BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF CARBON/EMERY TELCOM, INC.'S APPLICATION FOR AN INCREASE IN UTAH UNIVERSAL SERVICE FUND SUPPORT	)	**Docket No. 15-2302-01**
Applicant	)	

REVISED REDACTED REBUTTAL TESTIMONY

OF

DARREN WOOLSEY

ON BEHALF OF CARBON/EMERY TELCOM, INC.

September 4, 2015
(Revised Per Commission Order October 26, 2015)

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1 **REBUTTAL TESTIMONY OF DARREN WOOLSEY**

2 **Q. What is your name?**

3 A. My name is Darren Woolsey.

4

5 **Q. By whom are you employed and in what capacity?**

6 A. I am employed by Carbon/Emery Telcom, Inc. as its Chief Financial Officer.

7

8 **Q. There are numerous references to various affiliated entities in the testimony,**
9 **can you please identify the affiliated entities and the abbreviations you will**
10 **use in this testimony to refer to each?**

11 A. Yes. The affiliated entities and the abbreviations I will use to refer to each are:

12 • Emery Telecommunications & Video, Inc. (ETV) provides internet, circuits,
13 fiber transport, VOIP voice, customer premise equipment, and retail
14 computer sales and service.

15 • Emery Telcom Video, LLC (ETV LLC) provides cable tv, cable internet, and
16 local advertising.

17

18 **Q. Have you previously provided Direct Testimony in this matter?**

19 A. Yes. With the filing of Carbon/Emery Telcom's Application for Increase in UUSF
20 on April 2, 2015 ("Application"), I filed direct testimony in support of the Application.
21 My testimony included Confidential Exhibits 1-14 (with subparts). I also provided
22 Supplemental Direct Testimony on April 24, 2015 to include the 2014 Audited

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23 Financial Statements, 2014 Journal Entries, and 2014 Audit Memorandum when
24 Carbon/Emery Telcom, Inc. received them from the auditors.
25
26 **Q. What is the purpose of your reply testimony?**
27 A. The purpose of my rebuttal testimony is to respond to the various testimonies filed
28 in this proceeding by the Division of Public Utilities (the "Division") and the Office
29 of Consumer Services ("Office"). In their testimonies, these parties propose
30 modifications to Carbon/Emery's Application for Increase in UUSF. In this
31 testimony, I recommend that the Commission modify or reject many of these
32 proposed modifications. Specifically, I will address the testimony of:
33 - William Duncan, Division of Public Utilities;
34 - Joseph Hellewell, Division of Public Utilities;
35 - Bion C. Ostrander, Office of Consumer Services; and
36 - David Brevitz, Office of Consumer Services.
37 **Q. Have you reviewed the testimony of the individuals you have identified**
38 **above?**
39 A. Yes.
40
41 **Q. Please identify the exhibits to your testimony.**
42 A. I am attaching the following Confidential Exhibits:
43 - Carbon/Emery Rebuttal Testimony of Woolsey - Cable Internet Migration -
44 Exhibit 1

45 • Carbon/Emery Rebuttal Testimony of Woolsey - A&G Allocator Analysis -
46 Exhibit 2
47 • Carbon/Emery Rebuttal Testimony of Woolsey - CSR Allocation - Exhibit 3
48 • Carbon/Emery Rebuttal Testimony of Woolsey - Depreciation - Exhibit 4
49

50 **Q. Could you please summarize your reply testimony?**

51 A. My testimony will focus on the particular adjustments that the Division of Public
52 Utilities and the Office of Consumer Services are recommending in the testimonies
53 filed on their behalf. Specifically, I will address:

54 ▪ Adjustment BCO-2: Allocate Corporate Overhead Expenses from Carbon to
55 ETV/Nonregulated Affiliates
56
57 ▪ Adjustment BCO-3: Remove Prepayments from Rate Base
58
59 ▪ Adjustment BCO-4: Deduct Long-Term Liabilities from Rate Base
60
61 ▪ Adjustment BCO-5: Remove 50% of telephone plant under construction
62 (TPUC) from Rate Base
63
64 ▪ Adjustment BCO-6: Remove 50% of materials & supplies ("M&S") from Rate
65 Base
66 ▪ Adjustment BCO-7: Reverse Carbon's Projected Access Line Reduction
67 ▪ Adjustment BCO-8: Remove Depreciation on Fully Depreciated Assets
68 ▪ Division of Public Utilities' adjustment on Depreciation
69 ▪ Adjustment BCO-9: Adjust Income Tax Expense and Reflect Interest
70 Synchronization
71

72 **Q. What else will you address in this rebuttal testimony?**

73 A. Carbon/Emery Telcom is proposing four adjustments to the UUSF request
74 contained in the initial filing which I will discuss in detail below. However, by way
75 of summary, the four adjustments are:

76 - A decrease in the three year land line loss projection to reflect actual land
77 line losses experienced through August 1, 2015. This adjustment reduces
78 Carbon's UUSF request by [REDACTED].
79 - An increase in revenue resulting from anticipated additional fiber to the
80 home (FTTH) customers. This adjustment is [REDACTED] increase in
81 revenue. This adjustment reduces Carbon's UUSF request by [REDACTED].
82 - An adjustment to the amount of revenue requirement recognized by
83 Carbon/Emery Telcom (Carbon) for interstate special access services
84 referred to as "DSL revenue requirement". This adjustment accounts for
85 DSL revenue requirement reflecting the 2014 Interstate Cost Study filed in
86 July 2015, which was not available at the time of the initial filing. Carbon's
87 portion of this adjustment resulted in an increase of revenue in the amount
88 of [REDACTED] resulting in a decrease in the UUSF request.
89 - An adjustment related to long term liabilities in the amount of [REDACTED]
90 with a corresponding UUSF impact of [REDACTED] (10.5001% Carbon filed
91 rate of return).

