

MEMORANDUM

To: Official Case File
Case No. TO-2009 - _____

From: Mike Scheperle

/s/ Mike Scheperle 8/11/2008
Utility Operations Division/Date

/s/ Jennifer Heintz 8/11/2008
General Counsel's Office/Date

Subject: Telecommunications Department review of Relay Missouri fund balance

Date: August 11, 2008

Summary

Pursuant to Section 209.259.1 RSMo, the Missouri Public Service Commission (Commission) is required to conduct a review of the Deaf Relay Service and Equipment Distribution Fund (Fund) Surcharge at least every other year. The last Commission review concluded on June 17, 2007 in Case No. TO-2007-0306 whereby the Commission maintained the current \$.13 Relay Missouri surcharge. Therefore to comply with Section 209.259.1 RSMo the Commission will need to initiate a case to review the Relay Missouri surcharge no later than June 17, 2009. The Fund balance for May 2008 was \$3,179,217 and has steadily been increasing. If the Relay Missouri surcharge is maintained at \$.13 the Fund balance is projected to increase to \$3,927,907 by December 2009.

The Commission Staff (Staff) recommends the Commission reduce the Relay Missouri surcharge from \$.13 to \$.11 effective 90 days from the effective date of a Commission order directing the reduction. Reducing the surcharge will allow the current fund balance to be slowly reduced to slightly below \$3 million by December 2009. In Staff's opinion, a \$3 million balance for Relay Missouri is reasonable based on average monthly expenditures totaling \$347,000. In addition, Staff recommends the Commission maintain the current retention amount. This amount allows a company to retain one percent or \$30, whichever is greater, of the monthly surcharge revenue collected. If the amount collected is less than \$30 then the company simply retains the amount collected.

Background

Section 209.253.1, RSMo requires the Commission to provide a statewide dual-party relay system. In accordance with Section 209.255.1 RSMo, the Commission has established a rate recovery mechanism to recover the costs of implementing and maintaining the Relay Missouri Program (Relay) and Telecommunications Equipment Distribution Program (TEDP). Section 209.259.1 RSMo, requires the Commission to review the deaf relay surcharge no less frequently than every two years, nor more frequently than annually, and to order changes in the amount of the surcharge as is found necessary to ensure funds are available for the provision of the programs established in Section 209.253, RSMo. Section 209.259.3 RSMo, also requires the Commission, concurrent with its review of the surcharge, to review the Retention Amount, and, if necessary, to order adjustments

in the amount to assure a just and reasonable compensation to the local exchange telephone company (LEC). A finding in the last Commission review in Case No. TO-2007-0306 states: “The Commission finds that the possibility of under-funding, which may disrupt use of the Missouri Relay program, is more detrimental to the public interest than an increasingly large fund balance. At the time of the next review, if none of the scenarios that will cause an increase in expenditures has come to pass, the surcharge can be decreased to spend down the balance.”

Since the establishment of Relay in 1990 the Commission has adjusted the Relay surcharge five times. Listed below are the dates the surcharge was changed, the associated case number and the new surcharge:

- October 16, 1990, Case No. TO-90-174, \$0.06;
- November 1, 1992, Case No. TO-90-174, \$0.13;
- January, 22, 2001, Case No. TR-2001-182, \$0.09;
- July 1, 2003, Case No. TO-2003-0171, \$0.10;
- June 28, 2005, Case No. TO-2005-0308, \$0.13.

The Commission issued its order increasing the surcharge to \$0.13 on June 28, 2005. Since the adjustment of the surcharge on June 28, 2005, Staff has continued to analyze the appropriateness of the surcharge and Relay Missouri fund balance. The Commission last reviewed the surcharge in June 2007 in Case No. TO-2007-0306 and retained the Surcharge of \$0.13.

