

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC**

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY

Federal Universal Service Support Mechanisms Fund Size
Projections for the Fourth Quarter 2006

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

**FEDERAL UNIVERSAL SERVICE SUPPORT MECHANISMS
FUND SIZE PROJECTIONS FOR THE FOURTH QUARTER
2006**

INTRODUCTION

The Universal Service Administrative Company (USAC) submits the federal Universal Service Support Mechanisms fund size and administrative cost projections for the fourth quarter of calendar year 2006 (4Q2006), 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 Fund (USF) and the universal service support mechanisms: High Cost, Low Income, Rural Health Care, and Schools and Libraries.² USAC also performs the billing, collection, and disbursement functions for the 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 amounts owed from contributors, 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 INCOME 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, 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 USAC's methodology for allocating costs submitted to the Commission. On January 1, 2006, USAC implemented a revised methodology for allocating joint and common costs that was filed with the Commission on October 3, 2005.⁵

USAC projects a consolidated budget of \$25.267 million for 4Q2006. Direct costs for all support mechanisms total \$20.921 million⁶ and are listed for each mechanism in the chart provided below. Joint and common costs (including billing, collection, and disbursement activities) are projected at \$4.346 million and are allocated to each support mechanism as described in the chart below based on the allocation methodology on file with the Commission.

⁴ 47 C.F.R. § 54.709(a)(3).

⁵ See Letter from D. Scott Barash to Marlene H. Dortch regarding Revisions to the Method for Allocating Costs Among the Four Universal Service Support Mechanisms, CC Docket Nos. 97-21 and 96-45 (Oct. 3, 2005).

⁶ This includes \$0.090 million for High Cost Loop (HCL) data collection performed by the National Exchange Carrier Association (NECA). See 47 C.F.R. §§36.611-.613 and 47 C.F.R. § 69.603. 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).

Universal Service Administrative Company 4Q2006 Fund Size Projections

4th Quarter 2006 Administrative Expenses (millions)

| USF Mechanism | Direct Costs | USAC Common | Total |
|--------------------------------|---------------------|--------------------|-----------------|
| High Cost | \$2.012 | \$1.586 | \$3.598 |
| Low Income | .903 | .339 | 1.242 |
| Rural Health Care | .820 | .139 | 0.959 |
| Schools & Libraries | 17.186 | 2.282 | 19.468 |
| Total | \$20.921 | \$4.346 | \$25.267 |

Appendix M01 details USAC's administrative expense budget for 4Q2006.

Appendix M02 details the fund size projections for 4Q2006.

INTEREST INCOME PROJECTION

For 4Q2006, USAC projects interest income of approximately \$4.287 million for the High Cost Support Mechanism, \$2.466 million for the Low Income Support Mechanism, \$0.560 million for the Rural Health Care Support Mechanism, and \$40.111 million for the Schools and Libraries Support Mechanism. USAC projects total interest income of \$47.424 million. As in previous quarters, the projected interest income is being included as an offset to administrative expenses for each of the support mechanisms 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

For the three months ended June 30, 2006, on a cash basis, USAC disbursed \$1,659.680 million in universal service support as follows: \$998.000 million in High Cost support, \$204.056 million in Low Income support, \$447.650 million in Schools and Libraries support, and \$9.973 million in Rural Health Care support. On a cash basis, the total cash balance available as of June 30, 2006 to the universal service support mechanisms was

\$4,253.871 million. On an accrual basis, USAC had a fund balance of \$4,433.349 million at June 30, 2006.

Appendices M03 and M04 provide 2006 year-to-date statements of fund activity on a cash and accrual basis.

FUNDING REQUIREMENTS

HIGH COST SUPPORT MECHANISM

ELIGIBLE TELECOMMUNICATIONS CARRIER (ETC) DESIGNATION

A requirement of 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 Part 36 and Subpart D of Part 54 of the Commission's rules.⁷ ETCs are eligible to receive funds from the High Cost Support Mechanism,⁸ which includes High Cost Loop (HCL) support, Interstate Access Support, Local Switching Support, Interstate Common Line Support, and High Cost Model support. Together, the projected requirements for these five components of the High Cost Support Mechanism and 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

⁷ See 47 U.S.C. § 214(e), 47 C.F.R. § 54.201.

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

Universal Service Administrative Company 4Q2006 Fund Size Projections

carriers and rate-of-return versus price cap carriers.

| Count of Study Areas by Category | | | | | | | | |
|---|------------------------------|-------------------------|--------------|------------|------------------|------------------------|--------------------------------|--------------------------|
| | Incumbent Study Areas | | | | Price Cap | Total Incumbent | Competitive Study Areas | Total Study Areas |
| | Rate-of-Return | | | | | | | |
| | Cost Companies | Average Schedule | Total | | | | | |
| Rural | 760 | 492 | 1244 | 105 | 1357 | 223 | 1580 | |
| Non-Rural | 4 | 1 | 5 | 80 | 85 | 197 | 282 | |
| Total | 764 | 493 | 1249 | 185 | 1442 | 420 | 1862 | |

Appendix HC01 displays the projected minimum amount of individual company support segregated by rural and non-rural status. Appendix HC01 also contains the projected per-month amount for each component of High Cost support that each ETC⁹ will be eligible to receive (i.e., HCL, High Cost Model Support, Interstate Access Support, Local Switching Support, and Interstate Common Line Support). Appendix HC02 displays the total projected amount of High Cost support for 4Q2006 for each state or territory. HC03 displays rural study areas with competition. HC04 displays disaggregated per-line High Cost support by zone, consistent with disaggregation plans filed with USAC.

HIGH COST RURAL SUPPORT MECHANISM

High Cost Loop (HCL) Support

HCL support is calculated based on the results of the annual collection of 2004 incumbent local exchange carrier (LEC) loop cost and expense adjustment data that was submitted to the Commission and USAC on October 1, 2005.¹⁰ Growth in total HCL support for rural carriers is limited under Section 36.603(a) of the Commission’s rules to the current level of funding increased yearly by the annual growth in supported rural loops.

