

NATIONAL EXCHANGE CARRIER ASSOCIATION, INC.

OVERVIEW AND ANALYSIS OF 2013 USF DATA SUBMISSION

I. BACKGROUND

Section 36.613 of the Commission's rules requires NECA to file Universal Service Fund (USF) cost and expense adjustment information annually with the Commission and the Administrator¹ on October 1st each year.² The information in this filing is compiled from data as of December 31, 2012 supplied to NECA by Rural rate of return exchange carriers (RLECs) on or before July 31, 2013 as specified in section 36.611 of the Commission's rules.³ As in prior years, NECA is providing the detailed Part 32 data and loop counts submitted by companies pursuant to section 36.611 of the Commission's rules used in the cost per loop and expense adjustment calculations. The RLECs included with their data submission signed certifications attesting to the accuracy of their data.

This USF Data Submission includes estimated high cost loop expense adjustment amounts for average schedule companies. Support amounts for these companies for calendar year 2014 are consistent with the expense adjustment formulas proposed in NECA's 2014 Modification of Average Schedule Universal Service Formulas (filed August 27, 2013).

¹ The Universal Service Administrative Company (USAC) has been designated the administrator of the Federal Universal Service Programs.

² NECA's role, as detailed in Part 36 of the Commission's rules, is to collect the required data and develop an average cost per loop for each RLEC study area based on its historical data. The expense adjustment projections contained herein are based on the results of the annual submission data and are subject to change due to voluntary quarterly updates, reporting of errors and omissions, etc.

³ Data was not submitted by study areas that were price cap or affiliated with price cap carriers as of December 2012. These study areas are no longer required to submit this data under § 36.601 effective January 1, 2013. The following study areas submitted data after the July 31 deadline: Alliance Hills- IA (351405). Alliance Hills – MN (361405), Alliance Hills – SD (391405), Alliance Baltic (391642), Alliance Splitrock (391657). Data and certifications were received for these study areas in early August.

The 2013 USF Data Submission includes the following information:⁴

- Appendix A: Instructions and form used to collect the information for individual study area loop cost calculations
- Appendix B: Formulas and algorithms used to determine the study area and national average loop costs, including the limitations on Corporate Operations expenses
- Appendix C: Comparison of study area types during 2013 and 2014
- Appendix D: Rural ROR study area loops, loop cost and projected 2014 expense adjustments by state
- Appendix E: Rural ROR study area loops, loop cost and projected 2014 expense adjustments by study area code
- Appendix F: Listing of rural ROR incumbent carriers with acquired exchanges recognized during 2014
- Appendix G: Comparison of rural ROR support projections calculated with and without the annual cap
- Appendix H: Five-year trend of study area loops, loop cost and expense adjustment amounts.

II. RESULTS OF 2013 USF SUBMISSION

A. Indexed Cap Calculation

Pursuant to the Commission's rules, an indexed fund cap is calculated for the RLECs. Under the indexed cap mechanism, current year support for the RLECs is based on the prior year's high cost loop support grown by the Rural Growth Factor (RGF).⁵ The RGF is calculated as the sum of the annual change in the total number of RLEC working loops and the percentage change in the Gross Domestic Product-Chained Price Index (GDP-CPI).⁶ For 2014, the RGF is -2.4831%, which represents a decrease in loops of -4.2321% and a percentage change in GDP-CPI of 1.7490%. NECA has calculated the indexed cap for rural RLECs to be \$756.5 million for 2014, which is a

⁴ NECA is required to provide the results for the industry as a whole and a reporting of the current and previous four years' results annually to the Commission and USAC. The information provided herein is included in both paper format and on compact disc. In addition, the disc contains line item detail for each RLEC study area for each of the last five years.

⁵ 47 C.F.R. § 36.604.

⁶ U.S. Department of Commerce, Bureau of Economic Analysis, Gross Domestic Product: Second Quarter 2013 (Preliminary), *News Release*, rel. August 29, 2013, at Table 6.

decrease from the 2013 rural ROR fund cap of \$774.8 million. Attachment 1 displays the details of this calculation.

