

EXHIBIT 2

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of Manti Telephone Company's)
Application for Increased USF Eligibility) DOCKET NO. 13-046-01
) REPORT AND ORDER APPROVING
) SETTLEMENT STIPULATION
)

ISSUED: February 19, 2014

SYNOPSIS

By this order the Commission memorializes its bench order of February 10, 2014, approving the settlement stipulation. The Commission approves an annual Utah Universal Public Telecommunications Service Support Fund amount of \$950,000 for Manti Telephone Company.

BACKGROUND

On December 28, 2012, the Commission issued an order in Docket No. 08-046-01.¹ In that order, we raised concerns involving Manti Telephone Company's ("Manti" or the "Company") actions and decisions to modernize its network from copper to fiber, its relationship with its unregulated affiliates,² and its accounting practices and procedures. Based on the evidence and testimony presented by Manti, the Division of Public Utilities ("Division"), and the Office of Consumer Services ("Office"), the Commission ordered, in part, in the 08-046-01 docket that Manti was authorized to receive \$41,561 in Utah Universal Service Funds ("UUSF"), which necessitated a repayment of the excess interim UUSF received.³ Thereafter, we granted limited review solely to address Manti's UUSF repayment schedule.⁴ Subsequently, the parties

¹ See Confidential Report and Order (Docket No. 08-046-01), issued December 28, 2012.

² Manti's affiliates include Manti Tele Communications Company, Inc. ("MTCC") and P&C Rental, both of which included familial, ownership, and management also common to Manti.

³ See Confidential Report and Order (Docket No. 08-046-01) at 66.

⁴ See Order Granting Limited Review and Notice of Scheduling Conference (Docket No. 08-046-01), issued February 15, 2013.

filed a stipulation to stay the repayment until the conclusion of Manti's next general rate case,⁵ which Manti committed to file no later than December 31, 2013.⁶ The Commission approved the stipulation on June 17, 2013.⁷

On September 11, 2013, Manti filed its general rate case application and supporting documentation for an increase in UUSF eligibility of \$1,559,173, the subject of this docket.⁸ Manti filed its direct testimony on December 20, 2013.⁹ Parties then filed a settlement stipulation on January 28, 2014.¹⁰ At the request of the parties, the Commission suspended the remaining deadlines for written testimony and scheduled a hearing on the stipulation for February 10, 2014.¹¹ The proposed settlement stipulation provides for a total annual UUSF payment to Manti of \$950,000, or \$79,166.67 per month, beginning March 2014.¹² The parties further agree the proposed UUSF amount will be awarded retroactively effective from the date of the application (September 2013) due to the "unique circumstances of this case[.]"¹³ which have been further described as Manti's "current financial condition" and "precarious financial situation."¹⁴

On February 10, 2014, the Commission held a hearing at which parties were asked to provide testimony on whether the proposed settlement stipulation is just and reasonable

⁵ See Amended Stipulation Regarding Stay of USF Payback (Docket No. 08-046-01), filed June 3, 2013.

⁶ See Order Approving Settlement Stipulation (Docket No. 08-046-01) at 2, issued June 17, 2013.

⁷ See *id.*

⁸ See Confidential Application for Increase in USF Eligibility (Docket No. 13-046-01), filed September 11, 2013. A supplement to the application was also filed. See Confidential Supplement to Application for Increase in USF Eligibility, filed September 20, 2013.

⁹ See Confidential Direct Testimony of Dallas Cox; Confidential Direct Testimony of Tami Hansen; Direct Testimony of Curt Huttshell, PH.D.; and Confidential Direct Testimony of Kevin J. Kelly, filed December 20, 2013.

¹⁰ See Settlement Stipulation, filed January 28, 2014.

¹¹ See Notice of Hearing, issued January 29, 2014; and Notice of Suspension of Scheduling Order, and Notice of Public Witness Hearing, issued February 4, 2014.

¹² See Settlement Stipulation at 3, filed January 28, 2014.

