

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY

Federal Universal Service Support Mechanisms Fund Size
Projections for the Second Quarter 2005

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**BEFORE THE FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, DC 20554**

**FEDERAL UNIVERSAL SERVICE SUPPORT MECHANISMS
FUND SIZE PROJECTIONS FOR THE SECOND QUARTER 2005**

INTRODUCTION

The Universal Service Administrative Company (USAC) submits the Federal Universal Service Support Mechanisms fund size and administrative cost projections for the second quarter of calendar year 2005 (2Q2005), in accordance with Section 54.709 of the Federal Communications Commission's (FCC or Commission) rules.¹

USAC is the not-for-profit corporation responsible for administering the federal universal service support mechanisms: High Cost, Interstate Access, Low Income, Rural Health Care, and Schools and Libraries.² USAC also performs the billing, collection, and disbursement functions for all of these universal service support mechanisms.

Upon approval of the quarterly funding requirements for the universal service support mechanisms and the projected administrative expenses, and the submission of the contribution base amount, the Commission will establish a quarterly contribution factor. USAC will bill contributors on a monthly basis for their individual obligations based on the approved contribution factor, collect the funds, and distribute funds to eligible recipients based on the schedules filed herein.³

¹ 47 C.F.R. § 54.709(a)(3).

² 47 C.F.R. § 54.701.

³ See 47 C.F.R. §§ 54.709(a)(4), 54.201, 54.203, 54.515, 54.517, 54.301-54.307, 54.407, 54.413, 54.515, and 54.611.

ADMINISTRATIVE EXPENSES AND INTEREST PROJECTION

ADMINISTRATIVE EXPENSES

Section 54.709(a) (3) of the Commission's rules requires USAC to submit its projected quarterly budget at least 60 days prior to the start of the quarter.⁴ USAC includes any costs that can be directly attributed to the High Cost, Interstate Access, Low Income, Rural Health Care, and Schools and Libraries Support Mechanisms in the projected administrative expenses of each mechanism. USAC's remaining joint and common costs including costs associated with the billing, collection, and disbursement of funds are included in the projected administrative expenses of the respective support mechanisms based on the methodology for allocating costs.⁵ The allocation of billing, collection, and common costs also reflects the fact that the Commission directed that the costs associated with the Interstate Access Support Mechanism be allocated to the High Cost and Low Income Support Mechanisms.⁶

USAC projects a 2Q2005 consolidated budget of \$32.581 million. Direct costs for all support mechanisms total \$25.259 million.⁷ The detail for each mechanism is provided below. Joint and common costs (including billing, collection, and disbursement activities that are now performed in-house) are allocated to each support mechanism as detailed below based on the current allocation

⁴ 47 C.F.R. § 54.709(a)(3).

⁵ See Letter from Robert Haga to Magalie Salas regarding Revisions to the Method for Allocating Costs Among the Four Universal Service Support Mechanisms, CC Docket Nos. 96-45 and 97-21 (Jan. 28, 2000); Letter from Robert Haga to Magalie Salas regarding Revisions to the Method for Allocating Costs Among the Four Universal Service Support Mechanisms, CC Docket Nos. 96-45 and 97-21 (Apr. 1, 1999).

⁶ See Letter from Robert Haga to Magalie Salas regarding Revisions to the Method for Allocating Costs Among the Four Universal Service Support Mechanisms, CC Docket Nos. 96-45 and 97-21 (Jan. 28, 2000); Letter from Robert Haga to Magalie Salas regarding Revisions to the Method for Allocating Costs Among the Four Universal Service Support Mechanisms, CC Docket Nos. 96-45 and 97-21 (Apr. 1, 1999).

⁷ This includes \$0.0810 million for High Cost Support Mechanism data collection performed by the National Exchange Carrier Association, Inc. (NECA) pursuant to 47 C.F.R. Part 36. Although USAC is required to pay for the data collection, USAC does not have the ability to directly oversee the data collection and cannot independently verify, monitor, or otherwise evaluate the cost of performing the data collection function. Consistent with the fiduciary obligations of its members to safeguard USAC assets and the Universal Service Fund, USAC's Board of Directors has requested clarification from the Commission concerning this matter. See Letter from D. Scott Barash, USAC, to Irene Flannery, FCC (Dec. 10, 1999), Comments of the Universal Service Administrative Company to the *Further Notice of Proposed Rulemaking* in CC Docket No. 96-45, FCC 01-8 (Feb. 26, 2001).

methodology on file with the Commission. The 2Q2005 budget includes \$7.500 million to fund the Universal Service Fund Oversight Program initiated by the FCC Office of Inspector General.

2nd Quarter 2005 Administrative Expenses (millions)

USF MECHANISM	DIRECT COSTS	USAC COMMON	TOTAL
High Cost	6.787	4.144	10.931
Low Income	1.452	0.754	2.206
Rural Health Care	0.975	0.037	1.012
Schools & Libraries	16.045	2.387	18.432
Total	25.259	7.322	32.581

Note: Columns on table may not add perfectly due to rounding.

Commission rules currently direct the National Exchange Carrier Association, Inc. (NECA) to continue performing certain universal service administrative functions for the High Cost Loop (HCL) support mechanism, specifically, the collection and processing of annual HCL data as well as the optional quarterly updates to that data.⁸ Recovery of HCL data collection expenses is attributable to the High Cost Support Mechanism because these functions are associated with the administration of the universal service support mechanisms. NECA bills these costs to USAC.⁹ NECA’s projected 2Q2005 expenses to perform these universal service-related functions are \$0.085 million.

USAC budgets for all of the costs associated with the High Cost Support Mechanism, including the HCL data collection performed by NECA. As discussed above, consistent with the fiduciary obligations of its members to safeguard USAC assets and the Universal Service Fund Support Mechanisms, USAC’s Board of Directors has requested clarification from the Commission concerning this matter.¹⁰

⁸ 47 C.F.R. §§ 36.611-36.613.

⁹ 47 C.F.R. § 69.603.

¹⁰ See Letter from D. Scott Barash, USAC, to Irene Flannery, FCC (Dec. 10, 1999).

Appendix M01 details USAC's estimated administrative expense budget for 2Q2005.

Appendix M02 details the fund size projections for 2Q2005.

INTEREST INCOME PROJECTION

For 2Q2005, USAC projects interest income of approximately \$0.822 million for the High Cost Support Mechanism, \$0.290 million for the Low Income Support Mechanism, \$0.084 million for the Rural Health Care Support Mechanism and \$11.609 million for the Schools and Libraries Support Mechanism. In sum, USAC projects total interest of \$12.805 million. As in previous quarters, the projected interest income is being included as an offset to administrative expenses for each of the support mechanisms not projected to reach its funding cap, and reduces the amount that USAC will be required to collect from carriers for those support mechanisms that are funded at caps established by the Commission.