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

¹⁰ Universal Service Fund (USF) 2005 Submission of 2004 Study Results (filed October 1, 2005) (*USF Data Submission*).

Universal Service Administrative Company 4Q2006 Fund Size Projections

Effective July 1, 2001, pursuant to the *RTF Order*,¹¹ HCL support increased for rural companies.

Rural HCL support for calendar year 2006 will be less than the level of payments for 2005 because of a rural growth factor of negative 0.7466 percent. Rural HCL support for calendar year 2006, therefore, is capped at \$1,047.300 million.

Pursuant to the *RTF Order*, Safety Net Additive (SNA) support is support above the HCL cap for carriers that make significant investment in rural infrastructure in years in which HCL is capped.¹² To receive support, a rural carrier must show that growth in telecommunications plant in service (TPIS) per line is at least 14 percent greater than the study area's TPIS in the prior year. Carriers seeking to qualify for SNA support must provide written notice to USAC that a study area meets the 14 percent TPIS trigger.¹³ For 4Q2006, projected SNA support is \$5.473 million.

Also pursuant to the *RTF Order*, Safety Valve Support (SVS) is support above the HCL cap for rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.¹⁴ SVS is 50% of the difference between the index year HCL support amount and the HCL support amount in subsequent

¹¹ 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*).

¹² See *RTF Order* at ¶¶ 77-90.

¹³ See 47 C.F.R. § 36.605(c).

¹⁴ See *RTF Order* at ¶¶ 91-119.

Universal Service Administrative Company 4Q2006 Fund Size Projections

years.¹⁵ SVS is subject to an overall cap of no more than 5% of the HCL fund in any given year.¹⁶ For 4Q2006, projected SVS is \$0.593 million.

For 4Q2006, USAC projected HCL support is \$336.487 million. Of this amount, \$261.745 million is associated with rural carriers and \$74.742 million is associated with competitive ETCs. In addition, 4Q2006 SNA support is projected to be \$5.473 million and SVS is projected to be \$0.593 million. Based on these projections, total 4Q2006 HCL Support is projected to be \$342.554 million, and total annual 2006 HCL support is estimated to be \$1,358.785 million.

Appendix HC05 displays projected monthly HCL support payments by study area for 4Q2006. HC06 displays projected monthly SNA support payments by study area for 4Q2006. Appendix HC07 displays SVS for 4Q2006.

Local Switching Support (LSS)

ETC study areas having 50,000 or fewer access lines are eligible to receive support for local switching costs.¹⁷ Local Switching Support (LSS) is the product of a carrier's annual unseparated local switching revenue requirement multiplied by its local switching support factor.¹⁸

For 4Q2006, LSS for companies participating in the Traffic Sensitive Pool is projected to be \$57.273 million for cost study areas and \$19.677 million for average schedule study areas. LSS for non-Pool study areas is projected to be \$17.386 million for cost study

¹⁵ 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 ¶ 9. In addition, the FCC amended Section 54.305 to provide that rural carriers that acquire high cost exchanges may receive SVS for the investment made in the first year of operating the acquired exchanges. *Id.* at ¶ 10.

¹⁶ See 47 C.F.R. § 54.305(e).

¹⁷ See 47 C.F.R. § 54.301.

¹⁸ The LSS factor is defined as the difference between the 1996 weighted interstate Dial Equipment Minute (DEM) factor and the 1996 unweighted DEM factor.

Universal Service Administrative Company 4Q2006 Fund Size Projections

areas and \$1.902 million for average schedule study areas. In addition, 4Q2006 LSS for competitive ETCs is projected to be \$26.958 million. USAC projects, therefore, that \$123.196 million will be required for 4Q2006. Based on these projections, total 2006 LSS is estimated to be \$487.040 million.

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

INTERSTATE COMMON LINE SUPPORT MECHANISM (ICLS)

Interstate Common Line Support (ICLS) is designed to permit each rate-of-return carrier to recover its common line revenue requirement, while ensuring that its subscriber line charges (SLCs) remain affordable to its customers.¹⁹

For 4Q2006, ICLS for incumbent rate-of-return carriers is projected to be \$233.901 million. In addition, 4Q2006 ICLS for competitive ETCs is projected to be \$79.478 million. USAC projects, therefore, that \$313.379 million in ICLS will be required for 4Q2006. Based on these projections, total 2006 ICLS is estimated to be \$1,260.474 million.

Appendices HC09, HC10, and HC11 detail USAC's 4Q2006 projection of ICLS by study area, per line and by state, respectively. Appendix HC22 reflects the 2004 true-up for ICLS by state by study area, and HC23 reflects the 2004 true-up per line for ICLS.

INTERSTATE ACCESS SUPPORT MECHANISM (IAS)

Interstate Access Support (IAS) helps offset interstate access charges for price cap companies.²⁰ The *Interstate Access Order* targets the support mechanism at \$650 million annually for five years.²¹

¹⁹ 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*).

²⁰ 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*).

²¹ See *Interstate Access Order* at ¶ 201.

Universal Service Administrative Company 4Q2006 Fund Size Projections

The IAS projected industry-wide totals for 4Q2006 are \$38.026 million for rural carriers, \$95.913 million for non-rural carriers, and \$46.008 million for competitive ETCs. USAC projects \$179.947 million will be required for 4Q2006 with total annual IAS estimated to be \$716.509 million.

Appendices HC12, HC13, and HC14 detail USAC's 4Q2006 projection of IAS by study area, line, and state, respectively.

NON-RURAL FORWARD-LOOKING MECHANISM

Under the most recent calculation of forward-looking HCM support, 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 2006.²²

For 4Q2006, USAC projects \$85.812 million will be required for HCM support (\$51.621 million for incumbent non-rural carriers and \$34.191 million for competitive ETCs). Based on these projections, total 2006 HCM support is estimated to be \$335.939 million.

Appendices HC15, HC16, and HC17 detail USAC's 4Q2006 projection of non-rural forward-looking support by wire center, state, and study area, respectively.