¹³ *Id.* at 3, ¶7.

¹⁴ Transcript of Hearing, February 10, 2014, at 22; lines 21, 25.

in result, and in the public interest.¹⁵ Kira M. Slawson appeared on behalf of the Company along with Dallas Cox, general manager, and Tami Hansen, accounting manager. Justin Jetter represented the Division and was accompanied by William Duncan, telecom manager, and Bob Davies and Paul Hicken, utility analysts. Brent Coleman represented the Office and was accompanied by Cheryl Murray, utility analyst. Following the hearing in this matter, a public witness hearing was held and no one appeared. At the conclusion of the public witness hearing, the Commission issued a bench ruling approving the settlement stipulation.¹⁶ This order memorializes that ruling.

POSITIONS OF THE PARTIES

A. The Company

The Company testified it has implemented steps to address the accounting and operational deficiencies and corrections specified in the Commission's December 2012 order in Docket No. 08-046-01. The Company also testified it has worked with its lender to defer payment on the loan from Rural Telephone Finance Cooperative ("RTFC") to fund the fiber facilities; it has stipulated with the Division and the Office for a stay of the UUSF payback payments; and it has worked with its consultants, the Division, and the Office to address the accounting and operational issues, and has implemented changes suggested by those parties.

The Company testified it needed to install fiber to replace its deteriorating and outdated copper plant, and that the cost to use fiber was comparable to the cost of replacing the plant with new copper facilities. The Company further testified that fiber would allow the

¹⁵ See Notice of Hearing, issued January 29, 2014.

¹⁶ Transcript of Hearing, February 10, 2014, at 41; lines 1-15.

Company to provide advanced “state of the art” services and ensure that the Company’s network would not become “technologically obsolete” as it would with copper facilities.¹⁷

The Company provided the following summary of the changes it has implemented:

Briefly, we adopted a new increased rate for wholesale DSL services to compensate Manti Telephone Company for the use of its regulated network, over which retail broadband services are provisioned. The new rates that we implemented mirror the National Exchange Carrier Association’s cost-based DSL broadband tariff rate. We also implemented procedures to ensure that expenses charged by our non-regulated affiliate company, Manti Telecommunications Company, to Manti are based on the lower of either cost or market rate. And expenses charged by Manti to the non-regulated affiliate are based on the higher of cost or market rate.

We have identified the cost and market rates for expenses between the regulated and non-regulated companies and have developed a lease carrying charge that has been applied to intercompany expenses.

We implemented procedural changes to ensure that the regulated company is properly compensated by the non-regulated company for any use of Manti’s regulated employees, and that it properly compensates the non-regulated company if Manti Telephone uses the non-regulated employees.

We also allocated certain corporate and administrative expenses between the regulated and non-regulated companies, which includes an allocation of management costs. TCA has assisted us with developing an allocation factor to determine the appropriate amount of corporate and administrative overhead to include in the low-bid labor rate charge to the non-regulated affiliate.

In short, Manti has implemented all of the recommendations of TCA so that its operations reflect the proper and acceptable allocation between the regulated and the non-regulated companies as required by state and federal regulatory accounting and cost allocation rules consistent with industry practices.

¹⁷ Direct Testimony of Dallas Cox, filed December 20, 2013, at 14; lines 293-297, and 15; lines 298-301.

...

Manti continues to improve our work order system to track telephone plant under construction based on actual costs incurred. We have also modified our CPRs, or Continual Property Records, to better track our plant additions and rate [b]ase.¹⁸

In addition, the Company confirmed its accounting records used for the rate case are “completely separated” from tax records, which would include special tax treatment, including accelerated depreciation.¹⁹

The Company testified the stipulation is just and reasonable, and in the public interest.²⁰

B. The Division

The Division entered the following testimony in support of the stipulation. As evidence of the Company’s precarious financial circumstances in 2013, the Division testified:

In May of 2013, Manti entered into a three-month forbearance agreement with RTFC for a fixed amount of money to pay down principal and interest in lieu of their May obligation. In August, the Company was unable to make payments and asked for an amendment to the original forbearance in which an additional six months was granted, but required monthly payments of interest and principal.