FINANCIAL STATEMENTS

As of December 31, 2004, on a cash basis, USAC had disbursed \$5,638 million in universal service support to service providers in 2004: \$3,469 million in High Cost support, \$761 million in Low Income support, \$21 million in Rural Health Care support, and \$1,387 million in Schools and Libraries support. On a cash basis, the total cash balance available to the universal service support mechanisms was \$3,342 million.

For the period ending December 31, 2004, on an accrual basis, USAC had a fund balance of \$3,416 million.

Appendices M03 and M04 provide the 2004 statement of fund activity on a cash and accrual basis.

FUNDING REQUIREMENTS

HIGH COST SUPPORT MECHANISM

ELIGIBLE TELECOMMUNICATIONS CARRIER (ETC) DESIGNATION

A requirement for eligibility for receipt of High Cost support is that a common carrier must be designated as an eligible telecommunications carrier (ETC) by a state commission or the FCC in accordance with Subpart F of the FCC’s Part 36 rules and Subpart D of its Part 54 rules.¹¹ Qualified ETCs are eligible to receive funds from the High Cost Support Mechanism,¹² which includes High Cost Loop (HCL) support, Interstate Access Support (IAS), Local Switching Support (LSS), Long Term Support (LTS), Interstate Common Line Support (ICLS), and non-rural forward-looking High Cost Model (HCM) support. Together, the projected requirements for these six components of the High Cost Support Mechanism and the USAC administrative expenses constitute the overall funding requirement for the High Cost Support Mechanism.

The High Cost Support Mechanism provides support to more than 1,500 study areas, including those served by both incumbent and competitive ETCs. The table below contains the number of study areas served by rural versus non-rural carriers and rate-of-return versus price cap carriers.

Count of Study Areas by Category							
	Incumbent Study Areas				Total Incumbent	Competitive Study Areas	Total Study Areas
	Rate-of-Return			Price Cap			
	Cost Companies	Average Schedule	Total				
Rural	761	481	1242	105	1347	169	1516
Non-Rural	5	1	6	80	86	139	225
Total	766	482	1248	185	1433	308	1741

¹¹ See 47 U.S.C. § 214(e), 47 C.F.R. § 54.201.

¹² 47 C.F.R. § 36.631 and 47 C.F.R. §§ 54.301-54.303, 54.309, 54.311, 54.807, and 54.901.

Appendix HC01 displays the projected minimum amount of individual company support segregated by rural and non-rural status. Appendix HC01 also contains the projected minimum amount of per-month high cost support for each support mechanism that each ETC¹³ will be eligible to receive (i.e., HCL, HCM, IAS, LSS, and ICLS). Appendix HC02 displays the total projected amount of High Cost support for 2Q2005 for each state or territory. HC03 displays rural study areas with competition. HC04 displays disaggregated per-line High Cost support by zone, consistent with the disaggregation plans filed with USAC.

HIGH COST RURAL SUPPORT MECHANISM

High Cost Loop (HCL) Support

High Cost Loop (HCL) support is calculated based on the results of the annual collection of 2002 incumbent local exchange carrier (ILEC) loop cost and expense adjustment data that was submitted to the FCC and to USAC on October 1, 2003.¹⁴ Growth in total HCL support for rural carriers is limited under Section 36.603(a) of the FCC's rules to the current level of funding increased yearly by the annual growth in supported rural loops. Effective July 1, 2001, HCL support increased for rural companies due to the *RTF Order*.¹⁵

Rural HCL support for calendar year 2005 will be less than the level of payments for 2004 because of a negative rural growth factor of -0.04 percent. Rural HCL support for calendar year 2005, therefore, is capped at \$1,056.300 million.

Pursuant to the *RTF Order*, Safety Net Additive support is support above the HCL cap for carriers that make significant investment in rural infrastructure in years in which HCL is capped.¹⁶ To receive support, a rural carrier must show that growth in telecommunications plant in service

¹³ 47 C.F.R. § 36.631 and 47 C.F.R. §§ 54.301-54.303.

¹⁴ Universal Service Fund (USF) 2003 Submission of 2002 Study Results (filed October 1, 2003) (*USF Data Submission*).

¹⁵ See *Federal-State Joint Board on Universal Service, Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket Nos. 96-45, 00-256, Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256, FCC 01-157 (rel. May 23, 2001) (*RTF Order*).

¹⁶ See *RTF Order* at paras. 77 to 90.

(TPIS) per line is at least 14% greater than the study area's TPIS in the prior year. Carriers seeking to qualify for Safety Net Additive support must provide written notice to USAC that a study area meets the 14% TPIS trigger.¹⁷ For 2Q2005, projected Safety Net Additive support is \$4.222 million.

Also pursuant to the *RTF Order*, Safety Valve support is support above the HCL cap for rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.¹⁸ Safety Valve support is 50 percent of the difference between the index year HCL support amount and the HCL support amount in subsequent years.¹⁹ Safety Valve support is subject to an overall cap of no more than five percent of the HCL fund in any given year.²⁰ For 2Q2005, projected Safety Valve support is \$4.623 million.²¹

For 2Q2005, projected HCL support is \$323.938 million. Of this amount, \$264.075 million is associated with rural carriers and \$51.018 million is associated with competitive ETCs. Furthermore, 2Q2005 Safety Net Additive support is projected to be \$4.222 million and Safety Valve support is projected to be \$4.623 million. USAC projects that \$323.938 million will be required for 2Q2005. Based on these projections, total 2005 HCL support is estimated to be \$1,283.347 million.

Appendix HC05 displays projected monthly HCL support payments by study area for 2Q2005 in accordance with the hold-harmless provisions of the FCC's *Methodology Order*. Appendix HC06 displays projected monthly Safety Net Additive support payments by study area for 2Q2005. HC07 displays projected monthly Safety Valve support payments by study area for

¹⁷ See 47 C.F.R. § 36.605(c).

¹⁸ See *RTF Order* at paras. 91 to 119.

¹⁹ See 47 C.F.R. §54.305(c). In an order released on January 10, 2005, the FCC amended Section 54.305 so that it does not apply to transfers of exchanges between non-rural carriers after the phase-down of interim hold harmless support. See *Federal-State Joint Board on Universal Service, National Telephone Cooperative Association Petition for Reconsideration*, CC Docket No. 96-45, Order and Order on Reconsideration, FCC 05-1 (rel. Jan. 10, 2005), at para. 9. In addition, the FCC amended Section 54.305 to provide that rural carriers that acquire high cost exchanges may receive safety valve support for the investment made in the first year of operating the acquired exchanges. *Id.* at para. 10.