92 As indicated, I discuss these adjustments in detail below, the combination of the
93 four proposed adjustments would result in a decrease of [REDACTED] from

94 Carbon's initial Application filing (-$[REDACTED] - $[REDACTED] + [REDACTED] - [REDACTED] =
95 -$[REDACTED] plus the tax reduction effect on these adjustments of -$[REDACTED].
96
97 **Q. Do you agree with Mr. Ostrander that UUSF proceedings warrant rigorous**
98 **analysis and oversight?**
99 A. Carbon/Emery Telcom consistently files annual reports with the Division of
100 Telecommunications and receives review and oversight. Furthermore, Carbon has
101 not filed for increased rates but has filed for an increase in distribution out of the
102 UUSF. Also, the Division and Office reviewed Emery Telcom and Carbon/Emery
103 Telcom in a similar proceeding in 2014. Mr. Ostrander's testimony discredits the
104 purpose of Universal Service by stating that no direct or measurable benefit
105 accrues to citizens in areas not receiving UUSF funding. The very concept of
106 Universal Service inherently recognizes the value of providing affordable service
107 to higher cost rural areas and connecting urban Americans to their rural
108 counterparts. Citizens in urban areas pay into the UUSF for the ability to call
109 citizens who live in high cost rural areas. Universal service benefits both urban
110 and rural customers and the Office of Consumer Services represents both urban
111 and rural consumers and is mandated to assess the impact of regulatory action on
112 all residential consumers and small businesses (both urban and rural). All
113 telephone customers pay into the UUSF. The desire to minimize the payments
114 into the UUSF should not outweigh the proper use of the funds to further the public
115 interest of providing service (including advanced services) to rural end user phone

116 customers and special access (small commercial) customers. Additionally, it is
117 critical to remember that carriers who receive UUSF funding also have carrier of
118 last resort and E911 obligations. Ubiquitous service in Carbon's area would not be
119 possible without federal and state universal service support.
120
121
122 ~~**Q. In his testimony on behalf of the Office of Consumer Services ("Office"), Mr.**~~
123 ~~**Ostrander proposes two significant adjustments related to what Mr.**~~
124 ~~**Ostrander perceives as "allocation problems" between Carbon and its non-**~~
125 ~~**regulated affiliates. Mr. Ostrander identifies those adjustments as BCO-1**~~
126 ~~**(allocate fiber/internet-related common costs from Carbon to its non-**~~
127 ~~**regulated affiliates) and BCO-2 (allocate corporate overhead expenses from**~~
128 ~~**Carbon to non-regulated affiliates). Does your testimony address both of**~~
129 ~~**these adjustments?**~~
130 ~~A. No. Douglas Meredith addresses adjustment BCO-1 which purports to allocate~~
131 ~~fiber/internet related common costs from Carbon to its non-regulated affiliates.~~
132
133 **Q. Are you familiar with the Office's adjustment BCO-2 which purports to**
134 **allocate corporate overhead expenses from Carbon to non-regulated**
135 **affiliates?**

136 A. Yes. Mr. Ostrander proposes a modification of Carbon's A&G Allocation factor. In
137 Carbon's Application, Carbon applied an A&G Allocation factor of ███%[1] to
138 regulated operations and ███% to non-regulated operations. The A&G allocator
139 is used for several departments including CEO, Board of Directors and Public
140 Relations/Marketing (PR/MK). Mr. Ostrander proposes a change of the A&G
141 Allocation Factor to ███%/███% for CEO and Board of Directors and ███ reg
142 ███ non-reg for PR/MK.
143
144 **Q. Do you agree with this proposed adjustment?**
145 A. No. As I detail below, Carbon's allocation factors are accurate and no adjustment
146 is needed. Mr. Ostrander's analysis is cursory and flawed. Mr. Ostrander states
147 that Carbon has inappropriately used allocators to overstate regulated allocated
148 expenses and understate non-regulated allocated expenses. However, much of
149 the analysis performed by Mr. Ostrander and included in his testimony in lines 738
150 to 779 was based on unconfirmed and inaccurate assumptions, and the data used
151 to perform many of the calculations was incorrect. This erroneous data was then
152 used to justify a proposal to change the CEO and Board allocations to 50% reg
153 50% non-reg.
154

[1] In Table BCO-2 in Mr. Ostrander's testimony he correctly identifies the A&G Allocation Factor as ██%/██% regulated to non-regulated. However, in Table BCO-4, and on line 711 of Mr. Ostrander's testimony, Mr. Ostrander incorrectly identifies the A&G Allocation Factors as ██%/██% regulated/non-regulated.

155 **Q. Please explain.**

156 A. It is Mr. Ostrander's opinion that costs have been shifted from non-regulated
157 entities to the regulated entities. To support this opinion, Mr. Ostrander examined
158 the Consolidated Financial Statements and "other information" which is not
159 identified in Mr. Ostrander's testimony. The Office found that "certain financial data,
160 allocations, and changes in amounts from year to year appear unusual or appear
161 to favor the non-regulated affiliates," and concluded without explanation that "this
162 type of information lends support for my adjustment to reallocate some expenses
163 from regulated to non-regulated operations."