COMPETITIVE ETC LINES

Appendix HC18 displays competitive ETC lines reported for HCL support by incumbent study area. HC19 displays competitive ETC lines reported for ICLS by incumbent study area. HC20 displays competitive ETC lines reported for IAS by incumbent study area. HC21 displays competitive ETC lines reported for HCM support by incumbent study area.

²² 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).

Universal Service Administrative Company 4Q2006 Fund Size Projections

HIGH COST SUPPORT MECHANISM SUMMARY

USAC estimates the 4Q2006 High Cost Support Mechanism funding requirement as follows: \$342.554 million for HCL support; \$123.196 million for LSS; \$313.379 million for ICLS; \$179.947 million for IAS; and \$85.812 million for HCM for a total of \$1,044.888 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.²³ Increases in the size of the funding requirement for the prior period are added to the projected requirements; decreases from the prior period are subtracted from the projected revenue requirements.

Results for the Second Quarter 2006 (2Q2006) contributed to an over-funded condition for which this filing proposes to adjust the 4Q2006 funding requirements. The total adjustment to the 4Q2006 fund requirement based on actual results will decrease the funding needed by \$121.855 million. The explanation for the adjustment is described below.

| Reason for the Prior Period Adjustment | Adjustment in Millions |
|---|-------------------------------|
| The 2Q2006 actual billings were higher than expected due to higher revenues reported by contributors in quarterly revenue projection and annual true-up filings | \$(82.919) |
| High Cost Support Mechanism distributions were lower than projected in 2Q2006 | (52.302) |
| Interest income was lower than estimated for 2Q2006 | 0.996 |
| Bad debt expense was higher than anticipated | 12.370 |
| Total Prior Period Adjustment | \$(121.855) |

The total fund requirement of \$1,044.888 million, decreased by the prior-period adjustment of \$121.855 million, increased by administrative costs of \$3.598 million, and reduced by projected interest income of \$4.287 million, results in a total projected funding requirement for the High Cost Support Mechanism for 4Q2006 of \$922.344 million.

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

Appendix M02 provides information on 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.²⁴ 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.²⁵ Lifeline support provides funding from the interstate jurisdiction of up to \$10.00 per low-income subscriber per month, which can consist of a baseline amount of between \$3.50 and \$6.50 (Tier One),²⁶ 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 if the state provides support for the low-income subscriber as well (Tier Three).²⁷ Further, up to an additional \$25 per low-income subscriber per month is available to eligible residents of tribal lands (Tier Four).²⁸

For 4Q2006, USAC projects \$189.856 million will be required for Lifeline support. Based on this projection, total 2006 Lifeline support is estimated to be \$778.618 million.

²⁴ See 47 C.F.R. §§ 54.201.

²⁵ 47 C.F.R. §§ 54.401 - 54.417.

²⁶ 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 ¶ 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 ¶ 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).

²⁷ 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.

²⁸ 47 C.F.R. § 54.400(e).

LINK UP AMERICA

Link Up support compensates ETCs up to \$30 per eligible subscriber for revenue foregone in offering discounted service initiation fees to qualified low-income individuals.²⁹ The *Tribal Order* authorized additional Link Up support of up to \$70 per qualified low-income subscriber residing on eligible tribal lands.³⁰ For 4Q2006, USAC projects that \$8.060 million will be required for Link Up support. Based on this projection, total annual 2006 Link Up support is estimated to be \$35.554 million.

TOLL LIMITATION SUPPORT

Toll Limitation Support (TLS) compensates ETCs for providing voluntary toll-limitation service based on the carrier's incremental cost of providing toll-limitation services. The Commission 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.³¹ Toll limitation consists of toll blocking, which permits consumers to elect not to allow the completion of outgoing toll calls, and toll control, which allows consumers to specify a certain amount of toll usage that may be incurred per month or per billing cycle.³² For 4Q2006, USAC projects that \$2.191 million will be required for TLS. Based on this projection, total 2006 TLS is estimated to be \$7.656 million.

LOW INCOME SUPPORT MECHANISM SUMMARY

USAC estimates a 4Q2006 funding requirement for the Low Income Support Mechanism of \$200.107 million. This estimate includes \$189.856 million for Lifeline, \$8.060 million for Link Up, and \$2.191 million for Toll Limitation Service. Results of 2Q2006

²⁹ 47 C.F.R. §§ 54.411, .413.

³⁰ See *Promoting Deployment and Subscribership in Unserved and Underserved Areas, Including Tribal and Insular Areas*, CC Docket No. 96-45, Twelfth Report and Order, Memorandum Opinion and Order, and Further Notice of Proposed Rule-making, (rel. June 30, 2000)(*Tribal Order*).

³¹ See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) at ¶ 386 (*First Report and Order*) (subsequent history omitted).

³² 47 C.F.R. §§ 54.400(b), (c).

Universal Service Administrative Company 4Q2006 Fund Size Projections

contribute to an over-funded condition, for which this filing proposes to adjust the 4Q2006 funding requirements. The total adjustment to the 4Q2006 funding requirement based on actual results will decrease the funding needed by \$27.548 million.

The explanation for the adjustment is described below.

| Reason for the Prior Period Adjustment | Adjustment in Millions |
|---|-------------------------------|
| The 2Q2006 actual billings were higher than expected due to higher revenues reported by contributors in quarterly revenue projection and annual true-up filings | \$(18.397) |
| Low Income Support Mechanism distributions were lower than projected in 2Q2006 | (11.709) |
| Interest income was higher than estimated for 2Q2006 | (0.721) |
| Bad debt expense was higher than anticipated | 3.279 |
| Total Prior Period Adjustment | \$(27.548) |

The total fund requirement of \$200.107 million, decreased by the prior period adjustment of \$27.548 million, increased for administrative expenses of \$1.242 million, and decreased by the deduction of the projected interest income of \$2.466 million results in a total projected funding requirement for the Low Income Support Mechanism for 4Q2006 of \$171.335 million.

