

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE APPLICATION FOR INCREASE IN USE ELIGIBILITY FOR UINTAH BASIN TELECOMMUNICATIONS ASSOCIATION, INC.

DOCKET NO. 05-053-01

DIRECT TESTIMONY

OF

KARL SEARLE

ON BEHALF OF

UINTAH BASIN TELECOMMUNICATIONS ASSOCIATION, INC.

AND

UBET TELECOM, INC.

Q:PLEASE STATE YOUR NAME AND ADDRESS.

A: Karl Searle and I live in Roosevelt, Utah.

Q:BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A:I am currently employed by Uintah Basin Telecommunications Association, Inc. ("UBTA") and UBET Telecom,

Inc., a wholly-owned subsidiary of UBTA (“UBET Telecom”)(collectively, “UBTA-UBET”), as Chief Financial Officer (“CFO”) of both companies. I have been employed in that capacity since March 22, 2005. I have been in the telecommunications business for 19 years. Prior to coming to UBTA-UBET Communications in March 2005, I was with Project Mutual Telephone Cooperative in Rupert, Idaho as CFO for 7 years. Project Mutual is a rural local exchange company operating as a cooperative with approximately 11,500 access lines. I have been a licensed CPA in the State of Idaho since 1988. I hold an Associates Degree in Business Administration from the College of Southern Idaho and a Bachelor’s degree in Business Administration from Idaho State University.

Q: WHAT ARE YOUR RESPONSIBILITIES AS CFO OF UBTA-UBET?

A: As CFO I am ultimately responsible for the accounting and reporting functions of the companies.

Q:ARE YOU AUTHORIZED TO TESTIFY ON BEHALF OF UBTA-UBET IN THIS PROCEEDING?

A: Yes.

Q: HAVE OTHERS BEEN AUTHORIZED TO TESTIFY ON BEHALF OF UBTA-UBET IN THIS PROCEEDING?

A: Yes. Ray Hendershot of GVNW Consulting, Inc., will file direct testimony on behalf of UBTA-UBET covering the cost studies and rationale supporting the proposed increase in USF eligibility. Bruce Todd, the CEO/General Manager of UBTA-UBET, will also file direct testimony on behalf of UBTA-UBET. His testimony addresses the general management and policy considerations involved in the companies’ request for increased USF eligibility.

Q:PLEASE STATE THE NATURE OF YOUR TESTIMONY IN THIS PROCEEDING.

A:My testimony addresses UBTA-UBET’s Application for Increase in USF Eligibility (the “Application”). My testimony will primarily deal with the changes in financial reporting requirements, namely, the implementation of FAS No. 142 related to the impairment of goodwill carried on the financial statements of the company.

Q: WHAT IS FAS 142?

A:FAS is the Statement of Financial Accounting Standards that addresses financial accounting and reporting for

acquired goodwill and other intangible assets. A copy of a Summary of FAS 142 is attached hereto as Exhibit A. The companies are required by their Bylaws, lenders and the Commission, to obtain an annual audited financial report from the companies' auditor which are prepared in accordance with generally accepted accounting principles and which incorporate the requirements of applicable Financial Accounting Standards such as FAS 142.

Q:WHAT IS THE IMPACT OF FAS 142 ON AN ENTITY'S FINANCIAL REPORTING?

A:Prior to FAS 142, the accounting for Goodwill and Intangibles was governed by APB Opinion No. 17. Under that standard, Goodwill and other Intangibles were amortized over their useful life but not to exceed 40 years. The issuance of FAS 142 supersedes APB No. 17 and discontinues the amortization of Goodwill, while requiring the measurement of Goodwill each year. If the goodwill on an entities book exceeds the market value of the Goodwill then an impairment of the goodwill must be recognized on the entities financial statements.

Q:WHAT IS THE DIFFERENCE BETWEEN ACQUISITION ADJUSTMENT AND GOODWILL?

A:It is my understanding that prior to FAS 142, acquisition adjustment was a regulatory term used to describe what is referred to as goodwill in a non-regulatory environment. FAS 142 defines Goodwill as "the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed."

Q:WHY WAS THE IMPACT OF FAS 142 UNKNOWN AND UNFORESEEABLE AT THE TIME OF THE STIPULATION IN THE QWEST ACQUISITION?