As a result of deferred operating expenditure, OPEX, obligations in November--property tax--Manti was again unable to make the monthly payments asking for a third amendment to the original forbearance.

As a result of the forbearance agreement, Manti had to forfeit their common ownership stock, along with present and future patronage stock for RTFC. In reality, RTFC owns the company as a major shareholder.

¹⁸ Transcript of Hearing, February 10, 2014, at 11; lines 9-25, and 12; lines 1-16, 18-22.

¹⁹ Id. at 35; line 6.

²⁰ Id. at 16; lines 14-19.

The current state of the Company's cash flow without additional Utah Universal Service Funding, UUSF, despite its cost-cutting measures and revenue increases, does not and will not meet the needed cash working capital required to meet the principal and interest obligations to RTFC, let alone accrue the necessary OPEX for deferred liabilities occurring through the year.

Even with the changes implemented by Manti Telephone under the direction of its consultant, the DPU believes the financial health of the company to be timely and in peril. The DPU believes it is in the public interest to support the financial health of the Company by the reasonable settlements, as provided in the stipulation for this matter as outlined.²¹

The Division also provided the following testimony in support of the stipulation:

First, the annual amount of \$950,000 described in paragraphs 5 and 6 is within the reasonable range based upon the application of R746-360-8. Since the conclusion of Docket 08-046-01, Manti has made changes to their operations to bring it into compliance in alignment with other similar companies in Utah. Specifically, Manti no longer utilizes the local tariff to receive reimbursement from others that sell Manti [I]nternet services. Manti has now developed a master service agreement with rates that mirror the National Exchange Carrier Association tariff 5 for [I]nternet reimbursement. All other companies in Utah use the [National Exchange Carrier Association,] NECA[,] tariff to sell [I]nternet services to affiliates.

Manti has also implemented cost allocation procedures that are more closely aligned with the method used by other companies receiving Utah USF. These changes have taken place since the conclusion of Docket 08-046-01.

Therefore, the Division is now comfortable with evaluating this USF request using the same standards that have been applied to other similar companies.

Second, as to the lump sum payment described in paragraph 7, the Division believes this is reasonable due to the current financial condition of Manti as has been described by Division witness Bob Davis. At the conclusion of the 08-046-01 docket, Manti's USF distribution was decreased dramatically from what had been

²¹ Transcript of Hearing, February 10, 2014, at 19; lines 1-25, and 20; lines 1-3.

received previously. This has left Manti in a precarious financial situation.

At the present time, it is in arrears in principal payments to its lender, the Rural Telephone Finance Cooperative, by more than \$400,000. While there are alternative providers in the Manti area, Manti Telephone Company is the only provider that has Carrier of Last Resort obligations for the entire service area. In its current financial state, Manti could be in jeopardy of not being able to fulfill those obligations. One of the objectives of the Division [a]s found in Utah Code 54-4a-6(4)(a), says that we are to, “maintain the financial integrity of public utilities by assuring a sufficient and fair rate of return.” Without an initial influx of capital and sufficient monthly distributions to satisfy all obligations, Manti may be unable to remain as a going concern providing telephone service to the public in the communities of Ephraim, Manti and Sterling.

Third, concerning the obligation for payback of interim USF described in paragraph 8, the parties have agreed that as part of a comprehensive settlement that those obligations should be considered satisfied. This obligation was not ignored or taken lightly. Rather, it was fully considered as part of the negotiated agreement. The result of these negotiations is reflected in this stipulation.

Fourth, concerning paragraph 11, Manti has agreed to provide certain documents to the Division and the Office [concerning] the financial results of its affiliate, Manti Telecommunications Company, or MTCC, and transactions between the two companies for a three-year period. This will give the Division and the Office the ability to monitor the operational changes between the two companies and determine if these changes implemented by Manti during the past year are being continued.