²⁰ See 47 C.F.R. § 54.305(c).

²¹ This number includes retroactive support for 2003 and 2004, as well as projected support for 2Q2005.

2Q2005. HCL projected support for non-rural carriers receiving high cost support is superseded by the projections listed in HC15, HC16, and HC17. Appendix HC18 displays competitive ETC lines reported for HCL support by incumbent study area.

LOCAL SWITCHING SUPPORT (LSS)

ETC study areas having 50,000 or fewer access lines are eligible to receive support for local switching costs.²² Local Switching Support (LSS) is the product of a carrier's annual unseparated local switching revenue requirement multiplied by its local switching support factor.²³

For 2Q2005, LSS for companies participating in the Traffic Sensitive Pool is projected to be \$56.699 million for cost study areas and \$17.196 million for average schedule study areas. LSS for the non-pool study areas is projected to be \$19.915 million for cost study areas and \$3.718 million for average schedule study areas for 2Q2005. In addition, 2Q2005 LSS for competitive ETCs is projected to be \$20.089 million. USAC projects, therefore, that \$117.617 million will be required for 2Q2005. Based on these projections, total 2005 LSS is estimated to be \$468.907 million.

Individual study area LSS projections per month are displayed in Appendix HC08.

INTERSTATE COMMON LINE SUPPORT MECHANISM (ICLS)

In the *MAG Order* released on November 8, 2001, the FCC reformed the interstate access charge and universal service support systems for rate-of-return carriers.²⁴ Interstate Common Line Support (ICLS) is designed to permit each rate-of-return carrier to recover its common line

²² See 47 C.F.R. § 54.301.

²³ The LSS factor is defined as the difference between the 1996 weighted interstate Dial Equipment Minute (DEM) factor and the 1996 unweighted DEM factor.

²⁴ See *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, Federal-State Joint Board on Universal Service, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket Nos. 00-256, 96-45, 98-77, 98-166, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, FCC 01-304 (rel. Nov. 8, 2001) (*MAG Order*).

revenue requirement, while ensuring that its subscriber line charges (SLCs) remain affordable to its customers.

For 2Q2005, ICLS for incumbent rate-of-return carriers is projected to be \$232.563 million. In addition, 2Q2005 ICLS for competitive ETCs is projected to be \$54.840 million. USAC projects, therefore, that \$287.403 million will be required for 2Q2005. Based on these projections, total 2005 ICLS is estimated to be \$1,142.283 million.

Appendices HC09, HC10, and HC11 detail USAC's 2Q2005 projection of ICLS by state by study area, per line, and by state, respectively. Appendix HC19 displays competitive ETC lines reported for ICLS by incumbent study area.

INTERSTATE ACCESS SUPPORT MECHANISM (IAS)

Interstate Access Support (IAS) helps offset interstate access charges for price cap companies.²⁵ The *Interstate Access Order* targeted the support mechanism at \$650 million annually for five years.²⁶

The IAS projected industry-wide totals for 2Q2005 are \$44.876 million for rural carriers, \$107.142 million for non-rural carriers, and \$38.730 million for competitive ETCs. USAC projects that \$190.748 million will be required for 2Q2005. Based on these calculations, total annual IAS is estimated to be \$707.690 million.²⁷

Appendices HC12, HC13, and HC14 detail USAC's 2Q2005 projection of interstate access support by state by study area, per line, and by state, respectively. Appendix HC20 displays competitive ETC lines reported for IAS by incumbent study area.

²⁵ See *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262, 94-1, Sixth Report and Order, *Low-Volume Long Distance Users*, CC Docket No. 99-249, Report and Order, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Eleventh Report and Order, FCC 00-193 (rel. May 31, 2000) (*Interstate Access Order*).

²⁶ See *Interstate Access Order* at para. 201.

²⁷ The total annual IAS is likely to exceed the \$650 million target as permitted under 47 C.F.R. § 54.807. See also, Letter from Jeffrey Carlisle, FCC, to Irene Flannery, USAC (Jan. 27, 2005).

NON-RURAL FORWARD-LOOKING MECHANISM

Under the most recent running of the model used to calculate forward-looking High Cost Model (HCM) support for non-rural carriers, non-rural carriers in 10 states (Alabama, Kentucky, Maine, Mississippi, Montana, Nebraska, South Dakota, Vermont, West Virginia, and Wyoming) are eligible to receive forward-looking support in 2005.²⁸

For 2Q2005, USAC projects that \$72.827 million will be required for HCM support (\$55.367 million for incumbent non-rural carriers and \$17.460 million for competitive ETCs). USAC projects, therefore, that \$72.827 million of HCM support will be required for 2Q2005. Based on these projections, total 2005 forward-looking support is estimated to be \$291.307 million.

Appendices HC15, HC16, and HC17 detail USAC's 2Q2005 projection of non-rural forward-looking support by wire center, by state, and by study area, respectively. Appendix HC21 displays competitive ETC lines reported for HCM support by incumbent study area.

HIGH COST SUPPORT MECHANISM SUMMARY

As discussed above, USAC estimates 2Q2005 funding requirement as follows: \$323.938 million for HCL support; \$117.617 million for LSS; \$287.403 million for ICLS; \$190.748 million for IAS; and \$72.827 million for HCM for a total of \$992.533 million. Sections 54.709(b) and 54.709(c) of the Commission's rules require USAC to adjust the size of the projected support requirements to reflect adjustments based on actual dollar amounts compared to the projection included in the prior period.²⁹ Increases in the size of the funding requirement for the previous period are added to the projected requirements; decreases from the prior period are subtracted from the projected revenue requirements.

²⁸ See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order and Order on Reconsideration, DA 03-4070 (rel. Dec. 24, 2003); see also *Wireline Competition Bureau Releases Estimated State-By-State High-Cost Universal Service Support Amounts for Non-Rural Carriers for 2004*, CC Docket No. 96-45, Public Notice, DA 03-4071 (rel. Dec. 24, 2003).

²⁹ 47 C.F.R. §§ 54.709(b) and 54.709(c).

Results for 4Q2004 contribute to an under-funded condition, for which the instant filing proposes to adjust the 2Q2005 requirements. The total adjustment to the 2Q2005 fund requirement based on actual results will increase the funding needed by \$12.496 million. The detailed explanations for the adjustment are described below.

Reason for the Prior Period Adjustment	Adjustment in Millions
The 4Q2004 billings were lower than expected due to lower revenues reported by contributors in their quarterly revenue projections	\$74.263 M
Distributions were lower than expected in 4Q2004.	(46.541) M
Interest earned was lower than estimated for the 4Q2004.	0.345 M
Bad debt expense was lower than anticipated	(15.570) M
Total Prior Period Adjustment	\$12.496 M

Note: Column on table may not add perfectly due to rounding.