Appendix LI01 provides projected Low Income support amounts by state and study area for 4Q2006. LI02 provides detail on Low Income funding amounts available in each of the states and territories for 4Q2006. LI03 provides a list of ETCs for 2Q2006. LI04 provides detail on quarterly company-specific Low Income support disbursement amounts for 2Q2006. LI05 provides detail on annual company-specific Low Income support amounts through 2Q2006. LI06 provides historical data of monthly support amounts claimed by ETCs from January 1998 through June 2006. LI07 provides detail on Low Income support distributed by state for 2001 through 1Q2006. LI08 and LI09 provide subscriber information by state and jurisdiction for Lifeline and Link Up support, respectively. LI10 shows the Tier 1 amounts reported by all companies during 1Q2006.

RURAL HEALTH CARE SUPPORT MECHANISM

The following provides a status report on the Rural Health Care Support Mechanism commitments and disbursements for Funding Years 2002-06, as of June 30, 2006. Prior funding years are closed.

FUNDING YEAR 2002

Funding Year 2002 began on July 1, 2002 and ended on June 30, 2003. As of June 30, 2006, funding commitments have been issued totaling \$23.369 million. Based on information provided by applicants, USAC now estimates Funding Year 2002 demand will be \$22.062 million. The Commission previously authorized the collection of \$22.259 million for Funding Year 2002.

Authorized disbursements made to service providers through 2Q2006 are listed in Appendix RH01.

FUNDING YEAR 2003

Funding Year 2003 began on July 1, 2003 and ended on June 30, 2004. As of June 30, 2006, funding commitments have been issued totaling \$27.932 million. Based on information provided by applicants, USAC now estimates Funding Year 2003 demand will be \$26.250 million. The Commission previously authorized the collection of \$26.250 million.

Authorized funding by applicant during 2Q2006 and disbursements made to service providers through 2Q2006 are listed in Appendices RH02 and RH03, respectively.

FUNDING YEAR 2004

Funding Year 2004 began on July 1, 2004 and ended on June 30, 2005. As of June 30, 2006, 2,999 FCC Form 465s have been posted. In addition, as of June 30, 2006, 4,667

Universal Service Administrative Company 4Q2006 Fund Size Projections

FCC Form 466 and 466-A “packets” have been received, including 810 packets from applicants seeking support for Internet access only.³³

The status of Funding Year 2004 packet processing is provided below.

| FUNDING YEAR 2004 PACKET PROCESSING | |
|---|--------------|
| Completely Processed | 4,202 |
| Awaiting Supervisory Approval Only | 0 |
| Complete – Ready to Process | 0 |
| Withdrawn by Applicant | 332 |
| Denied | 133 |
| Incomplete – Require Forms and/or Clarification | 0 |
| Total Packets Received for Funding Year 2004 | 4,667 |

As of June 30, 2006, funding commitments have been issued totaling \$35.574 million. Based on information provided by applicants as of June 30, 2006, USAC estimates Funding Year 2004 demand will be \$31.676 million. The Commission previously authorized the collection of \$31.64 million for Funding Year 2004. Based on the revised estimate of demand, USAC recommends the Commission increase collections for Funding Year 2004 by \$0.04 million in 4Q2006.

Funding commitments made during 2Q2006 are included in Appendix RH04. Authorized funding by applicant during 2Q2006 and disbursements made to service providers during 1Q2006 are listed in Appendices RH05 and RH06, respectively.

FUNDING YEAR 2005

Funding Year 2005 began on July 1, 2005 and ended on June 30, 2006. As of June 30, 2006, 3,482 Form 465s have been posted. The total demand for Funding Year 2005 is not yet known and will not be known until all Form 466 packets are submitted and processed. USAC estimates Funding Year 2005 demand will be approximately 24% higher

³³ A “packet” typically consists of the FCC Form 466 or 466-A and contracts and invoices from service providers.

Universal Service Administrative Company 4Q2006 Fund Size Projections

than Funding Year 2004, resulting in Funding Year 2005 demand of \$39.339 million. This estimate assumes that applicants who receive support in Funding Year 2004 will receive a similar level of support in Funding Year 2005.

The estimate also projects an increase based on the large number of new applicants in Funding Year 2005. The Funding Year 2005 estimate includes a provision for Funding Year 2004 changes to the Rural Health Care Support Mechanism implemented by the Commission in December 2004. These changes include support for rural health care providers in states that have been designated as rural and who will, therefore, receive a 50% discount on their telecommunications services, as well as any new applicants who become eligible as a result of the new definition of rural. The Funding Year 2005 estimate also provides for the *Hurricane Katrina Relief Order*³⁴ and its impact on the Rural Health Care Program.

The status of Funding Year 2005 packets is provided below.

| FUNDING YEAR 2005 PACKET PROCESSING | |
|---|--------------|
| Completely Processed | 2,539 |
| Awaiting Supervisory Approval Only | 280 |
| Complete – Ready to Process | 26 |
| Withdrawn by Applicant | 353 |
| Denied | 21 |
| Incomplete – Require Forms and/or Clarification | 2,216 |
| Total Packets Received for Funding Year 2005 | 5,435 |

³⁴ See *Federal-State Joint Board on Universal Service, Schools and Libraries Universal Service Support Mechanism, Rural Health Care Support Mechanism, Lifeline and Link-Up*, CC Docket Nos. 96-45, 02-6, WC Docket Nos. 02-60, 03-109, Order, FCC 05-178 (rel. Oct. 14, 2005) (*Hurricane Katrina Relief Order*). In addition, the Commission had previously taken steps to provide relief to parties affected by Hurricane Katrina by extending deadlines and modifying recordkeeping and other USF procedural requirements. See *Schools and Libraries Universal Service Support Mechanism, Rural Health Care Support Mechanism, Lifeline and Link-Up, Federal-State Joint Board on Universal Service*, CC Docket No. 02-6, WC Docket Nos. 02-60, 03-109, CC Docket No. 96-45, Order, DA 05-2484 (rel. Sept. 21, 2005).