A:The Agreement for Purchase and Sale of Telephone Exchanges between UBTA and U S West Communications was dated October 22, 1999. Paragraph 1.7 states "Buyer will not seek recovery of an acquisition adjustment through its regulated interstate or intrastate rates, including from federal or state universal service funds." The Purchase Agreement was executed nearly 2 years prior to the issue date of FAS 142 in June 2001. The purchase of the exchanges was not consummated until April 6, 2001. At the time that the Stipulation between UBET Telecom and the Division of Public Utilities was executed on July 6, 2000 (the "Stipulation"), FAS 142 was not a factor and could not have been addressed at that time or prior to the closing of the sale of the subject exchanges.

Q: DID UBTA-UBET COMMUNICATIONS PLAN FOR AN ACQUISITION ADJUSTMENT IN ITS BUSINESS PLAN TO PURCHASE THE US WEST (QWEST) EXCHANGES?

A: Yes. The acquisition adjustment was planned to be amortized over 15 years.

1Q: WHAT OTHER FACTORS WERE UNKNOWN AND UNFORESEEABLE THAT HAVE ADVERSELY IMPACTED UBET TELECOM WHICH ARE RELATED TO THE PURCHASE OF THE US WEST EXCHANGES?

A: The Stipulation was signed July 6, 2000. After that date in 2001 the FCC issued some orders that had an impact on UBTA-UBET. One FCC order changes the rules to eliminate the prospects of rural telecommunications companies acquiring properties from Bell Operating Companies being eligible to receive Federal Universal Service Funds ("FUSF") for the high cost areas purchased. It is my understanding that prior areas in the state purchased from Qwest were eligible and do receive FUSF. UBET Telecom is not eligible and does not receive FUSF. UBET Telecom has high cost areas that it serves and none of it is eligible for FUSF. Prior to these orders, a rural exchange carrier could purchase exchanges and include the new costs in a single study area and be eligible for FUSF.

In addition, another FCC order changed the support mechanism for rural telephone companies from an implicit support to explicit support, and UBET Telecom was not eligible to receive these explicit support mechanisms. Obviously, there was significant federal regulatory activity which resulted in material changes in financial reporting requirements that took place during the period between signing the stipulation agreement and consummating the sale.

Q: WHO PERFORMED THE MEASUREMENT OF THE FAIR VALUE OF THE GOODWILL AND THE CORRESPONDING IMPAIRMENT?

A: Yeanopolos Drysdale Group, PLLC, has performed the measurement for years 2002, 2003, and 2004.

Q: WHAT WERE THE RESULTS OF THE MEASUREMENT OF THE FAIR VALUE OF GOODWILL?

A: The measurement for Fiscal Year ending December 31, 2002 an impairment was determined in the amount of

\$_____. This caused an increase in expenses in the amount of \$_____ and a corresponding loss to the company and reduction in equity. The impairment was recognized on the financial statements of UBET Telecom for the year ending December 31, 2002 by recording the impairment as a non-operating expense. For Fiscal year ending December 31, 2003 and December 31, 2004 it was determined the Fair Value exceeded the carrying amount of Goodwill and no impairment was recognized.

Q: IN MR. TODD'S DIRECT TESTIMONY HE STATES THAT THE COMPANIES' REQUEST FOR A PLANT ACQUISITION AND AMORTIZATION EXPENSE IS BASED, IN PART, ON A CHANGE IN THE ACCOUNTING TREATMENT FOR GOODWILL DUE TO FAS 142. WOULD YOU EXPLAIN WHAT THE CHANGE WAS AND HOW THE CHANGE IMPACTS UBTA-UBET?

A: As noted above, UBET Telecom's decision to acquire, and as part of its application for approval by the Commission for the acquisition of, the Vernal, Duchesne and Roosevelt exchanges, was based on its anticipated amortization of the Goodwill acquired in the exchange sales over 15 years. The problem was that the implementation of FAS 142, which requires a "write down" of goodwill which is reflected on the financial statements of the companies, resulted in a substantial decrease in the value of the assets carried on the financial statements of UBET Telecom. The acquisition of the exchange included a substantial amount of goodwill or "blue sky." As Mr. Todd testifies, the impairment of that goodwill, and resulting write down, has resulted in a negative equity position. As such, UBET Telecom no longer complies with its loan covenants with RUS and CoBank and the companies are technically in default of their respective loan covenants. As such, the ability of UBTA-UBET to borrow funds to meet the capital project demands for service required by UBTA-UBET's subscribers has been dramatically impacted.

Q: DOES THAT CONCLUDE YOUR TESTIMONY?

A: Yes.