Summarized below in Table 1 are the current Relay Missouri Fund Balance and the Fund balances as of December 31 for the last ten years:

TABLE 1

Relay Missouri Fund Monthly Ending Balances		
December 1998		\$6,396,523
December 1999		\$7,201,971
December 2000		\$7,691,948
December 2001		\$8,118,944
December 2002		\$6,038,010
December 2003		\$4,144,793
December 2004		\$3,026,568
December 2005		\$1,664,041
December 2006		\$2,336,667
December 2007		\$2,862,177
May 2008		\$3,179,217

Cash Flow History Analysis

Summarized below in Table 2 is a cash flow income statement analysis for receipts and expenses for the last four calendar years to date:

TABLE 2

Relay Missouri Fund Summary of Cash Flow					
	Year 2005	Year 2006	Year 2007	Year 2008 thru May	PROJECTED Year 2008
Beginning Cash Balance (first of year)	\$3,026,568	\$1,664,041	\$2,336,667	\$2,862,177	\$2,862,177
Revenue Analysis - Cash Received					
Receipts	\$3,846,849	\$5,006,999	\$4,906,798	\$1,877,879	\$4,623,270
Interest Earned	\$64,652	\$82,577	\$111,472	\$64,952	\$155,446
Total Received	\$3,911,501	\$5,089,576	\$5,018,270	\$1,942,831	\$4,778,716
Expenditures Analysis - Cash Basis					
TRS Invoices	\$3,159,249	\$2,207,198	\$1,968,797	\$647,430	\$1,548,221
CapTel Invoices	\$616,146	\$624,504	\$759,630	\$351,902	\$852,330
Tel. Equipment Distribution Program	\$1,425,871	\$1,516,605	\$1,699,379	\$594,392	\$1,700,000
Central Services Cost Allocation	\$69,068	\$66,929	\$64,395	\$31,432	\$63,432
Relay Missouri Meeting Expenses	\$3,694	\$1,714	\$559	\$635	\$1,635
Total Expenses	\$5,274,028	\$4,416,950	\$4,492,760	\$1,625,791	\$4,165,618
Cash Flow Increase/(Decrease)	(\$1,362,527)	\$672,626	\$525,510	\$317,040	\$613,098
Ending Cash Balance	\$1,664,041	\$2,336,667	\$2,862,177	\$3,179,217	\$3,475,275

Surcharge Rate June 2003 through August 2005 was \$0.10.

Surcharge Rate September 2005 through current is \$0.13.

Known Changes

The Fund balance at the end of May 2008 is \$3,179,217. The Fund balance has steadily increased since the surcharge was increased to \$0.13 in September 2005. With renewal of the Sprint contract extension (Commission decided to exercise the second of three optional two-year contract renewals) effective July 1, 2008, Sprint is increasing the TRS rate (\$0.94 to \$0.9682) and the CapTel rate

(\$1.45 to \$1.4935) by the allowed three (3) percent per contract. The three percent increase will increase projected expenses by \$82,000 per year assuming minutes of use for 2007 for both TRS and CapTel.

Revenue Analysis – Cash Received

Surcharge revenues

The Fund is supported by surcharges applied to basic local telecommunications access lines and interest paid into the fund. To determine the surcharge revenue on a going forward basis, Staff calculated the number of basic local access lines supporting the surcharge on a historical basis. Table 3 depicts the number of lines that have supported the Surcharge for the period 1999 through 2007. Table 3 shows the number of lines supporting the Surcharge is slightly declining. House Bill 1779 will go into effect August 28, 2008. One of the provisions of this bill is the requirement for interconnected voice over the Internet protocol providers to contribute to the Relay Missouri fund. The impact of this provision is unknown.

TABLE 3

Relay Missouri Fund
Calculated Count of Lines Supporting Surcharge

Year	Line Approximation 12 Months Total
1999	38,587,214
2000	38,954,696
2001	40,946,783
2002	41,070,309
2003	38,657,146
2004	38,955,784
2005	35,349,801
2006	38,515,377
2007	37,744,600

From a cash flow analysis on Surcharge receipts, a -\$0.01 surcharge decrease approximates a \$377,000 (37,744,600 annual access lines times \$0.01) annual cash flow decrease excluding interest.