Universal Service Administrative Company 4Q2006 Fund Size Projections

The Commission previously authorized the collection of \$38.165 million. Considering the revised demand estimate for Funding Year 2005, USAC recommends that the Commission increase collections for Funding Year 2005 by \$1.174 million in 4Q2006.

Funding commitments made during 2Q2006 are included in Appendix RH07. Authorized funding by applicant during 2Q2006 and disbursements made to service providers during 2Q2006 are listed in Appendices RH08 and RH09, respectively.

FUNDING YEAR 2006

Funding Year 2006 began on July 1, 2006 and will end on June 30, 2007. The filing window for Funding Year 2006 opened on March 13, 2006. USAC estimates that Funding Year 2006 demand will be approximately 6% higher than demand in Funding Year 2005, resulting in a Funding Year 2006 demand of \$41.715 million. USAC recommends that the Commission authorize the collection of one-third of the remaining demand for Funding Year 2006, or \$10.535 million, in 4Q2006 to meet total projected demand.

RURAL HEALTH CARE SUPPORT MECHANISM SUMMARY

The estimated 4Q2006 demand requirement for the Rural Health Care Support Mechanism is \$11.552 million. The results of 2Q2006 contributed to an under-funded condition of \$1.030 million, which will be adjusted in the September 1, 2006 Universal Service Fund Contribution Base filing for the 4Q2006 requirements. The explanation for the adjustment is provided below.

| Reason for the Prior Period Adjustment | Adjustment in Millions |
|--|-------------------------------|
| The 2Q2006 billings were lower than expected due to lower revenues reported by contributors in quarterly revenue projections | \$0.341 |
| Interest income was less than estimated for 2Q2006 | 0.004 |
| Bad debt expense was higher than anticipated | 0.685 |
| Total Prior Period Adjustment | \$1.030 |

Universal Service Administrative Company 4Q2006 Fund Size Projections

The total fund requirement of \$11.552 million, increased by the prior-period adjustment of \$1.030 million and administrative expenses of \$0.959 million, and decreased by projected interest income of \$0.560 million, results in a total projected funding requirement for the Rural Health Care Support Mechanism for 4Q2006 of \$12.981 million.

SCHOOLS AND LIBRARIES SUPPORT MECHANISM

The following provides a status report on the Schools and Libraries Support Mechanism commitments and disbursements by funding year, as of June 30, 2006.

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 | \$ 675.9 | 39.9% | \$ 507.7 | 36.3% | 75.1% |
| Internet Access | \$ 134.2 | 7.9% | \$ 94.8 | 6.8% | 70.7% |
| Internal Connections | \$ 886.1 | 52.2% | \$ 796.6 | 56.9% | 89.9% |
| TOTAL | \$1,696.2 | 100.0% | \$1,399.1 | 100.0% | 82.5% |

As of June 30, 2006, no Funding Year 1998 applications remained under review.

Funding Year 1998 began on January 1, 1998 and ended on June 30, 1999.

No payments were made to service providers during 2Q2006 for Funding Year 1998.

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 | \$ 635.1 | 29.5% | \$ 454.0 | 27.4% | 71.5% |
| Internet Access | \$ 149.5 | 7.0% | \$ 95.8 | 5.8% | 64.1% |
| Internal Connections | \$1,365.6 | 63.5% | \$1,106.4 | 66.8% | 81.0% |
| TOTAL | \$2,150.2 | 100.0% | \$1,656.2 | 100.0% | 77.0% |

Universal Service Administrative Company 4Q2006 Fund Size Projections

As of June 30, 2006, one Funding Year 1999 application remained under review.

Funding Year 1999 began on July 1, 1999 and ended on June 30, 2000.

Cumulative payments made to service providers through 2Q2006 are listed in Appendix SL01.

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 | \$ 719.0 | 34.6% | \$ 480.3 | 29.1% | 66.8% |
| Internet Access | \$ 219.1 | 10.6% | \$ 135.1 | 8.2% | 61.7% |
| Internal Connections | \$1,136.6 | 54.8% | \$1,033.8 | 62.7% | 91.0% |
| TOTAL | \$2,074.7 | 100.0% | \$1,649.2 | 100.0% | 79.5% |

As of June 30, 2006, no Funding Year 2000 applications remained under review.

Funding Year 2000 began on July 1, 2000 and ended on June 30, 2001.

Authorized funding by applicant during 2Q2006 and cumulative payments made to service providers through 2Q2006 are listed in Appendices SL02 and SL03, respectively.

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 | \$ 767.8 | 34.9% | \$ 531.2 | 31.5% | 69.2% |
| Internet Access | \$ 226.4 | 10.3% | \$ 151.3 | 9.0% | 66.8% |
| Internal Connections | \$1,205.9 | 54.8% | \$1,002.9 | 59.5% | 83.2% |
| TOTAL | \$2,200.1 | 100.0% | \$1,685.4 | 100.0% | 76.6% |

Universal Service Administrative Company 4Q2006 Fund Size Projections

As of June 30, 2006, 153 potentially fundable Funding Year 2001 applications remained under review. Funding Year 2001 began on July 1, 2001 and ended on June 30, 2002.

Authorized funding by applicant during 2Q2006 and cumulative payments made to service providers through 2Q2006 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 | \$ 852.6 | 38.5% | \$ 604.7 | 39.0% | 70.9% |
| Internet Access | \$ 248.6 | 11.2% | \$ 172.0 | 11.1% | 69.2% |
| Internal Connections | \$1,116.3 | 50.3% | \$ 773.1 | 49.9% | 69.3% |
| TOTAL | \$2,217.5 | 100.0% | \$1,549.8 | 100.0% | 69.9% |

As of June 30, 2006, USAC continued to review 91 potentially fundable Funding Year 2002 applications. Funding Year 2002 began on July 1, 2002 and ended on June 30, 2003.

Funding commitments made to applicants during 2Q2006 are included in Appendix SL06. Authorized funding by applicant during 2Q2006 and cumulative payments to service providers through 2Q2006 are listed in Appendices SL07 and SL08, respectively.

