$13.18 to \$14.00 for customers in SCC's Fredonia base rate area, to address the impact of the FCC's USF/ICC Order. Staff believes the proposed increase is just, fair and reasonable for the following reasons:

- The increase is necessitated by the FCC's November 18, 2011 USF/ICC Order;
- The increase is necessary to preserve the entirety of the Federal Universal Service Fund ("FUSF") funds that may flow to SCC pursuant to the FCC's rules;
- The increase will minimize/reduce the amount of future rate increase; and
- The increase will allow the Applicant to receive matching funds from the FUSF.

INTRODUCTION

On July 1, 2013, South Central Utah Telephone Association, Inc., dba South Central Communications ("SCC" or "Applicant") filed an Application for a determination of its earnings and the fair value of its investment and requested that its residential rates be increased as necessary to compensate for the rate impacts of the Federal Communication Commission's ("FCC's") November 18, 2011, USF/ICC Transformation Order ("USF/ICC Order") pursuant to Arizona Revised Statute ("A.R.S.") § 40-250 and the Arizona Corporation Commission's ("Commission") rules, Arizona Administrative Code ("A.A.C.") R14-2-103. A.A.C. R14-2-103(A)(1) requires specific financial and statistical information be filed with a request by a public service corporation doing business in Arizona for a determination of the value of the property of the corporation and of the rate of return earned. SCC submitted a streamlined filing containing the following five exhibits to support the requested increase in residential rates:

- Regulated 2012 Results of Operations Twelve Months Ending December 31, 2012
- 2012 Rate Base
- Calculation of Cash Working Capital
- Proposed Rate Design
- Estimated ICC Impact of FCC Order

On August 14, 2013, the Applicant filed a Motion for Procedural Order.

On August 15, 2013, the Hearing Division filed a Rate Case Procedural Order setting a Hearing, associated procedural deadlines, and directions for providing public notice of the Application and the Hearing.

BACKGROUND

SCC is a non-profit corporation duly organized and existing under and by virtue of the laws of the State of Utah. SCC is authorized to conduct a general communications business within the State of Arizona. SCC is a small rate-of-return ("RoR") regulated incumbent local exchange carrier ("ILEC").

On November 18, 2011, the FCC issued the USF/ICC Order. The USF/ICC Order transitions the outdated federal universal service programs and most intercarrier compensation systems into a new Connect America Fund ("CAF"). The FCC's press release characterized the USF/ICC Order as "the most significant policy step ever taken to connect all Americans to broadband."

In its USF/ICC Order, the FCC stated that it will reduce intercarrier compensation rates to zero by July 1, 2020, for RoR companies, with limited recovery from customers and partial recovery from the CAF. The recovery from the CAF will phase out over time at 5 percent annually. The USF/ICC Order adds new rules that will reduce federal high-cost loop support

Local	\$278,898
Intrastate	\$209,173
Miscellaneous	\$4,386
Uncollectible	\$19,026

The Applicant also stated that its Total Intrastate Operating Expenses for the Twelve Months Ending December 31, 2012, were \$368,223. Subcategories of Total Intrastate Operating Expenses are noted below:

Plant Specific Operations	\$74,148
Plant Non-specific Operations	\$6,131
Depreciation	\$143,931
Marketing	\$15,776
Customer Operations	\$53,410
Corporate Operations	\$74,827

Operating Income

As provided by the Applicant, SCC Total Intrastate Operating Income for the Twelve Months Ending December 31, 2012, was \$143,260 before taxes and \$80,192 after taxes.

RATE BASE

According to SCC, the combined Interstate and Intrastate rate base is \$1,584,705, as stated in the table below:

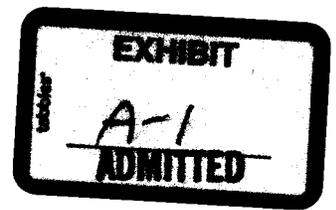
**South Central Utah Telephone Association, Inc.
2012 Rate Base**

	Total Company	Interstate	Intrastate
Plant In Service	7,538,550	3,509,851	4,028,699
Accumulated Depreciation	<u>6,154,077</u>	<u>3,190,187</u>	<u>2,963,890</u>
Net Plant in Service	1,384,473	319,663	1,064,809
Plant Under Construction	417	197	220
Material & Supplies	-	-	-
Deferred Income Taxes	-	-	-
Other Long Term Liabilities	162,392	75,608	86,784
Customer Deposits	4,850	2,291	2,559
Cash Working Capital	<u>32,573</u>	<u>15,004</u>	<u>17,569</u>
Rate Base	1,584,705	412,763	1,171,942

area, and from \$13.18 to \$14.00 for customers in SCC's Fredonia base rate area, beginning December 1, 2013, to address the impact of the FCC's USF/ICC Order. Staff believes the proposed increase is just, fair and reasonable for the following reasons:

- The increase is necessitated by the FCC's November 18, 2011 USF/ICC Order;
- The increase is necessary to preserve the entirety of the Federal Universal Service Fund ("FUSF") funds that may flow to SCC pursuant to the FCC's rules;
- The increase will minimize/reduce the amount of future rate increase; and
- The increase will allow the Applicant to receive matching funds from the FUSF.