The total fund requirement of \$992.533 million, increased by the prior-period adjustment of \$12.496 million, increased by administrative costs of \$10.931 million, and reduced by the projected interest of \$0.822 million, results in a total projected funding requirement for the High Cost Support Mechanism for 2Q2005 of \$1,015.138 million.

Appendix M02 details the individual components of the funding requirement for the quarter.

LOW INCOME SUPPORT MECHANISM

LIFELINE SUPPORT

All ETCs must offer Lifeline support to qualified low-income consumers.³⁰ ETCs providing Lifeline support in accordance with Subpart E of Section 54 of the Commission’s rules are entitled to receive funding from the federal Low Income Support Mechanism for the waiver of charges and reduced rates provided to qualified low-income subscribers.³¹ Lifeline support

³⁰ See 47 C.F.R. § 54.201.

³¹ 47 C.F.R. §§ 54.401 - 54.417.

provides funding from the interstate jurisdiction of up to \$10.00 per low-income subscriber per month. This can consist of a baseline amount of between \$3.50 and \$6.50 (Tier One),³² an additional \$1.75 per subscriber if the state commission authorizes a reduction in local rates equal to that amount (Tier Two), and up to an additional \$1.75 from the federal mechanism available if the state provides support for the low-income subscriber as well (Tier Three).³³ Further, the *Tribal Order* makes available up to an additional \$25 per low-income subscriber per month to eligible residents of tribal lands (Tier Four).³⁴

For 2Q2005, USAC projects that \$183.162 million will be required for Lifeline support. Based on this projection, total 2005 Lifeline support is estimated to be \$734.487 million.

LINK UP AMERICA

Link Up support compensates ETCs up to \$30 for revenue foregone in offering discounted service initiation fees to qualified low-income individuals. The *Tribal Order* authorized additional Link Up support of up to \$70 per qualified low-income subscriber residing on eligible tribal lands.³⁵ For 2Q2005, USAC projects that \$9.064 million will be required for Link Up support. Based on this projection, total 2005 Link Up support is estimated to be \$36.209 million.

³² Tier One support, which compensates the carrier for not charging the subscriber line charge (SLC) to eligible low-income customers, ranges from \$3.50 to \$6.50. See *Interstate Access Order* at para. 70 (permitting the baseline subscriber line charge to increase for price cap carriers from \$3.50 to \$4.35 effective July 1, 2000, and to increase again from \$4.35 to \$5.00 effective July 1, 2001); *MAG Order* at para. 42 (permitting rate-of-return carriers to increase their baseline subscriber line charge to \$5.00 effective January 1, 2002); *Cost Review Proceeding for Residential and Single-Line Business Subscriber Line Charge (SLC) Caps, Access Charge Reform, and Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262, 94-1, Order, FCC 02-161 (rel. June 5, 2002) (*2002 SLC Order*) (authorizing an increase in the baseline subscriber line charge for price cap and rate-of-return carriers to \$6.00, effective July 1, 2002, and to \$6.50, effective July 1, 2003).

³³ Tier Three support is equal to one-half of a state-funded amount up to \$3.50. For example, if a carrier operating in a state that has a matching program that provides \$3.50 in support through the matching program reduces its intrastate rates by \$10.00 for low-income customers, the customer would experience a total monthly rate reduction of \$13.50 (\$3.50 in interstate charges and \$10.00 in intrastate charges) of which \$10.00 would be funded from the federal jurisdiction and \$3.50 from the state matching program.

³⁴ 47 C.F.R. § 54.400(e); see also *Tribal Order*. On August 31, 2000, the FCC stayed the implementation of the federal Lifeline and Link Up rule amendments only to the extent that they apply to qualifying low-income consumers living near reservations.

³⁵ *Tribal Order* at para. 59.

TOLL-LIMITATION SUPPORT

Toll Limitation Support (TLS) compensates ETCs for providing voluntary toll-limitation based on the carrier's incremental cost of providing toll-limitation services. The FCC has defined these costs as the costs that carriers otherwise would not incur if they did not provide toll-limitation service to a given customer.³⁶ Toll limitation consists of toll blocking, which permits consumers to elect not to allow the completion of outgoing toll calls, and toll limitation, which allows consumers to specify a certain amount of toll usage that may be incurred per month or per billing cycle.³⁷ For 2Q2005, USAC projects that \$1.386 million will be required for TLS. Based on this projection, total 2005 TLS is estimated to be \$5.533 million.

LOW INCOME SUPPORT MECHANISM SUMMARY

As discussed above, the estimated 2Q2005 funding requirement for the Low Income Support Mechanism is as follows: \$183.162 million for Lifeline, \$9.064 million for Link Up, and \$1.386 million for Toll Limitation Service, for a total of \$193.612 million. Results of 4Q2004 contribute to an under-funded condition, for which the instant filing proposes to adjust the 2Q2005 requirements. The total adjustment to the 2Q2005 funding requirement based on actual results will increase the funding needed by \$12.288 million. The detailed explanations for the adjustment are described below.

³⁶ See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) at para. 386 (*First Report and Order*) (subsequent history omitted).

³⁷ 47 C.F.R. § 54.400(b), (c).

Reason for the Prior Period Adjustment	Adjustment in Millions
The 4Q2004 billings were lower than expected due to lower revenues reported by contributors in their quarterly revenue projections	\$17.729 M
Distributions were lower than expected in 4Q2004	(1.173) M
Interest earned was less than estimated for 4Q2004	0.054 M
Bad debt expense was lower than anticipated	(4.322) M
Total Prior Period Adjustment	\$12.288 M

Note: Column on table may not add perfectly due to rounding.

The total fund requirement of \$193.612 million, increased by the prior-period adjustment of \$12.288 million, increased for administrative expenses of \$2.206 million, and the deduction of the projected interest income of \$0.290 million results in a total projected funding requirement for the Low Income Support Mechanism for 2Q2005 of \$207.816 million.

Appendix LI01 provides projected Low Income support amounts by state by study area for 2Q2005. Appendix LI02 provides detail on Low Income funding amounts available in each of the states and territories for 2Q2005. Appendix LI03 provides a list of eligible telecommunications carriers (ETCs) for 4Q2004. Appendix LI04 provides detail on quarterly company-specific Low Income support disbursement amounts for 4Q2004. Appendix LI05 provides detail on annual company-specific Low Income support amounts through 3Q2004. Appendix LI06 provides historical data of monthly support amounts claimed by ETCs from January 1998 through December 2004. Appendix LI07 provides detail on Low Income support distributed by state for 2001 through 3Q2004. Appendices LI08 and LI09 provide subscriber information by state or jurisdiction for Lifeline and Link Up support, respectively. Appendix LI10 shows the Tier 1 amounts reported by all companies during 3Q2004.