Interest

Staff at the Missouri State Treasurer's office estimates the interest yield earned by the Fund will be 4.75% for fiscal year 2008 through March 2008 (April interest percent dropped below 3%). No

estimate is available for fiscal year 2009. Conservatively, Staff used 4.00% to forecast interest revenue earned by the fund through December 2009.

Expenditure Analysis

Overall, the Fund expenditures have decreased since 2005 from \$5.274 million to \$4.493 million (see Table 2). CapTel and the Telephone Equipment Distribution Program (TEDP) expenditures have increased but traditional relay expenditures (TRS) are declining more rapidly than CapTel and TEDP expenditures are increasing. These and other expenditures are discussed more fully below:

Traditional Relay

Minutes of use (MOU) for traditional relay are declining and are expected to continue to do so. It appears relay users are migrating to alternative relay technologies, video relay, and Internet-protocol relay. The alternative relay technologies are supported by the Federal Relay Fund. Table 4 below indicates that annual TRS usage has decreased significantly for Missouri intrastate activity on a historical basis for the last nine years. The MOU are minutes billed to the Missouri Relay Fund. As can be seen from Table 4, TRS usage has dropped from 4.675 million to 2.003 million over the last eight years. This trend is continuing in 2008.

TABLE 4

Relay Missouri Fund
TRS Usage (Minutes of Use)

Year	TRS Usage Minutes	Expense Accrual
1999	4,675,459	\$3,766,088
2000	4,457,851	\$3,744,595
2001	4,370,615	\$4,097,329
2002	4,370,153	\$4,107,945
2003	3,820,807	\$3,591,560
2004	3,551,852	\$3,338,572
2005	3,005,632	\$2,825,286
2006	2,379,641	\$2,236,861
2007	2,003,110	\$1,882,923

By contract, the current rate of \$0.94 per minute for traditional relay will continue through June 2008. In July 2008 (since the Commission decided to exercise the second of three optional two-year contract renewals), the rate for TRS service will increase by 3% or to \$.9682 per MOU. That rate

will remain in effect until June 2010. The three percent increase will increase TRS projected expenses by \$59,000 per year assuming 2007 MOU.

CapTel

CapTel MOU is increasing and is expected to continue to do so. Table 5 indicates annual usage on an historical basis. The rate of growth for CapTel increased approximately 9% in 2006 and 17% in 2007. Staff projects CapTel usage to increase in 2008 by 12% based on actual usage for 2008 over 2007.

TABLE 5

Relay Missouri Fund
CapTel Usage (Program started in 2003)

Year	CapTel Usage Minutes	Expense Accrual
2003	65,620	\$83,397
2004	151,902	\$215,240
2005	413,520	\$599,604
2006	450,224	\$652,824
2007	527,053	\$764,226

By contract, the current rate of \$1.45 per minute for CapTel will continue through June 2008. In July 2008 (since the Commission decided to exercise the second of three optional two-year contract renewals), the rate for CapTel service will increase by 3% or to \$1.4935 per MOU. That rate would remain in effect until June 2010. The three percent increase will increase CapTel projected expenses by \$23,000 per year assuming 2007 MOU.

Telecommunications Equipment Distribution Program

The TEDP usually expends about two-thirds of its appropriation. For the last three years, TEDP appropriation from the Missouri Legislature has approximated \$2.150 million on a fiscal year basis with approximately \$1.5 to \$1.7 million expended on a calendar year basis (see Table 2). TEDP appropriation for fiscal year 2009 is approximately \$1.864 million which is a \$300,000 decrease from fiscal year 2008. Staff forecasted monthly expenditures based on the \$1.7 million per year for 2008 and 2009 (actual expenditure for 2007).