Staff has reviewed the rate application and the federal rule changes that have prompted the rate application. Staff concludes that the costs appear reasonable and appropriate under the unique circumstances of this case. However, Staff's recommendation in these unique circumstances should not be viewed as precedent for the processing of future rate case applications.



BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

IN THE MATTER OF THE APPLICATION OF SOUTH CENTRAL UTAH TELEPHONE ASSOCIATION, INC., A UTAH NON-PROFIT CORPORATION, FOR A HEARING TO DETERMINE THE EARNINGS OF THE COMPANY, THE FAIR VALUE OF THE COMPANY FOR RATEMAKING PURPOSES, AND TO INCREASE RESIDENTIAL RATES AS NECESSARY TO COMPENSATE FOR THE RATE IMPACTS OF THE FCC'S USF/ICC TRANSFORMATION ORDER

DOCKET NO. T-01923A-12-

APPLICATION FOR EXPEDITED RATE INCREASE

1 South Central Utah Telephone Association, Inc., a non-profit Utah corporation, doing
2 business as South Central Communications ("SCC"), hereby applies pursuant to A.R.S. § 40-250
3 and the Commission's Rule R 14-2-103 for a determination of SCC's earnings and the fair value
4 of the company and requests that its residential rates be increased as necessary to compensate for
5 the rate impacts of the Federal Communication Commission's November 18, 2011, USF/ICC
6 Transformation Order ("USF/ICC Order").

7 **I. BACKGROUND**

8 On November 18, 2011, the Federal Communications Commission issued the USF/ICC
9 Order. The USF/ICC Order transitions the outdated federal universal service programs and most
10 inter-carrier compensation systems into a new Connect America Fund ("CAF"). The FCC's
11 press release characterized the USF/ICC Order as "the most significant policy step ever taken to
12 connect all Americans to broadband."

13 The USF/ICC Order will reduce certain terminating inter-carrier compensation rates to
14 zero by July 1, 2020, for rate of return companies, with limited recovery from customers and

1 partial recovery from the CAF. The recovery from the CAF will be reduced over time at 5%
2 annually.

3 SCC is a small rate-of-return regulated Incumbent Local Exchange Carrier (“ILEC”). Of
4 particular importance to SCC and other rural ILECs, the USF/ICC Order adds new rules that will
5 reduce federal high-cost loop support to carriers by the amount their flat-rate residential local
6 service rates fall below a specified annual urban rate floor.¹ The rate floor includes, if any, state
7 subscriber line charges, state universal service fees, and mandatory extended area service
8 charges. The FCC’s order establishes local residential rate floors of \$10.00 as of June 1, 2012,
9 and \$14.00 as of June 1, 2013, with the floor thereafter being determined annually by the FCC’s
10 Wireline Competition Bureau, based on a nationwide average.²

11 Federal and state support funding are vital to a robust telecommunications network in
12 high cost areas. To maintain federal loop support, SCC and other rural ILECs must increase
13 local rates to the FCC-mandated residential rate floors. Otherwise, the amount of federal support
14 funds will be reduced dollar-for-dollar for each customer by the difference between the existing
15 local rate and the new rate floor. If local rates are not increased, the new FCC rules will reduce
16 funds coming to the state of Arizona and negatively impact customers living in high-cost areas in
17 the state.

18 Low customer density makes SCC dependent on high-cost federal support mechanisms.
19 It is important that the company be allowed to increase local rates, to the FCC determined annual
20 rate floors, in order to maintain its existing federal support. Therefore, SCC requests the
21 Commission to approve local rate increases to the \$14 rate floor established by the FCC’s order.

22 **II. SCC**

23 South Central Utah Telephone Association, Inc. is a non-profit corporation duly
24 organized and existing under and by virtue of the laws of the State of Utah and authorized to

¹ 41 C.F.R § 54.318.

² USF/ICC Order paragraph 236 states the most recently available nationwide average local rate from 2008 was \$15.62.

1 conduct a general communications business within the State of Arizona. SCC is an Arizona
2 public service corporation within the meaning of Article XV, Section 2, of the Arizona
3 Constitution.