RURAL HEALTH CARE SUPPORT MECHANISM**FUNDING YEAR 2000**

Funding Year 2000 began on July 1, 2000 and ended on June 30, 2001. All Funding Year 2000 applications have been reviewed and processed. USAC issued funding commitments to rural health care providers for Funding Year 2000 totaling \$10.756 million. Based on information provided by the applicants as of December 31, 2004, USAC projects that Funding Year 2000 demand for support will total approximately \$10.314 million. The FCC previously authorized the collection of \$10.316 million for the Funding Year 2000. Of the \$10.316 million collected, \$10.314 million has been disbursed. An adjustment will be made to increase collections or to decrease collections by the \$0.002 million that has not been disbursed when we have completed processing appeals.

FUNDING YEAR 2001

Funding Year 2001 began on July 1, 2001 and ended on June 30, 2002. All Funding Year 2001 applications have been reviewed and processed. USAC issued funding commitments to rural health care providers for Funding Year 2001 totaling \$19.689 million. The FCC previously authorized the collection of \$18.575 million for Funding Year 2001. Of the \$18.575 million collected, \$18.553 million has been disbursed. An adjustment will be made to increase collections or to decrease collections by the \$0.022 million that has not been disbursed when we have completed processing any applications that are submitted based on appeals that have been approved.

Authorized funding by applicants during 4Q2004 and cumulative disbursements made to service providers through 4Q2004 are listed in Appendices RH01 and RH02, respectively.

FUNDING YEAR 2002

The Funding Year 2002 application filing window opened on January 28, 2002. Funding Year 2002 began on July 1, 2002, and ended on June 30, 2003. As of December 31, 2004, 2,785 Form 466/468 packets had been received. The status of those packets is provided below.

FUNDING YEAR 2002	
Packets Completely Processed	2,589
Denied	93
Withdrawn by Applicant	103
Total Packets Received for Funding Year 2002	2,785

As of December 31, 2004, funding commitments have been issued totaling \$23.369 million. Based on information provided by the applicants, USAC now estimates Funding Year 2002 demand will be \$22.293 million. The FCC previously authorized the collection of \$22.403 million for Funding Year 2002. Based on the revised estimate of demand, USAC recommends the FCC decrease collections for Funding Year 2002 by \$0.110 million in 2Q2005.

Funding commitments made during 4Q2004 are included in Appendix RH03. Authorized funding by applicant during 4Q2004 and disbursements made to service providers through 4Q2004 are listed in Appendices RH04 and RH05, respectively.

FUNDING YEAR 2003

The Funding Year 2003 application filing window opened on March 26, 2003. Funding Year 2003 began on July 1, 2003, and ended on June 30, 2004. As of December 31, 2004, 3,165 Form 466 packets had been received. The status of those packets is provided below.

FUNDING YEAR 2003	
Packets Completely Processed	2,820
Packets Awaiting Supervisory Approval Only	22
Withdrawn by Applicant	217
Denied	46
Incomplete – Require Forms and/or Clarification	60
Total Packets Received for Funding Year 2003	3,165

As of December 31, 2004, funding commitments have been issued totaling \$24.675 million. Based on information provided by the applicants, USAC now estimates Funding Year 2003 demand will be \$26.658 million. The FCC previously authorized the collection of \$26.171 million for Funding Year 2003. Based on the revised estimate of demand, USAC recommends the FCC increase collections for Funding Year 2003 by \$0.487 million in 2Q2005.

Funding commitments made during 4Q2004 are included in Appendix RH06. Authorized funding by applicant during 4Q2004 and disbursements made to service providers through 4Q2004 are listed in Appendices RH07 and RH08, respectively.

FUNDING YEAR 2004

The Funding Year 2004 application filing window opened on March 29, 2004. Funding Year 2004 began on July 1, 2004, and will end on June 30, 2005. As of December 31, 2004, 2,673 Forms 465 have been posted. In addition, as of December 31, 2004, 1,660 packets have been received including 374 packets from applicants seeking support for Internet access only. The status of Funding Year 2004 packets is provided below.

FUNDING YEAR 2004	
Packets Completely Processed	573
Packets Awaiting Supervisory Approval Only	248
Complete – Ready to Process	229
Withdrawn by Applicant	47
Denied	8
Incomplete – Require Forms and/or Clarification	555
Total Packets Received for Funding Year 2004	1,660

As of December 3, 2004, funding commitments have been issued totaling \$1.464 million. Based on information provided by the applicants as of December 31, 2004, USAC estimates Funding Year 2004 demand will be \$35.867 million. The FCC previously authorized the collection of \$31.900 million for the first three quarters of Funding Year 2004. Based on the estimate of demand, USAC recommends the FCC to authorize the collection of \$3.967 million in 2Q2005 to meet total projected demand.

Funding commitments made during 4Q2004 are included in Appendix RH09. Authorized funding by applicant during 4Q2004 and disbursements made to service providers through 4Q2004 are listed in Appendices RH10 and RH11, respectively.

RURAL HEALTH CARE SUPPORT MECHANISM SUMMARY

The estimated 2Q2005 demand requirement for the Rural Health Care Support Mechanism is \$4.344 million. The 2Q2005 demand requirements will be adjusted for the 4Q2004 results in the January filing. The total adjustment to the 2Q2005 requirement is \$0.822 million. The detailed explanation for the adjustment is as follows:

Reason for the Prior Period Adjustment	ADJUSTMENT IN MILLIONS
The 4Q2004 billings were lower than expected.	\$0.869 M
Interest earned was lower than estimated for the 4Q2004.	\$0.001 M
Bad Debt Expense was lower than anticipated in 4Q2004	(\$0.048 M)
Total Prior Period Adjustment	\$0.822M

The total fund requirement of \$4.344 million, increased by the prior-period adjustment of \$0.822 million, increased by administrative expenses of \$1.012 million, and reduced by the deduction of projected interest of \$0.084 million, results in a total projected funding requirement for the Rural Health Care Support Mechanism for 2Q2005 of \$6.094 million.

SCHOOLS AND LIBRARIES SUPPORT MECHANISM

The following provides a status report on the Schools and Libraries Support Mechanism commitment and disbursements by funding year.

FUNDING YEAR 1998

FUNDING YEAR 1998					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 675.8	39.5%	\$ 507.6	36.3%	75.1%
Internet Access	\$ 134.1	7.8%	\$ 94.9	6.8%	70.7%
Internal Connections	\$ 903.1	52.7%	\$ 796.9	56.9%	88.2%
TOTAL	\$1,713.0		\$1,399.3		81.7%

Note: Columns on table may not add perfectly due to rounding.

