

ORIGINAL NEW APPLICATION



0000149863

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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

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AZ CORP. COMMISSION
DOCKET CONTROL

2013 NOV 27 PM 3 13

IN THE MATTER OF THE APPLICATION OF ARIZONA TELEPHONE COMPANY, AN ARIZONA 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-02063A-13-0411

APPLICATION

Arizona Corporation Commission

DOCKETED

NOV 27 2013

DOCKETED BY

1 Arizona Telephone Company ("Arizona Telephone"), an Arizona corporation, hereby
2 applies pursuant to A.R.S. § 40-250 and the Commission's Rule R 14-2-103 for a determination
3 of Arizona Telephone's earnings and the fair value of its investment and requests that its
4 residential rates be increased as necessary to compensate for the rate impacts of the Federal
5 Communication Commission's November 18, 2011, USF/ICC Transformation Order ("USF/ICC
6 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 The USF/ICC Order transitions the outdated federal universal service programs and most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."

1 The USF/ICC Order will reduce inter-carrier compensation rates to zero by July 1, 2020,
2 for rate of return companies, with limited recovery from customers and partial recovery from the
3 CAF. The recovery from the CAF will phase out over time at 5% annually.

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

13 The Wireline Competition Bureau has not yet determined the rate floor to be in effect for
14 June 1, 2014. The nationwide residential average rate was \$15.62 in 2008. Estimates for the
15 2013 nationwide residential average rate range from \$17.00 to \$18.50, so the 2014 rate floor will
16 certainly be substantially higher than 2013’s \$14.00 rate floor.

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

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 Low customer density makes Arizona Telephone dependent on high-cost federal support
2 mechanisms. It is important that the company be allowed to increase local rates to the FCC
3 determined annual rate floors in order to maintain its existing federal support.

4 The Wireline Competition Bureau is not expected to set the 2014 rate floor until the end
5 of this quarter or the first quarter of 2014. If the rate floor is not set until 2014, it could be
6 difficult for the Commission to timely review an application and authorize new rates for Arizona
7 Telephone by June 1, 2014. This would cause Arizona Telephone to lose federal high-cost loop
8 support dollar-for-dollar by the amount the new rate floor exceeds current \$14 residential rates.

9 To prevent the loss of federal support, Arizona Telephone requests that the Commission
10 approve a local residential rate increase of up to \$19.00. The actual rate implemented would be
11 set at the lower of the approved 2014 residential rate floor and \$19.00. Arizona Telephone will
12 file the new FCC rate floor as soon as it is available.

13 **II. ARIZONA TELEPHONE**

14 Arizona Telephone Company is a corporation duly organized and existing under and by
15 virtue of the laws of the State of Arizona. Arizona Telephone is authorized to engage in and is
16 now engaged in the conduct of a general communications business within the State of Arizona.

17 **III. SUMMARY OF REQUEST**

18 This application is made pursuant to the provisions of A.R.S. §§ 40-250 and 40-367, and
19 Commission Rule R14-2-103. The Commission last considered Arizona Telephone's rates in
20 Docket No. T-02063A-12-0473, which resulted in Commission Decision 73873 issued on May
21 8, 2013. Decision No. 73873 authorized Arizona Telephone to raise its residential one-party
22 rates to \$14.00/month, effective June 1, 2013. As discussed above, these rates are substantially
23 below the expected federal rate floor that will go into effect on June 1, 2014.

24 Arizona Telephone is aware that many parties, including the Commission, have appealed
25 the USF/ICC Order. However, in the meantime, Arizona Telephone and other rural ILECS must
26 comply with all provisions of the USF/ICC Order and will remain subject to the increased local
27 residential rate floors and the corresponding losses of federal support funds.

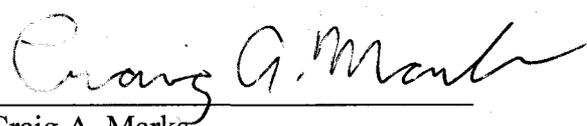
1 Arizona Telephone's loss of federal support funds would be particularly difficult to bear.
2 As the attached schedules demonstrate, Arizona Telephone's return on investment is negative at
3 current rates. Put another way, Arizona Telephone's jurisdictional earnings are negative. Losing
4 federal support funds will only drive earnings deeper into the red.