Central Services Cost Allocation and Relay Missouri Advisory Committee Expenses

The Fund can also be impacted by other factors. The Central Services Cost Allocation Program (CCAP) transferred \$64,395 in 2007 from the Fund to general revenue. Staff used an annual amount of \$64,000 as a proxy for the amount to be transferred for 2008 and 2009 (trend for 2007 and 2008).

Relay Missouri Advisory Committee expenses have been averaging about \$2,000 per year for 2005 through 2007 (see Table 2). Staff used this figure to forecast future expenses for 2008 and 2009.

Retention Amount

The Retention Amount is the amount of the relay surcharge revenue kept by LECs as compensation for billing, collecting, and remitting surcharge. The Commission established the effective retention amount on October 2, 1992. Currently, LECs may keep one percent or \$30, whichever is greater, of the surcharge revenue they collect. If the amount collected is less than \$30 then the company simply retains the amount collected. The Telecommunications Department inquired of ILEC and CLEC representatives whether or not the current Retention Amount is sufficient or if a change of the amount is required. Eight company representatives responded that the current retention amount is sufficient compensation for billing, collecting and remitting the surcharge. No company representatives proposed a change to the current system.

Recommendations

The Telecommunications Department recommends the Commission reduce the Relay Missouri surcharge from \$.13 to \$.11 effective 90 days from the date of a Commission Order. Reducing the surcharge from \$.13 to \$.11 will primarily stabilize the relay fund balance. For example, without calculating the amount to be contributed by VoIP providers, reducing the surcharge to \$.11 is projected to reduce the relay fund balance of \$3.179 million to \$2,992,869 by December 2009. For comparative purposes if the surcharge remains at \$.13 the fund balance will increase to \$3.938 million by December 31, 2009, prior to including any calculations for VoIP contributions.

In the Telecommunications Department Staff's opinion, maintaining a fund reserve of approximately nine months is reasonable based on monthly expenditures totaling \$347,135. This type of comparison is similar to the Missouri Universal Service Fund Board's desired targeted balance for the Missouri Universal Service Fund of at least six months worth of projected expenditures. However, a slightly more conservative approach is desired for the Relay Missouri Fund given the restrictions of reviewing the surcharge contained in Section 209.259.1 RSMo. Different target fund balances for the Relay Missouri Fund can be found in Table 6, which outlines a cash flow analysis, absent calculations for VoIP contributions, based on Surcharge assumptions of \$0.09 to \$0.13 effective October 1, 2008.

Staff recommends an effective date that is ninety days from the effective date of a Commission order. This time frame should allow companies to make the necessary modifications within their billing systems to reduce the surcharge. Companies should not be required to provide customer notice of the rate reduction.

Staff also recommends the Commission maintain the current retention amount. As previously discussed the current retention amount provides a limited form of reimbursement to a company for its billing and collection service. The current retention amount allows a company to keep one percent or \$30, whichever is greater, of the surcharge revenue it collects. If the amount collected is less than \$30 then the company simply retains the amount collected. This retention amount should simply be maintained because no compelling reason has been presented by the telecommunications industry to change this amount.

In summary, the Staff recommends the Commission issue an order with the following provisions:

1. The Relay Missouri surcharge is decreased from \$.13 to \$.11.
2. Ninety days from the effective date of this order companies responsible for billing and collecting the Relay Missouri surcharge should begin charging the new rate of \$.11.
3. The amount retained by companies shall be one percent or \$30, whichever is greater. If the amount collected is less than \$30 then the company simply retains the amount collected.