4 South Central Utah Telephone Association, Inc. is a member-owned telecommunications
5 cooperative, doing business as South Central Communications ("SCC"). In addition to its
6 customers in Utah, SCC provided service in 2012 to an average of 307 residential customers in
7 and around Colorado City, Arizona, and 372 residential customers in and around Fredonia,
8 Arizona.³

9 **III. SUMMARY OF REQUEST**

10 This application is made pursuant to the provisions of A.R.S. §§ 40-250 and 40-367, and
11 Commission Rule R14-2-103.

12 In its Colorado City rate area, SCC's local residential rates are currently \$11.00/month.
13 In its Fredonia rate area, SCC's local residential rates are currently \$13.18/month. The rates for
14 customers within these rate areas are below the federal \$14/month rate floor that went into effect
15 on June 1, 2013. The rate floor for 2014 and thereafter will be determined by an annual FCC
16 survey.

17 SCC is aware that many parties, including the Commission, have appealed the USF/ICC
18 Order. However, in the meantime, SCC and other rural ILECS must comply with all provisions
19 of the USF/ICC Order and will remain subject to the increased local residential rate floors and
20 the corresponding losses of federal support funds.

21 SCC's loss of federal support funds would be particularly difficult to bear. As the
22 attached schedules demonstrate, SCC's return on investment is already low. Losing federal
23 support funds would only drive earnings lower.

24 In connection with this application, SCC attaches Exhibit A which include a schedule of
25 the specific rate changes requested and the impact of the revenue generated on the company's

³ Business customers will not be affected by this rate request.

1 financial position. SCC asks that the Commission determine the fair value of the company for
2 ratemaking purposes and stipulates to use original cost less depreciation for those purposes.
3 Because the next opportunity to affect federal support funds is December 1, 2013, SCC further
4 asks that the Commission set new rates at the \$14.00 floor to be effective no later than December
5 1, 2013.

6 To facilitate processing of this application, SCC asks that the Commission waive any
7 provisions of Commission Rule R14-2-103 not required by the Arizona Constitution and laws.

8 Respectfully submitted on July 1, 2013.

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/s/Craig A. Marks
Craig A. Marks
Craig A. Marks, PLC
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Attorney for South Central Utah Telephone
Association, Inc.

Original and 13 copies filed
on July 1, 2013, with:

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

By: /s/Craig A. Marks
Craig A. Marks

South Central Utah Telephone Association, Inc.

as of December 31, 2012

Exhibit A

REGULATED 2012 RESULTS OF OPERATIONS
REFLECTS CHANGES EFFECTIVE WITH ARC AND CAF IMPLEMENTATION - YEAR 1

	2012 TOTAL TELEPHONE OPERATIONS			ADJUSTED 2012 RESULTS		
	OPERATIONS (a)	ADJUSTMENTS (b)	Ref (c)	INTERSTATE (d)	INTERSTATE (e)	INTRASTATE (f)
<u>OPERATING REVENUES</u>						
1	Local	\$ 278,898		\$ 278,898		\$ 278,898
2	Interstate	804,017	(54,217) *	749,799	749,799	-
3	Intrastate	209,173		209,173		209,173
4	Message Toll	-		-		-
5	Miscellaneous	4,386		4,386		4,386
6	Uncollectible	19,026		19,026		19,026
7		<u>\$ 1,315,499</u>	<u>\$ (54,217)</u>	<u>\$ -</u>	<u>\$ 1,261,282</u>	<u>\$ 749,799</u>
						<u>\$ 511,483</u>
<u>OPERATING EXPENSES</u>						
8	Plant Specific Operations	\$ 140,087		\$ 140,087	65,939	\$ 74,148
9	Plant Non-specific Operations	11,620		11,620	5,489	6,131
10	Depreciation	298,852		298,852	154,921	143,931
11	Marketing	23,600		23,600	7,823	15,776
12	Customer Operations	79,896		79,896	26,486	53,410
13	Corporate Operations	138,593		138,593	63,767	74,827
14		<u>\$ 692,647</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 324,424</u>	<u>\$ 368,223</u>
15	<u>OPERATING INCOME</u>	<u>\$ 622,853</u>	<u>\$ (54,217)</u>	<u>\$ -</u>	<u>\$ 425,376</u>	<u>\$ 143,260</u>
16	<u>OPERATING TAXES</u>	122,450		122,450	59,382	63,068
17	<u>NET OPERATING INCOME</u>	<u>\$ 500,403</u>	<u>\$ (54,217)</u>	<u>\$ -</u>	<u>\$ 365,994</u>	<u>\$ 80,192</u>
<u>NON-OPERATING INCOME</u>						
18	Interest Income	\$ 4,355		4,355	1,413	\$ 2,942
19	Interest on Funded Debt	(15,470)		(15,470)	(5,019)	(10,452)
20	CoBank dividends	-		-		-
21	Other	1,535		1,535	706	829
22		<u>\$ (9,580)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,900)</u>	<u>\$ (6,680)</u>
23	<u>NET OPERATING INCOME</u>	<u>\$ 490,823</u>	<u>\$ (54,217)</u>	<u>\$ -</u>	<u>\$ 363,094</u>	<u>\$ 73,511</u>
24	Total Year-End Rate Base	1,584,705			412,763	1,171,942
25	Return on Rate Base (Ln 23/Ln24)					6.27%
26	Estimated Revenue from Local Rate Increase					\$ 14,698
27	Net Operating Income After Increase (Ln 23 + Ln 26)					\$ 88,210
28	Return on Rate Base After Increase (Ln 27/Ln 24)					7.53%