164

165 **Q Do you know what financial data, allocations, and changes in amounts from**
166 **year to year appeared unusual to Mr. Ostrander?**

167 A. The Office referred to the net income for the regulated companies, and found that
168 the net income for the regulated companies decreased from [REDACTED] to [REDACTED] from
169 2013 to 2014. However, these numbers are incorrect. Review of the Consolidated
170 Financial Statements shows that the correct numbers regarding the regulated
171 companies' net income are [REDACTED] and [REDACTED] for 2013 and 2014 respectively,
172 evidencing a reduction of regulated net income of [REDACTED] not [REDACTED] as stated
173 by Mr. Ostrander.

174

175 **Q. Were you able to determine where Mr. Ostrander's regulated net income**
176 **numbers came from?**

177 A. No, I was not, but I can explain the reduction in regulated net income, and clarify
178 why Carbon needs additional UUSF support. The decrease in regulated net
179 income was almost entirely recorded on the books of Emery Telcom (not Carbon)
180 as demonstrated below:
181
182 [CONFIDENTIAL TABLE REDACTED]
183 Source: 2013-14 audited financial statements as provided to the Office and DPU
184
185 As shown in the table above, the net income of Emery declined by ██████. The
186 decrease is not the result of shifting costs, as inferred by Mr. Ostrander, but
187 primarily the result of lost revenue of ████ and to a lesser extent the investment
188 in FTTH resulting in increased depreciation of ████. The largest revenue
189 decrease was due to a federally dictated loss of reciprocal compensation revenue
190 associated with CAF-ICC reform ██████. Other state access revenues declined
191 by ██████, primarily as a result of this same CAF-ICC reform. Local service
192 revenues declined by ██████ due to declining local service customers. Billing
193 and collection revenue declined by ██████ as described in Emery's response to
194 DPU 4 2.2. Other revenue declines amounted to ██████. Emery Telcom did
195 experience some expense increases. Depreciation increased by ██████ as a
196 result of increased investment. All other expenses however only increased by
197 ██████. This accounts for the change in net income of ██████ on Emery
198 Telcom. The ██████ increase in all expenses excluding depreciation does not

199 support the offices premise that costs were shifted from the non-regulated entities
200 to the regulated entities.
201 The majority of the regulated decline in revenue highlighted by Mr. Ostrander was
202 due to revenue decreases on Emery. Carbon did evidence a smaller reduction in
203 net income of [REDACTED] from 2013 to 2014 demonstrated in the chart below:
204
205 [CONFIDENTIAL TABLE REDACTED]
206
207 Source: 2013-14 audited financial statements as provided to the Office and DPU.
208
209 This chart illustrates that Carbon actually had some revenue gain (special access
210 less a partial offset from land line loss), and that the loss in net income was largely
211 due to additional depreciation associated with recent and ongoing plant additions.
212
213 **Q. So did expenses shift from the non-regulated companies to the regulated**
214 **companies?**
215 A. No. Expenses did not shift from non-regulated companies as suggested by Mr.
216 Ostrander. In fact, as shown, Carbon's "other expenses" only increased [REDACTED]
217 from [REDACTED] to [REDACTED].
218
219 **Q. What conclusions do you draw from a review of the net income numbers?**
220 A. The conclusions to be drawn from a top level financial analysis are as follows:

221

222 • there is no shift in allocated costs from the non-regulated entities

223 • actual non-depreciation expenses did not change significantly in Carbon or

224 Emery

225 • the decline in the net income of Carbon/Emery Telcom was not the result of

226 inappropriately allocating expenses in 2014, but rather it illustrates

227 consistency between the two years.

228

229 **Q. Did Mr. Ostrander's use of inaccurate numbers for regulated net income**

230 **affect his analysis?**

231 A. While I find it difficult to follow Mr. Ostrander's analysis, if his conclusion is that

232 "changes from year to year appear unusual", the "unusual" appearance could be

233 a result of his use of inaccurate numbers. In my opinion, the inaccurate numbers

234 and shallow analysis used by Mr. Ostrander make the analysis meaningless and

235 the conclusions reached unsupportable.

236

237 **Q. Why?**

238 A. The analysis is meaningless because Mr. Ostrander starts with inaccurate

239 numbers on regulated net income and these incorrect numbers flow through the

240 analysis causing Mr. Ostrander to incorrectly calculate the regulated companies'

241 profit margin. He then compares the inaccurate profit margin of the regulated

242 companies to his calculated profit margin on the non-regulated affiliates, which Mr.

243 Ostrander uses (in some unascertainable way) to support his adjustment to
244 reallocate "some expenses" between regulated and non-regulated operations. A
245 slightly deeper analysis than that performed by Mr. Ostrander, as discussed above,
246 evidences the reasons for the noted changes and shows why this course is not
247 supportable.
248
249 **Q. Are the regulated companies net income and profit margins the only**
250 **numbers Mr. Ostrander has stated incorrectly in his analysis?**
251 A. No. Mr. Ostrander identifies the ETV net income change from 2013 to 2014 as
252 [REDACTED]. The actual decrease in net income was [REDACTED]. Additionally, while
253 Mr. Ostrander correctly states the ETV net income in 2014 as [REDACTED], he misstates
254 ETV's percentage of total consolidated profit of [REDACTED]%. Mr. Ostrander then
255 discusses expenses where he highlights an increase in RLEC expense of [REDACTED]
256 (the operating expense increase is actually only [REDACTED]) and implies that this
257 increase in regulated expenses corresponds to a similar decrease in ETV
258 expenses of the same amount of [REDACTED] (Operating expense decrease was actually
259 [REDACTED]). The implication in Mr. Ostrander's testimony is that somehow this is
260 related to a shift of costs from non-regulated to regulated operations. This is
261 misleading due to the errors in the numbers. However, the increase in cost was a
262 result of increased amortization and depreciation, which are the result of company
263 specific plant investments. The remaining actual costs evidence only a slight
264 increase in regulated costs of [REDACTED] and a slight decrease in non-regulated