Universal Service Administrative Company 4Q2006 Fund Size Projections

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 | \$ 885.4 | 33.2% | \$ 635.5 | 34.2% | 71.8% |
| Internet Access | \$ 267.3 | 10.0% | \$ 194.5 | 10.4% | 72.8% |
| Internal Connections | \$1,518.0 | 56.8% | \$ 1029.9 | 55.4% | 67.8% |
| TOTAL | \$2,670.7 | 100.0% | \$1,859.9 | 100.0% | 69.6% |

As of June 30, 2006, 104 Funding Year 2003 applications remained under review.

Funding Year 2003 began on July 1, 2003 and ended on June 30, 2004.

Funding commitments made to applicants during 2Q2006 are included in Appendix SL09. Authorized funding by applicant during 2Q2006 and cumulative payments to service providers through 2Q2006 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 | \$ 947.9 | 41.5% | \$ 646.5 | 47.5% | 68.2% |
| Internet Access | \$ 240.6 | 10.5% | \$ 184.6 | 13.6% | 76.8% |
| Internal Connections | \$1,095.6 | 48.0% | \$ 528.4 | 38.9% | 48.2% |
| TOTAL | \$2,284.1 | 100.0% | \$1,359.5 | 100.0% | 59.5% |

As of June 30, 2006, 228 Funding Year 2004 applications remained under review.

Funding Year 2004 began on July 1, 2004 and ended on June 30, 2005.

Funding commitments made to applicants during 2Q2006 are included in Appendix SL12. Authorized funding by applicant during 2Q2006 and cumulative payments to service providers through 2Q2006 are listed in Appendices SL13 and SL14, respectively.

Universal Service Administrative Company 4Q2006 Fund Size Projections

FUNDING YEAR 2005

| FUNDING YEAR 2005 | | | | | |
|----------------------------|----------------------------|-------------------------------|-------------------------------|--|--|
| | 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 | \$ 909.9 | 54.3% | \$ 250.1 | 51.9% | 27.5% |
| Internet Access | \$ 250.4 | 15.0% | \$ 120.2 | 25.0% | 48.0% |
| Internal Connections | \$ 423.3 | 25.3% | \$ 71.4 | 14.8% | 16.9% |
| Internal Connections-Maint | \$ 90.8 | 5.4% | \$ 39.8 | 8.3% | 43.8% |
| TOTAL | \$1,674.4 | 100.0% | \$ 481.5 | 100.0% | 28.8% |

As of June 30, 2006, approximately 769 Funding Year 2005 applications remained under review.

Funding Year 2005 began on July 1, 2005 and ended on June 30, 2006. Funding commitments made to applicants during 2Q2006 are included in Appendix SL15.

Authorized funding by applicant and cumulative payments to service providers through 2Q2006 are listed in Appendices SL16 and SL17, respectively.

FUNDING YEAR 2006

| FUNDING YEAR 2006 | | | | | |
|----------------------------|----------------------------|-------------------------------|-------------------------------|--|--|
| | 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 | \$ 338.3 | 76.2% | | | |
| Internet Access | \$ 105.8 | 23.8% | | | |
| Internal Connections | - | - | | | |
| Internal Connections-Maint | - | - | | | |
| TOTAL | \$ 444.1 | 100.0% | | | |

As of June 30, 2006, 14,414 funding commitment decision letters (FCDLs) had been mailed to applicants. Funding Year 2006 began on July 1, 2006 and will end on June 30,

2007. Funding commitments made to applicants during 2Q2006 are included in Appendix SL18.

SCHOOLS AND LIBRARIES SUPPORT MECHANISM SUMMARY

In the *Schools and Libraries Third Report and Order and Second Further Notice of Proposed Rulemaking*, the Commission amended its rules to allow unused funds from prior funding years to be carried forward on an annual basis in the second quarter of each calendar year for use in the next full funding year.³⁵ The Commission required USAC to file quarterly estimates of unused funds from prior funding years in submitting its projection of Schools and Libraries Support Mechanism demand for the upcoming quarter. 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 2003.³⁶ In accordance with the *Schools and Libraries Third Report and Order*, the Commission announced that \$150 million in unused funds from Funding Year 2001 would be carried forward to increase disbursements to schools and libraries in Funding Year 2004.³⁷

The following sections provide information regarding the use of funds for each funding year, including adjustments made by the Commission and projections of unused funds as required by Commission rules.

Funding Year 1998 True-Up

As of June 30, 2006, \$1,399.157 million of Funding Year 1998 support had been disbursed. USAC estimates that a contingency amount of \$6.860 million should be reserved to pay appeals pending at the Commission and to pay invoices on funding requests that may be granted extended invoice deadlines pursuant to Commission orders. Given these

³⁵ See *Schools and Libraries Universal Service Support Mechanism*, CC Docket 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*).

³⁶ *Id.*

³⁷ 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).

Universal Service Administrative Company 4Q2006 Fund Size Projections

requirements and to preserve the contingency amount, no Funding Year 1998 funds are available to carry forward.

The Funding Year 1998 balance is based on the following:

| FUNDING YEAR 1998 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 1,925.000 |
| Amount Disbursed | (1,399.157) |
| Administrative Expenses (21 months) | (41.791) |
| Amount Applied to Adjust 2000, 2001, and 2002 Collections | (477.160) |
| Potential Additional Disbursements on Committed FRNs | (0.032) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (6.860) |
| Estimated Remaining Balance | \$0.000 |

Funding Year 1999 True-Up

As of June 30, 2006, \$1,656.229 million of Funding Year 1999 support had been disbursed. 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 make disbursements on funding requests that may be granted extended invoice deadlines pursuant to Commission orders. Given these requirements, USAC estimates that \$15 million of Funding Year 1999 funds are available to carry forward.