In conclusion, the Division believes that the stipulation is just, reasonable in result, and in the public interest and requests the Commission approve the stipulation as presented.²²

C. The Office

The Office testified as follows in support of the settlement:

²² Id. at 22; lines 1-25, and 23; lines 1-25, and 24; lines 1-10.

The Office of Consumer Services represents residential and small commercial customers of public utilities. As such, we must review requests for USF disbursements from the perspective of the customers of the utility that will receive USF as well as from the perspective of the customers that are paying into the USF.

For this case, the Office contracted with the same expert consultants we used in the previous Manti case, Docket 08-046-01 to review Manti's filing and updated financial and other supporting data. The Office and our consultants reviewed the filing, the Company's testimony, submitted some data requests, and reviewed the responses to all data requests received to date. This initial review was sufficient for the Office to determine the categories of adjustments it would propose and a range of values for each category. However, the Office notes that due to the timing for testimony that was scheduled in this case, we engaged in settlement discussions prior to filing testimony of our own or submitting specific positions on the record.

The Office used the range of values for its intended adjustments to evaluate whether it could support settlement outcomes as being in the public interest. The Office notes that this settlement is being presented as an aggregate request for USF because each of the parties arrived at the outcome using a different set of adjustments and issues. We are here to speak in support of the settlement as being in the public interest.

In the Office's view, there were some general improvements in this filing over the prior filing. The Office and its consultants found the Company much more cooperative and forthcoming with information in this case, which facilitated a more accurate evaluation of their request. The Office commends the Company for the addition of a full-time, qualified accountant which has improved the accuracy and credibility regarding account and regulatory record keeping.

Some of the primary reasons for the Office's support of a higher USF disbursement at this time are Manti provided access to additional financial and operational data, which allowed a more precise and complete evaluation and calculation of the revenue requirement and shortfall. Increases in payroll costs consistent with the Commission's order in the prior case are reflected. It allows some recovery for income taxes as compared to the earlier case, in which the Office did not propose and the Commission did not allow recovery of income taxes.

In conclusion, the Office concurs that this settlement is just and reasonable in result and recommends Commission approval.²³

...

...We think that Manti has made significant progress. We expect that they will continue to make progress. And one of the reasons for getting the documentation that we will be receiving in this stipulation is so we can continue to monitor that and make sure that they maintain where they have come to and hopefully continue to make progress.²⁴

DISCUSSION, FINDINGS AND CONCLUSIONS

In our December 2012 order, we found the Company failed to justify its investment in fiber facilities as being prudent and necessary and, as a result, we made adjustments to the rate base accounts accordingly. A central question implicit in this docket is the rate base treatment of the cost of upgrading the network from copper to fiber facilities. In the normal course of business the Company repairs and replaces portions of its network on an ongoing basis. Current trends within the industry are to replace copper networks with more capable fiber networks. The Company's uncontested testimony in this docket is that it needed to install fiber to replace its deteriorating and outdated copper plant, and that the cost to use fiber was comparable to the cost of replacing the plant with new copper facilities. Further, the fiber network will allow the Company to provide advanced services and to receive substantial revenues resulting from broadband services offered by its unregulated affiliate using the fiber facilities. We note these revenues are consistent with the NECA tariff for use of such facilities, bringing the Company's practice in line with other rural carriers we regulate. Given these findings, we conclude the Company has satisfied our concerns that the upgrade was reasonable given the information it had at the time it made the decision to invest in the fiber upgrade.

²³ Transcript of Hearing, February 10, 2014, at 26; lines 1-25, and 27; lines 1-21.

²⁴ Id. at 30; lines 1-7.

Further, we find the Company has followed the principles contained in the 2012 order regarding removing obsolete copper from the rate base.