265 costs of ██████. Accounting for the change in DSL wholesale handling
266 (discussed below), non-regulated operating expense actually went up by ██████
267 which does not support Mr. Ostrander's conclusion.
268
269 **Q. What actually caused the decreases in ETV expenses and revenue?**
270 A. The decline in both revenue and expenses in ETV related to a change in
271 accounting for the DSL wholesale revenue charged by the regulated company to
272 the non-regulated company which occurred when our new billing system was
273 implemented in the fall of 2013. The new billing method avoids showing the
274 revenue and matching expense in separate accounts on ETV and just moves the
275 revenue to the regulated companies where it ultimately ends up under the old or
276 new method. This change resulted in a ██████ decrease in ETV revenue and
277 corresponding expense in 2014. The remaining decrease in ETV revenue is
278 related to a decrease of DSL subscribers (ETV) as they moved to higher speed
279 Cable Internet (ETV LLC) between 2013 and 2014. This revenue shift can easily
280 be viewed in the trial balances of the two non-regulated companies.
281
282 **Q. Did the Office have the trial balances of the two companies?**
283 A. Yes. The Office had the trial balances of the two companies, the General Ledger
284 of all companies and the consolidated financial statements with consolidating
285 information from 2012 to 2014. However, in the testimony of Mr. Ostrander, he
286 states "it is possible that the decrease in ETV's expense of ███ and the

287 corresponding increase in regulated RLEC expenses of ███ was the result of a
288 favorable shift of allocated expense from non-regulated operations to regulated
289 operations, but that cannot be confirmed." The reality, however, is that the GL
290 detail and allocation detail for both years were provided to the Office, and the Office
291 could have confirmed that the decreases in non-regulated expenses did NOT
292 result from a favorable shift of allocated expenses to regulated operations. But Mr.
293 Ostrander either did not perform this analysis or did not like the results. Rather,
294 he relied on supposition and unsupported assumptions to justify a reduction in the
295 allocation factor from ███% regulated to ███% regulated.
296
297 **Q. Was there anything else in Mr. Ostrander's testimony related to his assertion**
298 **that Carbon overstates its regulated allocated expenses and understates its**
299 **non-regulated allocated expenses that troubled you?**
300 A. Yes. Mr. Ostrander suggests that because ETV has profit, it can readily absorb his
301 allocation adjustments. This seems to imply that ability to pay is a proper cost
302 allocation factor. This position is not reasonable; it is not supported by analysis;
303 and it should be rejected by the Commission. It is unreasonable to have profitability
304 drive allocations or adjustments.
305
306 **Q. Do you find it unusual that the company does not have any allocation factors**
307 **that allocate 50% or more of expenses to nonregulated operations?**

308 **A.** No. Because the company direct codes many costs, not all of the costs are subject
309 to an allocation factor. Additionally, I am very familiar with the drivers that were
310 used to develop the allocators. With a proper understanding and examination of
311 the cost drivers, and analysis of the company's direct coding to ensure the non-
312 regulated companies are not favored, the allocators are very reasonable. However
313 neither my subjective opinion, nor anyone else's, should be considered support for
314 a cost allocation. Rather, any cost allocation factor or method should be supported
315 by data, which Mr. Ostrander failed to provide. Carbon has provided that data in
316 response to various data requests to support its allocation factors.
317
318 **Q. Mr. Ostrander suggests that total revenue and expenses can be used to**
319 **determine the appropriate allocation factors. Do you believe the total**
320 **revenue and expenses are rational drivers of costs?**
321 **A.** No. Revenue could be an appropriate standard to use to allocate costs if a
322 company had homogenous products. For example, if the consolidated entity of
323 Carbon/Emery Telcom consisted solely of Emery Telcom, Carbon Emery Telcom,
324 and Hanksville Telcom offering similar products at similar prices, then revenue
325 could be used without significant distortion (see possible exception noted below).
326 However when a consolidated entity offers non-homogenous services, such as
327 cable television, broadband internet, long haul transport, and newsprint, as in the
328 case of the consolidated entities of Carbon/Emery Telcom, revenue is an illogical
329 basis to use when developing cost allocations.

330

331 **Q. Please explain why revenues are not a rational driver of costs.**

332 **A.** As an example, consider this UUSF proceeding. Carbon/Emery Telcom is
333 requesting an additional [REDACTED] in UUSF funding. If Carbon is successful and
334 receives this additional revenue, a cost allocation based on revenue would result
335 in increased expenses going to Carbon Emery Telcom. At first this may seem
336 rational because a large amount of expenses were incurred to go through this
337 process (although those costs are not likely to continue). However, let's now
338 assume that Carbon incurs these same expenses and Carbon/Emery Telcom's
339 current USF of [REDACTED] is reduced to 0, as is being proposed by Mr. Ostrander.
340 A cost allocation based on revenue would then result in a reduction of cost to
341 Carbon/Emery Telcom. It is inappropriate to assume that the dollar result of a
342 UUSF proceeding should determine cost allocations. The fact that a UUSF case is
343 undertaken could be considered a reason for direct coding or maybe even a
344 temporary driver, but the result of the UUSF case should not be.