5 In connection with this application, Arizona Telephone has filed exhibits which include a
6 schedule of the specific rate changes requested and the impact of the revenue generated on the
7 company's financial position. Arizona Telephone asks that the Commission determine the fair
8 value of the company's investments for ratemaking purposes and stipulates to use original cost
9 less depreciation for those purposes. Because the next opportunity to affect federal support
10 funds is June 1, 2014, Arizona Telephone further asks that the Commission approve a local
11 residential rate of up to \$19.00. At \$19.00, Arizona Telephone's return on rate base would still
12 be negative. The actual rate implemented would be set at the lower of the approved 2014
13 residential rate floor and \$19.00, so the actual return on rate base would be negative at any rate
14 up to \$19.00. Arizona Telephone asks that the customer notice issued by the Hearing Division
15 inform customers of this potential range of rate increases.

16 To facilitate processing of this application, Arizona Telephone also asks that the
17 Commission waive any provisions of Commission Rule R14-2-103 not required by the Arizona
18 Constitution and laws.

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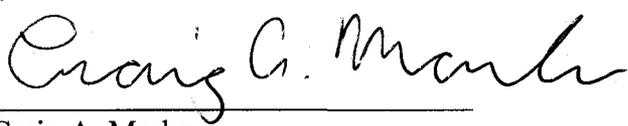
Respectfully submitted on November 27, 2013.



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Original and 13 copies **filed**
on November 27, 2013, with:

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

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Arizona Telephone Company

Streamlined filing to support residential rate increase due to FCC
floor implementation and resulting HCL loss.

November 15, 2013

Arizona Telephone Company

November 15, 2013

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Arizona Telephone Company

November 15, 2013

REGULATED RESULTS OF OPERATIONS FOR TWELVE MONTHS ENDING JUNE 30, 2013
REFLECTS CHANGES EFFECTIVE WITH ARC AND CAF IMPLEMENTATION -- YEAR 2

	TOTAL TELEPHONE OPERATIONS (a)	ADJUSTMENTS (b)	Ref (c)	ADJUSTED RESULTS (d)	INTERSTATE (e)	INTRASTATE (f)
1 Local	460,779	-4,869 #6		455,910	0	455,910
2 Universal Service Fund (USF-HCL)	116,163	2,019 #5,7		118,182	0	118,182
3 Access Revenues	2,079,339	#1,2,3,4		2,047,141	1,680,272	366,869
4 Billing & Collecting	21,178	16 #5		21,194	3,127	18,067
5 Other Misc., Uncollectibles	55,084			55,084	22,131	32,953
6 Total Operating Revenues	2,732,543	-35,032		2,697,511	1,705,530	991,981
7 Plant Specific Expenses	820,141	2,522 #12		822,663	405,382	417,281
8 Plant Nonspecific Expenses	370,813	-878 #6,12		369,935	207,395	162,539
9 Depreciation & Amortization Expenses	898,699	3,685 #12		902,384	406,934	495,450
10 Customer Operations Expenses	332,260	304 #1,1,2		332,564	99,927	232,637
11 Corporate Operations Expenses	523,074	1,122 #12		524,196	199,972	324,224
12 Other Operating Taxes and (Income)	140,625	5,589 #9,10,12		146,214	70,938	75,276
13 Nonregulated Adjustment (Part 69 WBI)		-9,856 #12		-9,856		0
14 Total Operating Expenses	3,085,612	2,488		3,088,100	1,380,693	1,707,407
15 OPERATING RETURN BEFORE TAXES	-353,069	-37,520		-390,589	324,837	-715,426
16 State Income Taxes (SIT) (6.97%)	62,252	-89,476 #13		-27,224	22,641	-49,865
17 Federal Income Taxes (FIT) (35%)	-115,801	-11,377 #13		-127,178	105,769	-232,946
18 Total Operating Income Taxes	-53,549	-100,853		-154,402	128,410	-282,811
19 Total Expenses and Income Taxes	3,032,063	-98,365		2,933,698	1,509,103	1,424,596
20 Net Operating Income	-299,520	63,333		-236,187	196,427	-432,615
21 Total Year-End Rate Base	3,921,169	0		3,921,169	1,629,233	2,291,937
22 Return on Rate Base (Ln 20 / Ln 21)						-18.9%
23 Estimated Revenue from Local Rate Increase						102,780
24 State Income Taxes (SIT) (6.97%)						7,164
25 Federal Income Taxes (FIT) (35%)						33,466
26 Increase in Net Operating Income						62,151
27 Net Operating Income After Increase (Ln 20 + Ln 26)						-370,464
28 Return on Rate Base After Increase (Ln27 / Ln21)						-16.2%