Universal Service Administrative Company 4Q2006 Fund Size Projections

The estimated remaining Funding Year 1999 balance is based on the following:

| FUNDING YEAR 1999 | Adjustment in Millions |
|---|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Disbursed | (1,656.229) |
| Administrative Expenses | (32.316) |
| Amount Applied to Adjust Third Quarter 2002 Collections | (256.160) |
| Amount Applied to Adjust Fourth Quarter 2002 Collections | (212.927) |
| Amount Carried Forward to Funding Year 2003 | (50.000) |
| Potential Additional Disbursements on Committed FRNs | (1.084) |
| Remaining Uncommitted Requests | (2.025) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (24.259) |
| Estimated Remaining Balance | \$15.000 |

Funding Year 2000 True-Up

As of June 30, 2006, \$1,649.234 million of Funding Year 2000 support had been disbursed. 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 contingency reserves to cover potential disbursements in Funding Year 2004, and to pay pending appeals and make disbursements on Funding Year 2000 funding requests that may be granted extended invoice deadlines pursuant to Commission orders. Given these requirements and to preserve the contingency amounts, no Funding Year 2000 funds are available to carry forward.

Universal Service Administrative Company 4Q2006 Fund Size Projections

The estimated remaining Funding Year 2000 balance is based on the following:

| FUNDING YEAR 2000 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Disbursed | (1,649.234) |
| Administrative Expenses | (32.235) |
| Amount Applied to Adjust Fourth Quarter 2002 Collections | (136.849) |
| Amount Applied to Adjust First Quarter 2003 Collections | (246.180) |
| Amount Carried Forward to Funding Year 2003 | (160.000) |
| Potential Additional Disbursements on Committed FRNs | (0.419) |
| Remaining Uncommitted Requests | (0.408) |
| Contingency Reserve for Potential Disbursements in Funding Year 2004 ³⁸ | (10.000) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (14.675) |
| Estimated Remaining Balance | \$0.000 |

Funding Year 2001 True-Up

As of June 30, 2006, \$1,685.420 million of Funding Year 2001 support had been disbursed. 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 contingency reserves to cover potential disbursements in Funding Year 2004, and to pay pending appeals and make disbursements on Funding Year 2001 funding requests that may be granted extended invoice deadlines pursuant to Commission orders. Given these requirements and to preserve the contingency amounts, no Funding Year 2001 funds are available to carry forward.

The estimated remaining Funding Year 2001 balance is based on the following:

³⁸ In a March 17, 2005, letter from FCC Wireline Competition Bureau Chief Jeffrey Carlisle to USAC CEO Lisa Zaina (March 17, 2005 WCB Letter), the FCC authorized USAC to make commitments above the funding cap in Funding Year 2004, noting that "historical disbursement patterns demonstrate that we are unlikely to exceed the \$2.4 billion cap" for Funding Year 2004, but also noting that "USAC represented that it has already collected these funds [that might be committed in excess of the funding cap] and has these funds available."

Universal Service Administrative Company 4Q2006 Fund Size Projections

| FUNDING YEAR 2001 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Disbursed | (1,685.420) |
| Administrative Expenses | (30.559) |
| Amount Carried Forward to Funding Year 2003 | (210.000) |
| Amount Carried Forward to Funding Year 2004 | (150.000) |
| Potential Additional Disbursements on Committed FRNs | (13.559) |
| Remaining Uncommitted Requests | (28.175) |
| Contingency Reserve for Potential Disbursements in Funding Year 2004 ³⁹ | (50.000) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (82.287) |
| Estimated Remaining Balance | \$0.000 |

Funding Year 2002 True-Up

As of June 30, 2006, \$1,549.816 million of Funding Year 2002 support had been disbursed. 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 contingency reserves to cover potential disbursements in Funding Year 2004, and to pay pending appeals and make disbursements on Funding Year 2002 funding requests that may be granted extended invoice deadlines pursuant to Commission orders. Given these requirements, USAC estimates that \$200 million of Funding Year 2002 funds are available to carry forward.

³⁹ See March 17, 2005 WCB Letter.

Universal Service Administrative Company 4Q2006 Fund Size Projections

The estimated remaining Funding Year 2002 balance is based on the following:

| FUNDING YEAR 2002 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Disbursed | (1,549.816) |
| Administrative Expenses | (38.531) |
| Potential Additional Disbursements on Committed FRNs | (84.237) |
| Remaining Uncommitted Requests | (19.308) |
| Contingency Reserve for Potential Disbursements in Funding Year 2004 ⁴⁰ | (100.000) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (258.108) |
| Estimated Remaining Balance | \$200.000 |

Funding Year 2003 True-Up

As of June 30, 2006, \$1,859.912 million of Funding Year 2003 support had been disbursed. USAC's projection of the remaining Funding Year 2003 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 Commission orders. Given these requirements, USAC estimates that \$150 million of Funding Year 2003 funds are available to carry forward.

⁴⁰ See March 17, 2005, WCB Letter..

Universal Service Administrative Company 4Q2006 Fund Size Projections

The estimated remaining Funding Year 2003 balance is based on the following:

| FUNDING YEAR 2003 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Carried Forward from Funding Years 1999, 2000 and 2001 | 420.000 |
| Amount Disbursed | (1,859.912) |
| Administrative Expenses | (44.194) |
| Potential Additional Disbursements on Committed FRNs | (206.985) |
| Remaining Uncommitted Requests | (62.563) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (346.346) |
| Estimated Remaining Balance | \$150.000 |

Funding Year 2004 True-Up

As of June 30, 2006, \$1,359.462 million of Funding Year 2004 support had been disbursed. USAC's projection of the remaining Funding Year 2004 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. Given these requirements and to preserve the contingency amounts, no Funding Year 2004 funds are available to carry forward at this time.