345

346 A second example is special access transport revenue earned from a route
347 provided significantly across ETV leased fibers from Grand Junction CO to Salt
348 Lake City, Utah. This route generates revenue with only a handful of customers
349 and related billing and compliance issues. The lease also provides for
350 maintenance, thus ETV is not allowed to work or manage work on the fibers under
351 such lease. As a result, this fiber generates revenue with no significant

352 management attention, billing complexity, compliance, or customer service. If
353 overhead costs were allocated on revenue ETV would receive an inappropriately
354 high level of costs unsupported by actual management time based on the revenue
355 from this route.
356
357 Similarly, but to a lesser extent, internet revenue generated by internet customers
358 on ETV and ETV LLC are much easier to manage as a one or two line item billing
359 compared to a phone customer with franchise fees, excise tax, sales tax, E911,
360 subscriber line charges, ARC charges, poison control, EAS, local service, call
361 features, universal service fees, and the associated billing and compliance
362 associated with all of these billing line items. These examples highlight the
363 inappropriateness of revenue as a cost driver. This example also begins to show
364 why the billing records are reflective of associated management time in managing
365 the complexity of regulated operations including compliance, regulatory changes,
366 proceedings, and oversight of CSR and administrative employees.
367
368 **Q. Do you believe expenses are a rational driver of costs?**
369 A. No. Expenses are not a rational driver of costs.
370
371 **Q. Why not?**
372 A. There are significant direct coded expenses that have no relationship to the
373 amount of time spent by the CEO, Board, Marketing/PR, or CSR's. One of the

374 best examples that illustrates the problem with using expense as a substitute for a
375 substantive cost driver can be seen with the expenses of Emery Telcom Video LLC
376 (ETV LLC). The single largest expense category on the non-regulated entities is
377 Cable TV programming costs in ETV LLC. These costs totaled [REDACTED] for 2014
378 (activity 73 in account 7962.61 in previously provided GL detail). This cost alone
379 is similar to [REDACTED], yet programming and negotiation is handled through
380 ETV LLC's association with the National Cable Television Cooperative (NCTC)
381 leaving very little management time related to cable TV programming. If expenses
382 were used as an allocation basis, significant costs would be inappropriately
383 allocated to ETV LLC. It simply is not logical that a random programming cost
384 increase would result in additional CEO cost allocation. There is no reasonable
385 correlation.
386
387 **Q. Do the "billing record" inputs to the company's A&G allocation factor have**
388 **a "direct" or "cost-causative" relationship to the expenses in the department**
389 **cost pool that they are used to allocate?**
390 A. Yes. Billing records are representative because they are representative of the -
391 types of services, number of customers, complexity of regulatory compliance, and
392 issues that the CEO/Board, and Marketing represent. Forward looking plans are
393 extensions of or improvements to the existing services and have focused primarily
394 of regulated issues since 2011 when CAF/ICC reform was implemented and
395 continues today with ACAM model based support proposals being considered by

396 the FCC. Billing records also reflect forward looking CEO plans board decisions,
397 and marketing efforts as these efforts can be measured in resulting customer
398 growth in new and existing areas. Extension of plant to new customers and areas
399 is also reflected in the billing records on a slight lag. This allocator is updated
400 frequently.
401
402 **Q. What is your assessment of the revised A&G allocator calculation performed**
403 **by Mr. Ostrander?**
404 A. Carbon/Emery Telcom is not opposed to the idea of considering other cost
405 causative drivers in addition to billing records to maintain the accounting and
406 general allocator. As was pointed out by Mr. Ostrander, drivers in addition to billing
407 records have been used by Carbon/Emery Telcom in the past. However, I do not
408 agree with all of the Offices proposed drivers, or its methodology in considering
409 those drivers.
410
411 **Q Which of the proposed drivers suggested by Mr. Ostrander to you reject?**
412 A. I reject the use of "Revenue" and "Expenses" as cost allocators. For the reasons I
413 discussed above "Revenue" and "Expenses" are not at all appropriate to use to
414 develop allocations.
415
416 **Q. Do you agree that Plant can be used as an input for developing cost**
417 **allocators?**

418 A. Yes. Carbon/Emery Telcom could consider Plant as a possible cost driver to
419 determine the accounting and general allocator. If "plant" were to be used, "Gross
420 Plant" would be a better indicator than "Net Plant" because the regulated entities
421 use group asset depreciation per FCC part 32 whereas the non-regulated entities
422 use single asset straight line depreciation. Because group asset depreciation has
423 had an accelerated effect on the regulated entities, use of net plant as an indicator
424 for cost allocation would result in an artificially low allocation to the regulated
425 entities to the extent of the accelerated depreciation.
426
427 Also, when using Plant as a proposed driver, shared assets need to properly
428 accounted for and shown on the books of the correct entity based upon allocation
429 of that asset, not ownership. As indicated in Carbon's Application, to reduce
430 duplication of equipment and costs, the Carbon/Emery Telcom entities share
431 certain equipment, vehicles, and computers. This shared equipment is recorded
432 on the books of ETV. This cost of this shared equipment is then allocated to the
433 various related party entities based upon usage or other allocators. The shared
434 equipment is presented and discussed in the initial filing as Exhibit 7b – Shared
435 Assets and this exhibit was used as the basis for a rate base adjustment to include
436 the appropriate portion of shared equipment in the rate base of Carbon. Therefore,
437 an allocator based upon plant would need to reflect the portion allocated to each
438 entity to prevent the overstatement of assets on ETV and related understatement