The 2012 order also identified concerns with the Company's operating policies and procedures. The evidence presented in the pre-filed direct testimony and testimony provided at hearing supports findings that Manti has adopted corrective operating procedures; has made appropriate adjustments to its depreciation, property, and other relevant accounts; and has implemented approved accounting practices and procedures that adequately address the operational concerns identified in our December 28, 2012, order. We note the stipulation requires Manti to provide audited financial statements for both Manti and MTCC for 2013-2015, which will allow the Division and Office to track whether Manti's policy and procedural changes are maintained. We find that UUSF support in the amount of \$950,000 per year is justified for Manti. Further, the parties have entered a stipulation for a UUSF amount below the requested amount in its application, which all parties testify is sufficient, just and reasonable in result, and in the public interest.

We also reiterate our statement at the conclusion of the hearing in this docket:

[W]e . . . recognize that there's significant exigency in this matter. We have determined that facts have been presented that are sufficient for us to find that the settlement is in the public interest. And we believe that there also has been information presented to the Commission upon which we can base conclusions of law that the settlement is consistent with pertinent laws and regulations.²⁵

²⁵ Transcript of Hearing, February 10, 2014, at 41; lines 3-10.

ORDER

Therefore, we approve the stipulation, filed January 28, 2014, and order:²⁶

1. Beginning calendar year 2015, Manti is authorized a total ongoing annual UUSF subsidy rate of \$950,000, to be paid in equal monthly installments.

2. Beginning March 2014, Manti is authorized a total of \$791,666.70 of UUSF subsidy, to be paid in equal monthly installments for the remainder of calendar year 2014.

3. Manti is also authorized a UUSF payment of \$475,000 to cover the period from Manti's application (September 2013) through February 2014 to be paid with Manti's March 2014 UUSF payment.

4. Manti is absolved of its obligation to repay UUSF funds, as ordered in Docket No. 08-046-01.

²⁶ As set forth by statute and as previously noted by the Commission in other orders, settlements of matters before the Commission are encouraged at any stage of the proceedings. See Utah Code Ann. § 54-7-1 (2010). See also In the Matter of the Notice of Rocky Mountain Power of Intent to File a General Rate Case, Docket No. 11-035-200 (Report and Order; Sept. 19, 2012), at 26; and In the Matter of the Application of Questar Gas Company to Adjust Rates for Natural Gas Service in Utah, Docket No. 04-057-04 (Report and Order; Jan. 6, 2006), at 26. The Commission may approve a settlement proposal after considering the interests of the public and other affected persons, if it finds the settlement proposal in the public interest. See Utah Code Ann. § 54-7-1(2)(a). See also Utah Dept. of Admin. Services v. Public Service Comm'n, 658 P.2d 601, 613-14 (Utah 1983).

DATED at Salt Lake City, Utah this 19th day of February, 2014.

/s/ Ron Allen, Chairman

/s/ David R. Clark, Commissioner

/s/ Thad LeVar, Commissioner

Attest:

/s/ Gary L. Widerburg
Commission Secretary
DW#251007

Notice of Opportunity for Agency Review or Rehearing

Pursuant to Utah Code Ann. §§ 63G-4-301 and 54-7-15, a party may seek agency review or rehearing of this order by filing a request for review or rehearing with the Commission within 30 days after the issuance of the order. Responses to a request for agency review or rehearing must be filed within 15 days of the filing of the request for review or rehearing. If the Commission fails to grant a request for review or rehearing within 20 days after the filing of a request for review or rehearing, it is deemed denied. Judicial review of the Commission's final agency action may be obtained by filing a Petition for Review with the Utah Supreme Court within 30 days after final agency action. Any Petition for Review must comply with the requirements of Utah Code Ann. §§ 63G-4-401, 63G-4-403, and the Utah Rules of Appellate Procedure.

CERTIFICATE OF SERVICE

I CERTIFY that on the 19th day of February, 2014, a true and correct copy of the foregoing was served upon the following as indicated below:

By Electronic Mail:

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