TABLE 6

Missouri Public Service Commission
Projection of Relay Missouri Balances

Month	Surcharge \$0.13	Surcharge \$0.12	Surcharge \$0.11	Surcharge \$0.10	Surcharge \$0.09
November 2007	\$2,835,209	\$2,835,209	\$2,835,209	\$2,835,209	\$2,835,209
December	\$2,862,177	\$2,862,177	\$2,862,177	\$2,862,177	\$2,862,177
January, 2008	\$2,969,624	\$2,969,624	\$2,969,624	\$2,969,624	\$2,969,624
February	\$3,025,433	\$3,025,433	\$3,025,433	\$3,025,433	\$3,025,433
March	\$3,083,061	\$3,083,061	\$3,083,061	\$3,083,061	\$3,083,061
April	\$3,142,206	\$3,142,206	\$3,142,206	\$3,142,206	\$3,142,206
May	\$3,179,217	\$3,179,217	\$3,179,217	\$3,179,217	\$3,179,217
June	\$3,235,086	\$3,235,086	\$3,235,086	\$3,235,086	\$3,235,086
July	\$3,262,690	\$3,262,690	\$3,262,690	\$3,262,690	\$3,262,690
August	\$3,303,111	\$3,303,111	\$3,303,111	\$3,303,111	\$3,303,111
September	\$3,354,511	\$3,354,511	\$3,354,511	\$3,354,511	\$3,354,511
October	\$3,386,812	\$3,354,783	\$3,324,648	\$3,294,513	\$3,264,377
November	\$3,433,815	\$3,369,589	\$3,309,252	\$3,248,914	\$3,188,577
December	\$3,475,275	\$3,378,807	\$3,288,201	\$3,197,594	\$3,106,988
January, 2009	\$3,496,354	\$3,367,271	\$3,246,076	\$3,124,882	\$3,003,688
February	\$3,523,632	\$3,363,390	\$3,213,164	\$3,062,939	\$2,912,713
March	\$3,537,793	\$3,347,233	\$3,168,817	\$2,990,401	\$2,811,985
April	\$3,564,329	\$3,340,895	\$3,131,801	\$2,922,707	\$2,713,613
May	\$3,582,282	\$3,328,214	\$3,090,657	\$2,853,100	\$2,615,543
June	\$3,641,839	\$3,354,487	\$3,085,868	\$2,817,249	\$2,548,630
July	\$3,679,051	\$3,358,464	\$3,058,712	\$2,758,961	\$2,459,210
August	\$3,728,466	\$3,374,455	\$3,043,502	\$2,712,549	\$2,381,596
September	\$3,789,982	\$3,402,487	\$3,040,262	\$2,678,037	\$2,315,812
October	\$3,831,824	\$3,410,777	\$3,017,210	\$2,623,642	\$2,230,074
November	\$3,888,128	\$3,433,347	\$3,008,366	\$2,583,385	\$2,158,404
December	\$3,937,907	\$3,449,335	\$2,992,869	\$2,536,404	\$2,079,938

Assumptions:

1. Surcharge change effective October 1, 2008
2. Sprint TRS Rate and CapTel Rate change July 1, 2008 per Renewal of Contract with 3% Increase.

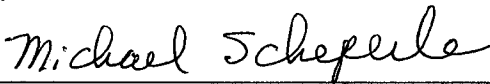
**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of a Recommendation)
Concerning the Surcharge for Deaf Relay)
Service and Equipment Distribution)
Program Fund.)

AFFIDAVIT OF Michael S. Scheperle

STATE OF MISSOURI)
) ss:
COUNTY OF COLE)

Michael S. Scheperle, employee of the Staff of the Missouri Public Service Commission, being of lawful age and after being duly sworn, states that he has participated in the preparation of the accompanying memorandum and that the facts therein are true and correct to the best of his knowledge and belief.



Michael S. Scheperle

Subscribed and affirmed before me this 11th day of August 2008

I am commissioned as a notary public within the County of Callaway, State of Missouri

and my commission expires on 9-21-10



SUSAN L. SUNDERMEYER
My Commission Expires
September 21, 2010
Callaway County
Commission #06942086



NOTARY PUBLIC