ASSUMPTIONS

Used 2012 Cost Study run dated 07/15/2013 for Part 36 separation of expenses.
Separated results based upon frozen 2000 traffic factors
Separated results based upon 6/30/2013 financials, interstate rules, adjusted for Part 64 activities
Working Capital included for all jurisdictions

Arizona Telephone Company
Adjustments to Revenues and Expenses

Ref	Account	Description	Debit	Credit
1.	5082200	Access Revenues		449
	5083000	Access Revenues		303
	Exclude		752	
		To remove prior period (2009) interstate revenue requirement adj.		
2.	5082200	Access Revenues		887
	5083000	Access Revenues		600
	Exclude		1,487	
		To remove prior period (2010) interstate revenue requirement adj.		
3.	5082100	Access Revenues	22,826	
	5082200	Access Revenues		16,878
	5083000	Access Revenues	4,069	
	Exclude			10,017
		To remove prior period (2011) interstate cost study true-up.		
4.	5082200	Access Revenues		9,495
	5083000	Access Revenues		6,812
	Exclude		16,307	
		To remove prior period (2011) interstate revenue requirement adj.		
5.	5270100	Interstate B&C		16
	PPA		16	
		To remove prior period adjustment.		
6.	5082110	Universal Service Fund		6,171
	K&M		6,171	
		To adjust for Federal HCL projected change for 2013.		
7.	5082110	Universal Service Fund	4,152	
	5082100	Access Revenues		139
	5082200	Access Revenues		1,140
	PPA			2,873
		To remove prior period HCL/LSS/ICLS revenues.		
8.	5001000	Local Revenues	4,869	
	5082200	Access Revenues	28,994	
	5084220	Access Revenues	13,012	
	6540010	Plant Nonspecific Exp		1,556
	Exclude			45,319
		Year 2 FCC Order ICC intrastate and interstate revenue and expense reductions.		
9.	7240300	Other Operating Taxes	3,429	
	PPA			3,429
		To remove prior period property tax true-ups.		
10.	7240200	Other Operating Taxes	634	
	Exclude			634
		To true-up 2012 assessment.		

Arizona Telephone Company
Adjustments to Revenues and Expenses

Ref	Account	Description	Debit	Credit
11.	6623304	Customer Operations Exp		19
	PPA		19	
		To remove aging balance.		
12.	6112004	Plant Specific Exp	11	
	6121004	Plant Specific Exp	334	
	6232004	Plant Specific Exp	2,177	
	6532004	Plant Nonspecific Exp	678	
	6561000	Depreciation Exp	3,685	
	6611004	Customer Operations Exp	265	
	6623304	Customer Operations Exp	58	
	6728904	Corporate Operations Exp	1,122	
	7130000	Other Operating Income	1,307	
	7240900	Other Operating Taxes	219	
	7990000	Nonregulated Exp		9,856
		To reverse transfer of estimated Part 69 interstate expenses for WBI (Internet) to enable proper Part 36 allocation of total company expenses.		
13.	7220000	Federal Income Tax		11,377
	7230020	State Income Tax		89,476
	PPA		100,853	
		Adjust income taxes to remove prior period amounts and for adjustments to results.		