B. Corporate Operations Expense Limitation

Section 36.621 of the Commission's rules limits the amount of corporate operations expenses assigned to the loop cost calculation. The corporate operations expense limitation is based on a formula in which the dollar values in the formula are indexed by the GDP-CPI.⁷ For calendar year 2014, the applicable GDP-CPI increase is 1.7490%. Corporate operations expense limitations developed in accordance with the prescribed formulas have been increased by this amount over the calendar year 2013 levels to establish the maximum allowable assignment for calendar year 2014.⁸ The algorithm used to implement the corporate operations expense limitation is displayed in Appendix B.

C. National Average Cost Per Loop Calculation

A fixed NACPL of \$240.00 is used to calculate expense adjustment levels for RLECs subject to the availability of funds under the indexed capping mechanism discussed previously. Total RLEC expense adjustment amounts are the lesser of the actual payment calculated at the \$240 frozen NACPL or the capped amount for the applicable period. Based on the \$240 frozen NACPL, RLEC expense adjustment calculations for 2014 would total \$1,803 million, which exceeds the indexed cap of \$756.5 million. As a result, RILEC expense adjustment payments are limited as a result of the indexed cap.⁹

⁷ The Commission's rules limit corporate operations expense assigned to the loop cost calculation to the lesser of the actual corporate operations expense per loop per month or a monthly per-loop amount computed according to Section 36.621(a)(4)(iii).

⁸ The GDP-CPI factor used in the corporate operations expense limitation schedule for calendar year 2014 is 1.039187. This factor captures the composite growth over a two-year time span.

⁹ Actual 2014 expense adjustment amounts paid to individual study areas may change subject to optional quarterly updates permitted by the Commission's rules, to correct errors and omissions in the data should they occur, and due to
(continued ...)

The capped NACPL calculated from calendar year 2012 data reported by the RLECs is \$596.17, which is \$28.54 more than the capped NACPL of \$567.33 calculated from the current view of 2011 data used for 2013 support payments.¹⁰

D. Sale of Exchanges

Section 54.305 of the Commission's rules governs the high cost loop support for situations where an RLEC purchases an exchange from another carrier.¹¹ If an RLEC incorporates acquired exchanges into an existing study area it excludes the costs and loops associated with the acquired exchanges from the costs and loops associated with the pre-acquisition study area. Acquiring RLECs must separately provide the information listed in section 36.611 of the Commission's rules for acquired and existing exchanges as if these two categories of exchanges constitute separate study areas.¹² Appendix F provides information on study areas that have acquired exchanges.

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the impacts of the benchmark limits on combined capital expenses and operating expenses. Actual expense adjustment amounts paid to an individual study area may also be reduced as a result of application of the Commission's \$250 per line per month limitation on high cost support, and/or the adjustment for local rates below the minimum threshold.

¹⁰ If the limitation on Corporate Operations Expense had not been instituted, the NACPL for 2014 for RLECs would have been \$618.78, an increase of \$37.20 over the \$581.58 calculated from the current view of 2011 data used for 2013 support payments.

¹¹ See 47 C.F.R. § 54.305. Specifically, the rules state the acquiring carrier receives support for the acquired exchange at the lessor of the same per-loop support as calculated at the time of the transfer and support as calculated using the actual costs of the acquired exchange.

¹² The information provided for the acquired exchanges will, upon notice to the Administrator, be used as the index year for determination of potential Safety Valve support for those exchanges. See 47 C.F.R. § 54.305.

III. KEY STATISTICS FOR 2013 AND 2014 USF DATA

The following table displays the percentage changes between data underlying the 2013 and 2014 high cost loop expense adjustments. These data include the impact of both the limitation on Corporate Operations Expenses and the indexed cap on Expense Adjustment growth for the Fund and exclude any effects of Capital Expense or Operating Expense limitations.