ASSUMPTIONS

Audited 2012 financial statements
Used 2011 cost study factors (latest available factors)

Ref Notes

* Prior period adjustments as per NECA 3050

South Central Utah Telephone Association, Inc.

2012 Rate Base

	Total Company	Interstate	Intrastate
Plant In Service	7,538,550	3,509,851	4,028,699
<i>Accumulated Depreciation</i>	6,154,077	3,190,187	2,963,890
Net Plant in Service	1,384,473	319,663	1,064,809
Plant Under Construction	417	197	220
Material & Supplies	-	-	-
Deferred Income Taxes	-	-	-
Other Long Term Liabilities	162,392	75,608	86,784
Customer Deposits	4,850	2,291	2,559
Cash Working Capital	32,573	15,004	17,569
Rate Base	1,584,705	412,763	1,171,942

South Central Utah Telephone Association, Inc.

CALCULATION OF CASH WORKING CAPITAL (CWC)

Plant Specific Operations Expense	140,087	
Plant Non-Specific Operations Expense Excluding Depreciation and Amortization	11,620	
Customer Operations Expense	103,495	
Corporate Operations Expense	138,593	
Contributions	-	
Interest on Customer Deposits	-	
Operating Taxes	122,450	
Interest Expense - Operating	15,470	
Total Annual Expense	531,715	
Cash Working Capital Factor	0.06126	22.36/365
Cash Working Capital Base	32,573	
Minimum Cash Balance	-	
Working Cash Allowance	-	
Total Cash Working Capital	32,573	

South Central Utah Telephone Association, Inc.

Proposed Rate Design
2012 Average Units

(A) Service Description	(B) Average Units	(C) Current Rates	(D) 2012 Annual Revenues	(E) Proposed Rates		(F) Proposed Revenues		(G) Proposed Change		(H) Percent
				Rates	Revenues	Revenues	Revenue	Revenue	Percent	
Basic Service	307	\$ 11.00	\$ 40,469.00	\$ 14.00	\$ 51,506.00	\$ 11,037.00	27.27%			
Residence in Colorado City Base Rate Area (CLCY)	372	\$ 13.18	\$ 58,848.70	\$ 14.00	\$ 62,510.00	\$ 3,661.30	6.22%			
Residence in Fredonia Base Rate Area (FRDN)						\$ 14,698.30				
Estimated Revenue from Local Rate Increase										

Year	Area	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2012	CLCY	315	319	321	316	313	314	305	303	295	291	292	295
2012	FRDN	393	389	381	379	374	371	367	366	361	363	363	358
2012 Total		708	708	702	695	687	685	672	669	656	654	655	653

Multi-line business Lines

Year	Area	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2012	CLCY	199	199	202	203	202	201	196	194	194	190	180	172
2012	FRDN	176	177	178	180	181	181	180	180	178	173	173	173
2012 Total		375	376	380	383	383	382	376	374	372	363	353	345

Total AZ Lines

CLCY	514	518	523	519	515	515	515	501	497	489	481	472	467
FRDN	569	566	559	559	555	555	552	547	546	539	536	536	531
	1083	1084	1082	1078	1070	1070	1067	1048	1043	1028	1017	1008	998

462
507
970

South Central Utah Telephone Association, Inc.

Estimated ICC Impact of FCC Order

Base Line of Eligible Recovery:

	Total	Estimated Revenue Reduction		
Interstate SWA (Includes LSS)	83,010	4,151	Access Revenue	Interstate
Intrastate Terminating Access	57,774	2,889	Access Revenue	Intrastate Access
Recip Comp Revenue	0	0	Local Revenue	Intrastate Local
Recip Comp Expense	0	0	Plant Non-Specific	Intrastate Local
Total Base of Eligible Recovery	<u>140,784</u>	<u>7,039</u>		