No Funding Year 1998 applications remain in the program integrity assurance (PIA) review process.

No payments were made to service providers during 4Q2004.

FUNDING YEAR 1999

FUNDING YEAR 1999					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 635.0	29.5%	\$ 453.9	27.3%	71.5%
Internet Access	\$ 149.3	6.9%	\$ 95.8	5.8%	64.2%
Internal Connections	\$1,366.7	63.5%	\$1,112.2	66.9%	81.4%
TOTAL	\$2,151.0		\$1,661.9		77.3%

Note: Columns on table may not add perfectly due to rounding.

No Funding Year 1999 applications remain in the PIA review process.

Authorized funding by applicant during 4Q2004 and cumulative payments made to service providers through 4Q2004 are listed in Appendices SL01 and SL02, respectively.

FUNDING YEAR 2000

FUNDING YEAR 2000					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 718.4	34.5%	\$ 474.4	28.9%	66.0%
Internet Access	\$ 219.2	10.5%	\$ 134.8	8.2%	61.5%
Internal Connections	\$ 1,144.8	55.0%	\$1,035.3	63.0%	90.4%
TOTAL	\$ 2,082.4		\$ 1,644.5		79.0%

Note: Columns on table may not add perfectly due to rounding.

As of December 31, 2004, one potentially fundable Funding Year 2000 application remained under review pending a decision by the FCC.

Authorized funding by applicant during 4Q2004 is listed in Appendix SL03. No payments were made to service providers during 4Q2004.

FUNDING YEAR 2001

FUNDING YEAR 2001					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 761.3	34.6%	\$ 518.6	31.3%	68.1%
Internet Access	\$ 225.4	10.2%	\$ 148.7	9.0%	65.9%
Internal Connections	\$1,215.5	55.2%	\$ 989.4	59.7%	81.4%
TOTAL	\$2,202.2		\$1,656.6		75.2%

Note: Columns on table may not add perfectly due to rounding.

As of December 31, 2004, four potentially fundable Funding Year 2001 applications remained in the PIA review process.

Authorized funding by applicant during 4Q2004 and cumulative payments made to service providers through 4Q2004 are listed in Appendices SL04 and SL05, respectively.

FUNDING YEAR 2002

FUNDING YEAR 2002					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 856.5	39.5%	\$ 587.2	40.8%	68.6%
Internet Access	\$ 229.2	10.6%	\$ 156.3	10.9%	68.2%
Internal Connections	\$ 1,084.0	50.0%	\$ 696.5	48.4%	64.3%
TOTAL	\$ 2,169.7		\$1,439.9		66.4%

Note: Columns on table may not add perfectly due to rounding.

SLD continues to review and process the remaining 57 potentially fundable applications that were not included in a regular commitment wave and will issue Funding Commitment Decision Letters (FCDLs) on an individual basis.

Funding commitments made to applicants during 4Q2004 are included in Appendix SL06. Authorized funding by applicant during 4Q2004 and cumulative payments to service providers through 4Q2004 are listed in Appendices SL07 and SL08, respectively.

FUNDING YEAR 2003

FUNDING YEAR 2003					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 859.2	33.5%	\$ 503.1	45.1%	58.6%
Internet Access	\$ 242.6	9.5%	\$ 164.9	14.8%	68.0%
Internal Connections	\$1,466.5	57.1%	\$ 448.9	40.2%	30.6%
TOTAL	\$2,568.3		\$1,116.8		43.5%

Note: Columns on table may not add perfectly due to rounding.

As of December 31, 2004, 485 applications remained in the PIA review process

Funding commitments made to applicants during 4Q2004 are included in Appendix SL09. Authorized funding by applicant during 4Q2004 and cumulative payments to service providers through 4Q2004 are listed in Appendices SL10 and SL11, respectively.

FUNDING YEAR 2004

FUNDING YEAR 2004					
	Commitments		Authorized for Payment		Auth/Com
	Millions of Dollars	% of Total Commitments	Millions of Dollars	% of Total Authorized for Payment	% of Committed Authorized for Payment
Telecommunications	\$ 608.7	57.6%	\$ 21.3	58.5%	3.5%
Internet Access	\$ 162.9	15.4%	\$ 13.1	35.9%	8.0%
Internal Connections	\$ 285.9	27.0%	\$ 2.0	5.4%	0.7%
TOTAL	\$1,057.5		\$ 36.4		3.4%

Note: Columns on table may not add perfectly due to rounding.

As of December 31, 2004, approximately 85% of applications certified for processing had received at least one FCDL.

Funding commitments made to applicants during 4Q2004 are included in Appendix SL12. Authorized funding by applicant during 4Q2004 and cumulative payments to service providers through 4Q2004 are listed in Appendices SL13 and SL14, respectively.

SCHOOLS AND LIBRARIES SUPPORT MECHANISM SUMMARY

In a series of actions from December 1999 through December 2002, the FCC used a net total of \$477.16 million of undisbursed Funding Year 1998 funds to reduce collection requirements for the Universal Service Fund. Consistent with the Commission's direction in the *Schools and Libraries First Report and Order*, the FCC used a total of \$852.116 million of undisbursed Funding Years 1999 and 2000 collections to stabilize contributions to the Universal Service Fund and offset collections for 3Q2002, 4Q2002, and 1Q2003.³⁸

In the *Schools and Libraries Third Report and Order and Second Further Notice of Proposed Rulemaking*, the Commission amended its rules so that available unused funds from prior years would be carried forward on an annual basis in the second quarter of each calendar year for use in the next full funding year. The Commission required USAC to file quarterly estimates of unused funds from prior funding years when it submits its projection of Schools and Libraries Support Mechanism demand for the upcoming quarter.³⁹ The Commission modified the schedule to implement the process for Funding Year 2003 and directed USAC to carry forward \$420 million of unused prior year funds for use in Funding Year 2003.⁴⁰ In accordance with the *Schools and Libraries Third Report and Order*, the FCC announced that \$150 million in

³⁸ See *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, First Report and Order, FCC 02-175 (June 13, 2002) (*Schools and Libraries First Report and Order*).

³⁹ See *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Third Report and Order and Second Further Notice of Proposed Rulemaking, FCC 03-323 (December 23, 2003) (*Schools and Libraries Third Report and Order*).

⁴⁰ *Id.*

unused funds from Funding Year 2001 would be carried forward to increase disbursements to schools and libraries in Funding Year 2004.⁴¹

The following sections provide information about the use of funds for each funding year, including adjustments made by the Commission, and USAC’s projections of unused funds from prior funding years available for carrying forward.