Arizona Telephone Company
 Year 2 Estimated ICC Impact of FCC Order

Base Line of Eligible Recovery:

	Total	Reduction	
Interstate SWA (Includes LSS)	610,396	(28,994)	Access Revenue Interstate
Intrastate Terminating Access	276,591	(13,012)	Access Revenue Intrastate Access
Recip Comp Revenue	102,501	(4,869)	Local Revenue Intrastate Local
Recip Comp Expense	(32,764)	1,556	Plant Non-Specific Intrastate Local
Total Base of Eligible Recovery	956,724	(45,319)	
			AJE #8

Arizona Telephone Company

Rate Base

As of June 30, 2013

	Total Company	INTERSTATE	INTRASTATE
Plant in Service	\$ 21,227,431	\$ 10,160,505	\$ 11,066,926
Accumulated Depreciation	(18,319,033)	(9,021,096)	(9,297,937)
Net Plant in Service	\$ 2,908,398	\$ 1,139,409	\$ 1,768,989
Plant Under Construction	974,495	465,159	509,336
Material & Supplies	33,078	11,480	21,598
Deferred Income Taxes	(164,010)	(78,626)	(85,384)
Cash Working Capital	169,208	91,811	77,398
Rate Base	\$ 3,921,169	\$ 1,629,233	\$ 2,291,937

Arizona Telephone Company
For Twelve Ending June 30, 2013

CALCULATION OF CASH WORKING CAPITAL (CWC)

CASH OPERATING EXPENSES	Total Company	INTERSTATE	INTRASTATE
Total Operating Expenses	\$ 3,088,100	\$ 1,380,693	\$ 1,707,407
Less Depreciation & Amortization	902,384	406,934	495,450
Cash Operating Federal Income Taxes	(127,178)	105,769	(232,946)
Cash Operating State & Local Taxes	(27,224)	22,641	(49,865)
Total Cash Operating Expenses	\$ 2,031,314	\$ 1,102,169	\$ 929,146
% LAG (30 days)	8.33%	8.33%	8.33%
TOTAL CASH WORKING CAPITAL	<u>\$ 169,208</u>	<u>\$ 91,811</u>	<u>\$ 77,398</u>

Arizona Telephone Company
Proposed Rate Design
2013 June Units

(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)
Service Description	Jun-13 Units (a)	Current Rate	Annual Revenues	Proposed Rates	Proposed Revenues	Proposed Revenue	Proposed Change Percent
Basic Service							
Residence One-Party	1,712	\$ 14.00	\$ 287,616	\$ 19.00	\$ 390,336	\$ 102,720	35.71%
Residence Four-Party	1	\$ 14.00	\$ 168	\$ 19.00	\$ 228	\$ 60	35.71%
Estimated Revenue from Local Rate Increase						<u>\$ 102,780</u>	

Notes:
(a) No reduction made for line loss.

Year	Type	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2009	One-Party	2,898	2,888	2,872	2,865	2,858	2,922	2,927	2,849	2,785	2,718	2,602	2,532
2009	Four-Party	13	13	13	13	13	13	13	13	13	13	13	12
2009 Total		2,911	2,901	2,885	2,878	2,871	2,935	2,940	2,862	2,798	2,731	2,615	2,544
2010	One-Party	2,502	2,461	2,434	2,404	2,375	2,412	2,405	2,382	2,365	2,334	2,288	2,217
2010	Four-Party	11	11	11	11	11	11	10	10	10	10	7	7
2010 Total		2,513	2,472	2,445	2,415	2,386	2,423	2,415	2,392	2,375	2,344	2,295	2,224
2011	One-Party	2,195	2,177	2,167	2,154	2,146	2,178	2,169	2,159	2,154	2,125	2,069	2,031
2011	Four-Party	7	7	7	6	6	6	6	6	6	6	6	5
2011 Total		2,202	2,184	2,174	2,160	2,152	2,184	2,175	2,165	2,160	2,131	2,075	2,036
2012	One-Party	1,993	1,976	1,955	1,942	1,939	1,969	1,961	1,951	1,932	1,890	1,846	1,811
2012	Four-Party	5	5	5	5	5	5	5	5	5	5	4	3
2012 Total		1,998	1,981	1,960	1,947	1,944	1,974	1,966	1,956	1,937	1,895	1,850	1,814
2013	One-Party	1,788	1,758	1,741	1,708	1,690	1,712	1,712	1,712	1,712	1,712	1,712	1,712
2013	Four-Party	1	1	1	1	1	1	1	1	1	1	1	1
2013 Total		1,789	1,759	1,742	1,709	1,691	1,713	1,713	1,713	1,713	1,713	1,713	1,713