The estimated remaining Funding Year 2004 balance is based on the following:

| FUNDING YEAR 2004 | Adjustment in Millions |
|--|-------------------------------|
| Amount Authorized and Actually Collected | \$ 2,250.000 |
| Amount Carried Forward from Funding Year 2001 | 150.000 |
| Amount Disbursed | (1,359.462) |
| Administrative Expenses (unaudited) | (56.902) |
| Potential Additional Disbursements on Committed FRNs | (493.046) |
| Remaining Uncommitted Requests | (49.625) |
| Contingency Amount for Pending Appeals and Invoice Deadline Extension Requests | (440.965) |
| Estimated Remaining Balance | \$0.000 |

4Q2006 Demand Estimate and Contribution Requirement

Pursuant to FCC order, USAC changed the accounting methodology for the USF to generally accepted accounting principles for government entities on October 1, 2004.⁴¹ Commission staff subsequently determined that Funding Commitment Decision Letters (FCDLs) for the Schools and Libraries Support Mechanism funding are to be treated as “obligations” for federal budgetary accounting purposes and subject to the Antideficiency Act (ADA).⁴² The ADA generally requires that sufficient unobligated resources be available before an obligation can be incurred. Congress exempted the USF from requirements of the ADA through December 31, 2006.⁴³

To reduce the USF cash reserve that has accumulated primarily because the structure of the program necessarily results in significant time lags between the commitments and actual disbursements 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 Support Mechanism demand in 2004. The Commission applied \$200 million of the cash balance in both Second Quarter and Third Quarter 2004, and \$150 million in Fourth Quarter 2004.⁴⁴

⁴¹ 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). **CAN WE GET A FED REGISTER CITE FOR THIS?**

⁴² 31 U.S.C. § 1341.

⁴³ See H.R. 5419, 108th Cong 2d Sess., §302, Universal Service Antideficiency Temporary Suspension Act (effective Dec. 23, 2004) and H.R. 2862, 109th Cong 1st Sess., 8,633, Science, State, Justice, Commerce, and Related Agencies Appropriations Act, 2006 (effective Nov. 22, 2005).

⁴⁴ As stated in its January 31, 2004, Federal Universal Service Support Mechanisms Fund Size Projections for the Second Quarter 2005, and in its subsequent quarterly filings, USAC will continue to consult with the Commission as appropriate concerning the necessity and timing of any recovery of this \$550 million..

Universal Service Administrative Company 4Q2006 Fund Size Projections

Based on the level of applicant demand in Funding Year 2006, which exceeds the annual funding cap of \$2.250 billion, USAC requests authority to collect an amount to provide \$562.500 million in funding for 4Q2006, which is one-quarter of the \$2.250 billion annual cap on federal universal service support for schools and libraries. Results for 2Q2006 contribute to an over-funded condition for which this filing proposes to adjust the 4Q2006 requirements. The total adjustment to the 4Q2006 fund requirement based on actual results will decrease the funding needed by \$41.416 million. The explanation for the adjustment is provided below.

| Reason for the Prior Period Adjustment | Adjustment in Millions |
|---|-------------------------------|
| 2Q2006 billings were higher than projected | \$ (40.978) |
| Interest income was lower than estimated | 0.316 |
| Bad debt expense was lower than anticipated | (0.754) |
| Total Prior Period Adjustment | \$ (41.416) |

The fund requirement of \$562.5 million, which includes administrative expenses of \$19.468 million, decreased by the prior-period adjustment of \$41.416 million, and reduced by the projected interest income of \$40.111 million, results in a projected collection requirement of \$480.973 million for the Schools and Libraries Support Mechanism for 4Q2006.

CONTRIBUTION BASE

USAC collects quarterly interstate and international revenue information from carriers on FCC Form 499-Q four times each year on March 2, June 1, September 1, and December 2, and submits aggregate information on a quarterly basis to the Commission.⁴⁵ Based on these filings, the Commission establishes the contribution factor for the upcoming

⁴⁵ See 47 C.F.R. § 54.709(a)(3). 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. See also 47 C.F.R. §§ 54.706, .708, .711, .713 for contributor reporting requirements.

Universal Service Administrative Company 4Q2006 Fund Size Projections

quarter. The Commission uses USAC projections of collected revenues to determine the contribution factor.

Approximately 5,500 FCC Forms 499-Qs were distributed to carriers in early June 2006. Interstate telecommunications service providers are required to complete this form, reporting October - December 2006 projected revenue information, and return it to USAC by August 1, 2006.

USAC invoices and receives contributions from more than 2,500 telecommunications companies each month. USAC has maintained the uncollectible billings rate below 1% of the total funds billed to contributing telecommunications carriers.

USAC continues to assist the Commission in its USF collection enforcement efforts, including providing documentation on a monthly basis to assist the Commission in issuing Notices of Apparent Liability (NALs) against non-payers. USAC also assists the Commission by working with carriers to achieve compliance with filing and contribution requirements. USAC transfers to the Commission amounts owed to the USF that are 90 days delinquent after USAC has provided delinquent carriers with the notice required under Commission and Debt Collection Improvement Action (DCIA)⁴⁶ requirements. Upon receipt of the outstanding debts, the Commission provides delinquent carriers with notice advising them of their USF debt and the possibility of further enforcement activities pursuant to the DCIA and/or by the Commission's Enforcement Bureau. If a delinquent carrier fails to respond to the Commission's request for payment, the delinquent account is typically forwarded to the United States Treasury Department for collection.

USAC implemented the Red Light Rule on November 1, 2004 for contributor debts to the USF.⁴⁷ If a contributor is delinquent to the USF, USAC performs USF-to-USF

⁴⁶ 31 U.S.C. §§ 3701 et seq.

⁴⁷ 47 C.F.R. § 1.910.

Universal Service Administrative Company 4Q2006 Fund Size Projections

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 delinquent on a debt owed to the Commission, USAC places administrative holds on any disbursements for SPINs that share the same TIN until the Commission provides information stating that the debt has been satisfied. USAC continues to work closely with the Commission and stakeholders affected by the Red Light Rule implementation.

AUTHORIZATION TO FILE WITH THE COMMISSION

At their July 24, 2006 meetings, USAC's High Cost & Low Income Committee, Rural Health Care Committee, and Schools & Libraries Committee adopted resolutions authorizing USAC staff to file with the Commission the 4Q2006 projected support mechanism funding requirements described herein. At its July 25, 2006 meeting, the USAC Board of Directors adopted a resolution authorizing the inclusion of the projected 4Q2006 administrative expenses in this report to the Commission.

Respectfully submitted,

UNIVERSAL SERVICE
ADMINISTRATIVE COMPANY

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