439 on each of the other Carbon/Emery related entities. Mr. Ostrander's analysis of
440 plant as a driver does not take these issues into consideration.
441
442 **Q. Are there other inputs that Carbon agrees are appropriate?**
443 A. Yes. Carbon believes that records and payroll can also be valuable inputs in
444 determining the appropriate A&G Allocation factor.
445
446 **Q. Has the Office employed the proper methodology for considering these**
447 **allocation inputs?**
448 A. No. The calculation performed by Mr. Ostrander in "Confid. 15-2302-01 - Ostr. WP
449 1.3 - Adj. BCO-2 (OCS DR 2-40 CAM Alloc.).xlsx" uses an equal weighting of the
450 various dollar types and records. This method skews the allocation to the highest
451 dollars (revenue and net plant totaling ████████) and essentially gives no weight
452 to billing records (█████████). A more reasonable approach is to assume that
453 each of the drivers, if representative, should be given equal weighting. This can
454 be easily accomplished by taking the average of the resulting allocation
455 percentages of each appropriately identified driver.
456
457 **Q. Have you recalculated the Accounting and General Allocator using**
458 **additional inputs as suggested by Mr. Ostrander?**
459 A. Yes. Carbon recalculated the A&G Allocator using Gross Plant (properly adjusted
460 for shared assets), Monthly Records, and Payroll, and then weighted each

461 associated allocation percent equally. This produced essentially the same
462 allocation as was used by Carbon in the initial application ███% Emery (ET),
463 ███% Carbon/Emery (CT) and ███% Hanksville (HT) (74.42% total to regulated
464 entities) as opposed to ███% ET, ███% CT, and ███% HT (███% total to
465 regulated entities). This calculation can be viewed in Carbon/Emery Rebuttal
466 Testimony of Woolsey – A&G Allocator Analysis - Exhibit 2.xlsx.
467
468 Although the revised allocation would result in slightly greater expenses being
469 allocated to the regulated entities (███%), because of the insignificance of the
470 increase, I am of the opinion that the base year is representative and no adjustment
471 is necessary.
472
473 **Q. The Office proposed a different basis for Public Relations/Marketing**
474 **allocations. Do you agree with the proposed adjustment?**
475 A. No. Mr. Ostrander's proposed PR/MK adjustment premise is that because there
476 are three services and the one regulated service should be then allocated 33% of
477 the cost; he then randomly decides 25%. Neither the 33% or the 25% is backed
478 by substantive support. The three services considered by Mr. Ostrander were
479 IPTV, Internet, and Phone. The affiliated companies of Emery do not offer IPTV
480 but do offer Cable TV.
481 When considering how to allocate costs for marketing, if certain services are not
482 advertised at all they should get little or no allocation of costs, conversely if a

483 particular service appears more frequently it should receive an increased
484 allocation. With this in mind, only considering the number of services offered, is
485 over simplistic as it does not consider the focus or frequency of marketing efforts
486 of these services. If services are specifically non-regulated and do not contain
487 phone advertising they are direct coded as is the case with Moab advertising which
488 is all direct coded to non-regulated entities and reduces the actual amount of
489 PR/MK subject to the allocator. In the regulated operating areas, phone receives
490 a primary focus either directly or through bundles. Due to decreased interest in
491 land lines, the advertising of bundles is critical to the success and survival of
492 Carbon. Bundles in the regulated operating areas are designed to be Phone and
493 "something else" either LD, cable, internet provided over regulated plant, or
494 internet provided over non-regulated plant. Whenever a bundle is advertised and
495 sold the regulated entity benefits. This benefit is enhanced by the sale of long-
496 distance or DSL which are tied to the regulated entity due to the requirement to
497 have a land line or to allocate additional loop cost (DSL revenue requirement) for
498 standalone DSL. Thus, the actual sales (and advertising) of LD, DSL, and Bundles
499 in general, benefit the regulated entity and cost should reflect this.
500
501 As of December 31, 2015, nearly ████ of the customers in the Carbon serving
502 area are phone customers (████ phone vs ████ (internet and cable). Of the
503 internet customers ████ were DSL making them also regulated customers (ETV
504 purchases wholesale DSL special access service from Carbon). The number of

505 Carbon serving area customers being serviced by regulated plant is ████ or
506 ████%.
507
508 In the absence of a more appropriate allocation basis, the current use of the A&G
509 allocator by Carbon for PR/MK is reflective of the results of marketing efforts and
510 is comparable to the customers being served by regulated vs non-regulated plant.
511
512 **Q. In addition to the A&G Allocation change and PR/MK Adjustment, the Office**
513 **is proposing an adjustment to the CSR Allocator. Do you agree with the**
514 **proposed adjustment?**
515 A. No. Mr. Ostrander's proposed CSR adjustment contains a variety of errors.
516
517 **Q. What errors are contained in the CSR adjustment being proposed by the**
518 **Office?**
519 A. Mr. Ostrander states that the CSR allocator should be adjusted from ███%
520 regulated and ███% non-regulated to ███% regulated and ███% non-regulated.
521 However, Mr. Ostrander has not provided any data or evidence to support this
522 conclusion. There is no evidence that Mr. Ostrander's opinion of how CSR costs
523 should be allocated is more accurate than the time study performed by Carbon in
524 2010. In fact, it would appear that Mr. Ostrander did not verify any of his findings
525 related to CSR's in the Office data requests, and as a result, Mr. Ostrander made
526 several errors in his testimony related to the CSR Allocation factor.