Rural Rate of Return Carrier Statistics

| Category | Filed For 2013 | Latest View of 2013 | Filed For 2014 | % Change (LV 2013 vs. Filed 2014) |
|---------------------------------|----------------|---------------------|----------------|---|
| Unseparated Revenue Requirement | \$3,650.1 M | \$3,663.1 M | \$3,641.6 M | -0.59% |
| USF Loops | 4.316 M | 4.314 M | 4.089 M | -5.22% ¹³ |
| Cost per Loop ¹⁴ | \$829.49 | \$832.72 | \$872.50 | 4.78% |
| Capped NACPL | \$551.06 | \$567.63 | \$596.17 | 5.03% |

¹³ The percent change in USF loop counts is for a consistent set of study areas for 2013 and 2014. The percent change in loop counts used in the calculation of the rural growth factor includes the removal of Surewest and addition of Fremont study areas resulting in a reduction in loops of -4.2321%

¹⁴ Cost per loop is based on actual unseparated revenue requirement, except where limited by the Corporate Operations Expense limitation, divided by total loops.

**NATIONAL EXCHANGE CARRIER ASSOCIATION, INC.
UNIVERSAL SERVICE FUND
ATTACHMENT 1 - RURAL ROR HIGH COST LOOP FUND
2014 CAP DEVELOPMENT**

| | <u>Source</u> | <u>Data</u> | |
|----|---|----------------------|-------------------|
| 1 | RURAL ROR LOOPS AS OF 12/2011 | 2012 Submission | 4,354,079 ** |
| 2 | RURAL ROR ACQUIRED EXCHANGE LOOPS | 2012 Submission | 84,072 |
| 3 | ADJUSTED RURAL ROR 12/2011 LOOPS | Ln 1 - Ln 2 | 4,270,007 |
| 4 | RURAL ROR LOOPS AS OF 12/2012 | Appendix D | 4,173,719 |
| 5 | RURAL ROR ACQUIRED EXCHANGE LOOPS | Appendix D | 84,423 |
| 6 | RURAL ROR ADJUSTED 12/2012 LOOPS | Ln 4 - Ln 5 | 4,089,296 |
| 7 | CHANGE IN RURAL ROR ILEC LOOPS | (Ln 6 - Ln 3) / Ln 3 | -4.2321% |
| 8 | GDP-CPI 2011 | BEA, Table 6 * | 103.203 |
| 9 | GDP-CPI 2012 | BEA, Table 6 * | 105.008 |
| 10 | CHANGE IN GDP-CPI 2012 | (Ln 9 - Ln 8) / Ln 8 | 1.7490% |
| 11 | RURAL GROWTH FACTOR | Ln 7 + Ln 10 | -2.4831% |
| 12 | MAXIMUM 2013 RURAL ROR FUND SIZE | 2012 Submission | \$775,770,461 *** |
| 13 | MAXIMUM 2014 RURAL ROR FUND SIZE | Ln 12 x (1 + Ln 11) | \$756,507,305 |
| 14 | ROR 2014 ACQUIRED EXCHANGE SUPPORT | from USAC | \$842,919 |
| 15 | MAXIMUM 2014 ROR EXPENSE ADJUSTMENTS (EXCL. ACQUIRED EXCHANGE SUPPORT) | Ln 13 - Ln 14 | \$755,664,386 |

* U.S. Department of Commerce, Bureau of Economic Analysis, Gross Domestic Product: Second Quarter 2012 (Preliminary), *News Release*, rel. August 29, 2013, at Table 6.

** Rural ROR Loops as of 12/2011 exclude loops for Surewest and include loops for Fremont. Surewest became a Price Cap affiliated study area and Fremont became a ROR affiliated study area.

| | |
|----------------------------|-----------|
| ROR Loops | 4,400,348 |
| Surewest (2012 Submission) | (50,050) |
| Fremont (2011 Submission) | 3,781 |
| Net ROR Loops | 4,354,079 |

*** Maximum 2013 Rural ROR Fund Size excludes HCL Support for Surewest and includes HCL Support for Fremont. Surewest became a Price Cap affiliated study area and Fremont became a ROR affiliated study area.

| | |
|----------------------------------|---------------|
| Maximum 2013 Rural Fund Size | \$774,845,716 |
| Surewest (2012 Submission) | \$0 |
| Fremont (2011 Submission) | \$924,745 |
| Net Maximum 2013 Rural Fund Size | \$775,770,461 |