FUNDING YEAR 1998 TRUE-UP

As of December 31, 2004, \$1,399.337 million of Funding Year 1998 support had been disbursed. The estimated Funding Year 1998 balance is based on the following:

FUNDING YEAR 1998	Adjustments in Millions
Amount Authorized and Actually Collected	\$ 1,925.000 M
Amount Disbursed	(1,399.337) M
Administrative Expenses (21 months)	(41.791) M
Amount Applied to Adjust 2000, 2001, and 2002 Collections	(477.160) M
Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests	(6.712) M
Estimated Remaining Balance	\$0.000 M

USAC estimates that a contingency amount of \$6.712 million should be reserved to pay appeals pending at the FCC and to pay invoices on funding requests that may be granted extended invoice deadlines pursuant to FCC order. Based on these figures, and in order to preserve the contingency amount, no Funding Year 1998 funds are available to carry forward.

FUNDING YEAR 1999 TRUE-UP

As of December 31, 2004, \$1,661.930 million of Funding Year 1999 support had been disbursed. The estimated remaining Funding Year 1999 balance is based on the following:

⁴¹ See *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Carryover of Unused Funds for Funding Year 2004, DA 04-1848 (June 28, 2004).

FUNDING YEAR 1999	Adjustments in Millions
Amount Authorized and Actually Collected	\$ 2,250.000 M
Amount Disbursed	(1,661.930) M
Administrative Expenses	(32.316) M
Amount Applied to Adjust 3Q2002 Collections	(256.160) M
Amount Applied to Adjust 4Q2002 Collections	(212.927) M
Amount Carried Forward to Funding Year 2003	(50.000) M
Potential Additional Disbursements on Committed FRNs	(13.403) M
Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests	(13.264) M
Estimated Remaining Balance	\$10.000 M

USAC’s projection of the remaining Funding Year 1999 funds includes an estimate of funds needed to pay additional disbursements on committed funding requests and a contingency reserve to pay pending appeals and to make disbursements on funding requests that may be granted extended invoice deadlines pursuant to FCC order. Based on these figures, USAC estimates that \$10 million of Funding Year 1999 funds is available to carry forward.

FUNDING YEAR 2000 TRUE-UP

As of December 31, 2004, \$1,644.473 million of Funding Year 2000 support had been disbursed. The estimated remaining Funding Year 2000 balance is based on the following:

FUNDING YEAR 2000	Adjustments in Millions
Amount Authorized and Actually Collected	\$ 2,250.000 M
Amount Disbursed	(1,644.473) M
Administrative Expenses	(32.235) M
Amount Applied to Adjust 4Q2002 Collections	(136.849) M
Amount Applied to Adjust 1Q2003 Collections	(246.180) M
Amount Carried Forward to Funding Year 2003	(160.000) M
Potential Additional Disbursements on Committed FRNs	(1.401) M
Remaining Uncommitted Requests	(1.658) M
Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests	(17.204) M
Estimated Remaining Balance	\$10.000 M

USAC’s projection of the remaining Funding Year 2000 funds includes estimates of funds needed to pay additional disbursements on committed funding requests and disbursements

on remaining requests that have not received funding commitments, as well as a contingency reserve to pay pending appeals and to make disbursements on funding requests that may be granted extended invoice deadlines pursuant to FCC order. Based on these figures, USAC estimates that \$10 million of Funding Year 2000 funds is available to carry forward.

FUNDING YEAR 2001 TRUE-UP

As of December 31, 2004, \$1,656.646 million of Funding Year 2001 support had been disbursed. The estimated remaining Funding Year 2001 balance is based on the following:

FUNDING YEAR 2001	Adjustments in Millions
Amount Authorized and Actually Collected	\$ 2,250.000 M
Amount Disbursed	(1,656.646) M
Administrative Expenses	(30.559) M
Amount Carried Forward to Funding Year 2003	(210.000) M
Amount Carried Forward to Funding Year 2004	(150.000) M
Potential Additional Disbursements on Committed FRNs	(65.422) M
Remaining Uncommitted Requests	(40.750) M
Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests	(46.623) M
Estimated Remaining Balance	\$50.000 M

USAC’s projection of the remaining Funding Year 2001 funds includes estimates of funds needed to pay additional disbursements on committed funding requests and disbursements on remaining requests that have not yet received funding commitments, as well as a contingency reserve to pay pending appeals and to make disbursements on funding requests that may be granted extended invoice deadlines pursuant to FCC order. Based on these figures, USAC estimates that \$50 million of Funding Year 2001 funds is available to carry forward.

FUNDING YEAR 2002 TRUE-UP

As of December 31, 2004, \$1,439.914 million of Funding Year 2002 support had been disbursed. The estimated remaining Funding Year 2002 balance is based on the following:

FUNDING YEAR 2002	Adjustments in Millions
Amount Authorized and Actually Collected	\$ 2,250.000 M
Amount Disbursed	(1,439.914) M
Administrative Expenses	(38.531) M
Potential Additional Disbursements on Committed FRNs	(276.594) M
Remaining Uncommitted Requests	(65.504) M
Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests	(329.457) M
Estimated Remaining Balance	\$100.000 M

USAC's projection of the remaining Funding Year 2002 funds includes estimates of funds needed to pay additional disbursements on committed funding requests and disbursements on requests that have not yet received funding commitments, as well as a contingency reserve to pay pending appeals and to make disbursements on funding requests that may be granted extended invoice deadlines pursuant to FCC order. Based on these figures, USAC estimates that \$100 million of Funding Year 2002 funds is available to carry forward.

2Q2005 DEMAND ESTIMATE AND CONTRIBUTION REQUIREMENT

Pursuant to FCC order, USAC changed the accounting methodology for the Universal Service Fund (USF) to generally accepted accounting principles for government entities on October 1, 2004.⁴² FCC staff has determined that FCDLs for Schools and Libraries Support Mechanism funding are to be treated as "obligations" for federal budgetary accounting purposes.⁴³ Although the Federal Antideficiency Act (ADA), 31 U.S.C. § 1341, generally requires that unobligated resources be available before any obligation can be incurred, the United States Congress passed and the President signed legislation in December 2004 to exempt the Universal Service Fund (USF) from the ADA until December 31, 2005.⁴⁴

⁴² See *In re Application of Generally Accepted Accounting Principles for Federal Agencies and Generally Accepted Government Auditing Standards to the Universal Service Fund*, CC Docket No. 96-45, Order, FCC 03-232 (rel. Oct. 3, 2003).