527

528 **Q. Please identify the errors you are referring to.**

529 A. In Mr. Ostrander's calculation of CSR costs he uses [redacted] total CSR dollars
530 as a basis for allocating 2014 CSR costs, the correct amount of total CSR costs is
531 [redacted] which results in a 35% misstatement upfront and makes any resulting
532 proposed adjustment wrong. This data is a subset of total allocations given to the
533 Office in DR 2-40. Carbon has utilized an Excel pivot table to summarize the data
534 and demonstrate the error, see Carbon Emery Rebuttal Testimony of Woolsey –
535 CSR Allocation - Exhibit 3.xlsx. The error was limited to this one data point. From
536 the pivot table you can see that total expenses subject to allocation tie to Mr.
537 Ostrander's analysis showing [redacted] in total allocated expenses. The highlighted
538 green numbers on Carbon Emery Rebuttal Testimony of Woolsey – CSR
539 Allocation - Exhibit 3.xlsx also tie to amounts shown for Board, CEO,
540 Marketing/PR, and Human Resources. The CSR allocation amount does not tie
541 and should have been [redacted].

542

543 Mr. Ostrander states that there are [redacted] CSR's per DPU 1-4(b), then goes on to
544 state that "It is not clear why [redacted]%, or a substantial majority of these CSR costs
545 would be allocated to regulated operations". DPU 1-4(b) does not indicate that
546 [redacted]% of CSR costs were allocated to the regulated entities. It does however
547 clearly demonstrate that there were [redacted] different CSR's between January 31,
548 2012 and April 1, 2015. Mr. Ostrander failed however to notice that there were also

549 ███ additional "CSR/Advanced Trouble Shooting" employees making ███ total
550 CSR's that worked in any given month over the 40 month period presented. His
551 count does not consider turnover, part-time, or temporary employment. Mr.
552 Ostrander also failed to notice that there was a table at the bottom of this data
553 request that clearly demonstrates the number of employed employees in any given
554 month. The summary is presented below with highlights for the base year and a
555 summary at the bottom of the sheet:
556
557
558 [CONFIDENTIAL TABLE REDACTED]
559
560
561 Source: DPU DR 1-4b Emery & Carbon - Employee List.xlsx (highlights and summary of
562 CSR counts below data added)
563
564 **Q. Please explain this data.**
565 A. Though there were a total of ███ total different employees employed during the
566 40 month period the number employed in any given month was never more than
567 ███. The average number of CSR's during the base period was ███ From this
568 ███ an adjustment needs to be made for part-time employees to arrive at full time
569 equivalents. There are ███ part-time employees, so a reduction of ███
570 employees brings the FTE employee count average to ███

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571

572 **Q. Do all of the ███ FTE CSR employees use the CSR allocator for their primary**
573 **coding?**

574 A. No. Out of the ███ FTE employees there are ███ dispatch CSR's that primarily
575 use the dispatch allocator which more closely follows plant labor. There are also
576 ███ CSRs included in the advanced trouble shooting CSR group and ███ Moab
577 CSR who's coding is all to non-regulated entities (ETV and ETV LLC). This
578 essentially lowers the actual number of CSR's using the CSR allocator for their
579 primary coding to ███

580

581 **Q. What other changes have you made with respect to CSRs?**

582 A. In conjunction with the establishment of the troubleshooting group, additional
583 plant troubleshooting software tools were given to the CSR group to diagnose
584 initial trouble calls. If a CSR determined that the trouble is not isolated to the
585 outside plant, the call is passed to the advanced trouble shooting group. This
586 greatly reduces the amount of time the CSR's spend with non-regulated
587 customers. These changes were made as DSL and Cable internet customers
588 increased, and despite the increased number of customers, the additional tools
589 and cooperation between advanced troubleshooting has allowed customers to be
590 served without requiring a significant increase in CSRs. The CSRs' actual time
591 can be reviewed with a Pivot table on DPU DR1-4a Emery & Carbon- Labor
592 Reports – testimony analysis.xlsx the pivot reveals the following:

593
594
595
596 [CONFIDENTIAL TABLE REDACTED]
597
598
599 Source: Carbon Response to DPU DR 1-4a Emery & Carbon-Labor Reports – testimony
600 analysis.xlsx
601
602 **Q. What does the Pivot table show?**
603 A. The Pivot table reflects the final disposition of all CSR Labor and shows use of
604 CSR, Dispatch, Directory, and Moab CSR distributions as well as direct coding.
605 The results indicate that more CSR time is actually coded to the non-regulated
606 entities than the regulated entities (█% non-reg vs █% regulated). As the
607 current actual coding is highly non-regulated and combines the proper use of direct
608 coding and representative allocators based on real cost drivers, the hypothetical
609 allocator proposed by Mr. Ostrander is not appropriate and is wholly without basis.
610
611 **Q. The Office is proposing several adjustments to your rate base accounts.**
612 **How did you determine the rate base accounts used in Carbon's**
613 **Application?**

614 A. Carbon/Emery Telcom relied on pages 17 and 18 of the Incumbent Local
615 Exchange Carrier Annual Report to the Public Service Commission of Utah
616 (Annual Report) for guidance in determining appropriate rate base accounts.
617 Carbon's Annual Report for the period January 1, 2014 to December 31, 2014 was
618 submitted to the PSC and has been provided to the Office and DPU. Page 17 of
619 the Annual Report lists the net telecommunications plant in service by account.
620 Page 18 is entitled "Other Rate Base Accounts" and includes a listing of accounts
621 typically considered as part of the rate base. A snap shot of Carbon's 2014 report
622 is shown below as an example of the included accounts:

623 [CONFIDENTIAL EXCEPRT FROM ANNUAL REPORT REDACTED]

624

625

626 Generally the asset accounts listed in the Annual Report are added to the rate
627 base and certain liability accounts are deducted from the rate base. Carbon
628 included these accounts in the Rate Base in its Application as has been the
629 practice in the previous proceedings before the PSC. Carbon has not departed
630 from the accounts prescribed by the Utah PSC in their Annual Report nor changed
631 the common practice with respect to rate case or UUSF filings.

