

Agenda Date: June 14, 2006
Item Number: A1

Docket: UT-060760
Company Name: Beaver Creek Telephone Company

Staff: Bob Shirley, Telecommunications Policy Analyst
Tim Zawislak, Telecommunications Regulatory Analyst

Recommendation

Issue an Order in Docket UT-060760 granting Beaver Creek Telephone Company's petition for waiver of notice and filing dates as set forth in paragraph 8 of the Washington Carrier Access Plan as approved in Docket UT-971140, and establish an initial WECA pool revenue objective of \$319,150 with an expiration date of December 31, 2007.

Background

Silverton is a remote community in eastern Snohomish County that does not have telephone service. Beaver Creek Telephone Company (BCTC) is prepared to provide service on June 30 under a tariff filed May 30.

This matter was before the commission on May 17 with a recommendation for a WECA revenue objective of \$571,431. At that time, the commission asked staff to examine the prudence of the actions of the company, examine more closely the investment already made by BCTC, and examine the reasonableness of its anticipated expenses. The commission also requested that staff examine other instances of companies entering the WECA pool and compare those entrances with the request of BCTC.

The commission considered BCTC's request again during an open meeting on June 6, 2006. After that meeting there were still several unresolved issues:

- a) The apparent discrepancy between BCTC's June 2006 rate base of \$2.4 million (\$2.0 million invested and \$0.4 million planned) and its reported total capital of only \$1.36 million at year-end 2005;
- b) The appropriate rate of return for BCTC given its rather low amount of equity compared to debt;
- c) The level of corporate operations expense that should be allowed.

Analysis

Differences Between December 31, 2005 Balance Sheet and June 2006 Rate Base

Beaver Creek provided staff with information suggesting a June 2006 rate base of \$2.4 million (\$2.0 million invested and \$0.4 million planned), but the December 2005 balance sheet indicates its total capital is only \$1.36 million for year-end 2005. The difference is due to two issues:

- 1) The company's correction to the cable and wire facilities account as reflected in the "company correction" column on Attachment 1.
- 2) Additional equipment and plant items ordered and budgeted between December 31 and June 2006.

Staff's review of accounting information subsequent to December 2005 also indicates that the Company has obtained additional capital since December 2005 to finance the additional investment, through both debt and equity financing.

Based on the additional information received, staff believes it is reasonable to use the June 2006 rate base amounts for the revenue objective calculations on Attachments 1, 2, and 3. Total capital as of March 31, 2006, is used to determine the ratio of debt (87.62%) to equity (12.38 %).

Average Rate-of-Return and Return-on-Equity

Staff recommends an overall rate-of-return (ROR) of 5.52%, with a return-on-equity (ROE) of 10%. Attachment 2 reflects the details of this calculation. The company originally proposed an overall ROR of 10.5%, and staff had used this rate in its original recommendation (see Attachment 4 for analysis).

The current staff recommendation reflects the low amount of equity and the fact that most of BCTC's debt is low interest loans from the Rural Utility Service (RUS).

Corporate Operations Expense Adjustment

Staff recommends that the revenue objective include corporate operations expenses of \$59,155 for the intrastate portion, with total corporate operations anticipated to be \$100,000. This is the same amount staff recommended on June 6.

BCTC has contended that this is an unreasonably low level of corporate operations expense, citing conclusions of the Federal Communications Commission and work of the FCC's rural task force. Staff continues to believe that \$100,000 in corporate expenses is appropriate for BCTC, based on its size, nature, and scope of operations. Staff has considered the comments of BCTC regarding the FCC's benchmark minimum for corporate operations expense, which is \$50,000 per month for companies serving less than 6,000 lines. BCTC anticipates serving under 100 lines.

Since June 6, BCTC provided a general breakdown of some of the expenses it included as corporate operations expense. They include substantial amounts for consulting fees, travel and board expenses. Staff believes it likely that BCTC's first-year projected expenses include one-time costs, and costs at levels higher than normal ongoing operating levels. Therefore, staff also examined the 2005 corporate operations expenses of 10 small Washington local exchange telephone companies. The range of corporate operations expenses for the 10 small companies reviewed is from about \$20,000 to \$4.8 million annually, or \$10 to \$65 per line per month. The average expense in that category

is \$30 per line per month. In comparison, Staff's recommendation equals \$83 per line per month assuming 100 lines, an optimistic prediction for total lines. While \$83 per line per month is substantially more than the top of that range, it also reflects staff's understanding that some expenses do not vary with the number of lines served.

Relationship to Expected Federal High-Cost Loop (HCL) Funds

In order to operate over time, BCTC needs \$319,150 in intrastate revenue or an equivalent amount of federal support. HCL support is considered a substitute for intrastate support and intrastate support can be reduced when HCL is available.

For BCTC over the next 18 months, there will be no federal HCL payments to offset intrastate revenue requirement, so the full amount of intrastate support should come from intrastate rates. After BCTC operates for a year and files with the National Exchange Carrier Association for HCL support, it will be clear how much of the WECA revenue objective can be replaced by HCL support. For that reason, staff recommends a WECA revenue objective that expires on December 31, 2007.

Summary

Staff believes that the recommended WECA revenue objective will provide BCTC with a reasonable level of revenues for the period July 1 through December 31, 2007. After a year of operation, the company, staff, and the commission should reevaluate the revenue objective based on experience. At this time, however, under the circumstances as they are, staff recommends an initial WECA revenue objective of \$319,150.

Attachments (4)