⁴³ FCC staff has indicated that Rural Health Care Support Mechanism funding commitments are also "obligations" for government accounting purposes. USAC has requested clarification regarding whether projections and other data submitted by USAC to the FCC and by participants in the High Cost and Low Income Support Mechanisms to USAC must be treated in a similar manner.

⁴⁴ See H.R. 5419, 108th Cong. 2d Sess., § 302, Universal Service Antideficiency Temporary Suspension Act (effective Dec. 23, 2004).

In order to reduce the large USF cash reserve that has accumulated primarily because structural aspects of the program result in actual disbursements lagging commitments —while at the same time retaining the ability for the USF to satisfy all outstanding commitments based on historic disbursement patterns — the Commission applied a total of \$550 million of the undisbursed USF balance from prior years against schools and libraries program demand in 2004. The Commission applied \$200 million of the cash balance in both 2Q2004 and 3Q2004. The Commission used \$150 million in 4Q2004.

The recent FCC actions to manage the USF cash reserve and the accounting system changes reduced the unobligated cash balance for the Schools and Libraries Support Mechanism. In anticipation of the conversion to government accounting rules, and due to the questions surrounding whether funding commitments and USF investments were to be treated as “obligations” under government accounting standards and whether the ADA applied to the USF, USAC suspended issuance of Schools and Libraries Support Mechanism FCDLs in early August 2004. After USAC obtained guidance from the FCC on the accounting questions, USAC resumed issuing commitments in December 2004 using unobligated funds. USAC submitted a 1Q2005 demand estimate and contribution requirement to the FCC that included recovery of one-half of the \$550 million used by the Commission to stabilize the contribution factor in 2Q2004, 3Q2004, and 4Q2004. After passage of the legislation temporarily exempting the USF from the ADA, the Commission did not include the \$275 million in the demand estimate used to calculate the 1Q2005 contribution factor.

USAC management does not propose at this time to recover some or all of the \$550 million in 2Q2005. USAC is analyzing potential effects of the Universal Service Antideficiency Temporary Suspension Act and consulting with the Commission in order to obtain guidance regarding implementation of the statute. USAC anticipates providing results of that analysis and

a recommendation, if any, for recovery of any portion of the \$550 million as part of the 2Q2005 Revenue Data Filing due to the Commission on March 2, 2005.

At this time, USAC requests authority to collect \$562.500 million, an amount equal to one-quarter of the annual \$2.250 billion cap on federal universal service support for schools and libraries.

Results for 4Q2004 contributed to an under-funded condition for which the instant filing proposes to adjust the 2Q2005 requirements. The total adjustment to the 2Q2005 fund requirement based on actual results will increase the funding needed by \$26.564 million. The explanation for the adjustment is described below:

Reason for the Prior Period Adjustment	Adjustment in Millions
4Q2004 billings were lower than projected	\$ 35.635 M
Interest earned was lower than projected.	1.423 M
Bad debt expense was lower than anticipated.	(10.493) M
Total Prior Period Adjustment	\$26.564 M

Note: Column on table may not add perfectly due to rounding.

The fund requirement of \$562.500 million, which includes administrative expenses of \$18.432 million, increased by the prior-period adjustment of \$26.564 million, and reduced by the projected interest of \$11.609 million, results in a projected collection requirement of \$577.455 million for the Schools and Libraries Support Mechanism for 2Q2005.

CONTRIBUTION BASE

USAC collects quarterly interstate and international revenue information from carriers on the FCC Form 499-Q four times each year and submits aggregate information on a quarterly basis to the FCC (March 2, June 1, September 1, and December 2).⁴⁵ Based on these filings, the FCC establishes the contribution factor for the upcoming quarter. Telecommunications providers qualifying for the *de minimis* exemption from contribution requirements need not complete the

⁴⁵ The Form 499-Q includes a box for each of the quarterly filing submissions. Carriers check the appropriate box to indicate the quarter for which revenue information is being reported.

Form 499-Q. USAC reports and the FCC uses projected collected revenues in order to determine the contribution factor.

Approximately 5,384 FCC Forms 499-Q were distributed to carriers in early January 2005. Interstate telecommunications service providers are required to complete this form, reporting April - June 2005 projected revenue information, and return it by February 1, 2005.

OPERATIONS

USAC invoices and receives contributions from more than 2,200 telecommunications companies each month. Over the course of the year USAC disburses funds to service providers as appropriate under each of the support mechanisms. USAC has been able to maintain the uncollectible rate below 1 percent of the total funds billed to contributing telecommunications carriers.

USAC continues to assist the FCC in its USF collection enforcement efforts. USAC works closely with the FCC to obtain compliance from carriers not remitting required contributions, and provides required documentation monthly to assist the FCC in issuing Notices of Apparent Liability (NALs) against non-payers. USAC also assists the FCC by working with carriers to achieve compliance with filing and contribution requirements; by providing information to the FCC regarding carriers that have not filed a Form 499; by providing monthly reports listing non-payers by amount owed and by type of carrier; by contacting the FCC to determine which non-paying carriers, if any, have petitioned the FCC regarding their funding obligation; and by providing the FCC with call log information and written correspondence of carriers that have not filed a petition with the FCC.

USAC successfully implemented the Red Light Rule on November 1, 2004 and has been following additional guidelines for debt treatment. If a contributor is over one day delinquent to the fund, USAC performs USF-to-USF administrative offsets to resolve the delinquency, netting

any pending service provider disbursements where the Service Provider Identification Number (SPIN) shares the same Taxpayer Identification Number (TIN) as the delinquent contributor. If an entity is over one day delinquent on a debt owed to the FCC, USAC is placing administrative holds on any disbursements for those SPINs that share the same TIN until the FCC provides information stating that the debt has been satisfied.

The impacts of the Red Light Rule implementation have been very positive to date. In one month, USAC has seen a noticeable change in contributor payment behavior. Many outstanding contributor debts to USAC have been satisfied through the forced netting procedures of the Red Light Rule. As the FCC continues to define additional Red Light Rule requirements, USAC is prepared to implement new processes and new procedural checks based on the instructions provided by the FCC. USAC is working with the FCC's Office of the Managing Director (OMD) and Wireline Competition Bureau (WCB) on the USAC implementation plan and outstanding questions.

CONCLUSION

At their January 24, 2005 meetings, USAC's High Cost & Low Income Committee, Rural Health Care Committee, and Schools & Libraries Committee passed resolutions authorizing the 2Q2005 support mechanism funding requirements described herein. At its January 25, 2005, meeting, the USAC Board of Directors adopted a resolution authorizing the inclusion of the 2Q2005 administrative expenses and 2Q2005 funding base in this report to the Commission.

Respectfully submitted,

UNIVERSAL SERVICE
ADMINISTRATIVE COMPANY

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