632

633

634 **Q. Mr. Ostrander has identified 4 adjustments to rate base including**
635 **Prepayments (BCO-3), Long-Term Liabilities (BCO-4), Telephone Plant**

636 **Under Construction (BCO-5), and Materials and Supplies (BCO-6). Do you**
637 **agree with any of these adjustments?**
638 A. Yes, one. I believe that deducting the Long-Term Liabilities from Rate Base (BCO-
639 4) is appropriate. Carbon originally did not consider the deduction of a post
640 retirement benefit obligation because it was not specifically identified as a liability
641 account on the PSC report. Upon examination of the nature of this account as well
642 as the handling for interstate purposes as noted by Mr. Ostrander, I agree that a
643 reduction from rate base should be made. I do not, however, agree with Mr.
644 Ostrander's Part 36 value used for this adjustment. The Long-Term liability
645 represents post-retirement health care related obligations and is appropriately
646 removed from rate base because the company has already recovered the expense
647 that created the liability in prior years. However, the total liability needs to be
648 reduced by:
649 • the portion created through non-income statement adjustments (other
650 comprehensive income); and
651 • the portion that was allocated to other non-regulated entities.
652 Considering these adjustments, [REDACTED] is the amount that should remain on
653 Emery, Carbon, Hanksville. Only Carbon's portion, in the amount of [REDACTED],
654 should be deducted from Carbon's rate base. This amount differs slightly from the
655 Part 36 amount identified by Mr. Ostrander due to the adjustments for other
656 comprehensive income mentioned above.
657

658 **Q. Do you agree with BCO-3 related to prepayments?**

659 A. No. I reject the appropriateness BCO-3. The inclusion of prepaid expenses is
660 straight forward and allowed by practice. This policy should not be changed.
661

662 **Q. Do you agree that telephone plant under construction (TPUC) should be**
663 **excluded from rate base (BCO-5)?**

664 A. No. With respect to the adjustment BCO-5, Mr. Ostrander seeks to remove 50%
665 of TPUC in the amount of [REDACTED] and provides two reasons for its exclusion.
666 The first is his opinion that a normalized basis of TPUC would result in a lower and
667 more appropriate TPUC value. Though normalization conveniently reduces
668 TPUC, it does not recognize that these are actual capital expenditures, that TPUC
669 is directly tied to plant investment, and that a lower TPUC just means the assets
670 have moved to another rate base account (plant in service) or have not occurred
671 yet. Carbon is not proposing known and measurable plant additions in TPUC.
672 Rather, Carbon is only including actual plant expenditures which currently reside
673 in TPUC. This is not an account that should be normalized to find an “appropriate”
674 operating level. This account by its very nature accurately reflects actual plant
675 expenditures.
676

677 **Q. What is the second reason that Mr. Ostrander gives for removing 50% of**
678 **TPUC?**

679 A. Mr. Ostrander also suggests that we should consider the "matching principle"
680 which is a GAAP principle not a "regulatory" principle. Matching attempts to align
681 the financial impact of actual events to the periods in which they occur. As
682 examples:
683 - a retail sale should match corresponding reductions in inventory and
684 recognition of cost of goods sold in the same period;
685 - expensing of a prepaid should be ratably over the periods of benefit;
686 - in the case of assets, they are not depreciated until they are placed in
687 service;
688 - likewise existing assets that new assets are to replace are not reduced on
689 the books until they incur an impairment or are actually taken out of service.
690 Mr. Ostrander's strange interpretation of mismatching does not provide adequate
691 basis for adjustment; by suggesting that Carbon should somehow project an offset
692 to the inclusion of TPUC of events that have not occurred. With respect to capital
693 expenditures I have never heard of projecting future revenues, affiliate
694 transactions, or disposals related to an asset addition that have not yet occurred
695 under the theory of matching. This would in fact be a violation of both the matching
696 principle which requires a transaction to be recorded in a correct period and also
697 a violation of a second GAAP principle which prevents the recognition of contingent
698 gains. Mr. Ostrander's arguments on removing 50% of TPUC should be rejected.
699

700 **Q. Do you agree with the Offices' proposed adjustment for Materials and**
701 **Supplies contained in BCO-6?**
702 A. No. In BCO-6, Mr. Ostrander has proposed a reduction in materials and supplies
703 to a "normalized" lower level arguing that the current level is artificially high. While
704 the current level of materials and supplies on site is higher than historical levels,
705 the higher level is real, on site, and necessary due to several factors:
706 - Carbon is experiencing increased construction activity associated
707 with the FTTH curb and business district in Price;
708 - Carbon's lead time on fiber and fiber related products has increased.
709 Carbon is currently experiencing delivery delays of three to six
710 months.
711 - As a result of the increase lead times with vendors, Carbon is
712 required to keep more inventory on hand to prevent shortages, and
713 work stoppages that will result if required fiber and fiber facilities are
714 not on site.
715 The increased level of inventory is anticipated for at least the next five years and
716 is properly reflected in the rate base at full value.
717
718 **Q. The Office is proposing a depreciation adjustment on assets that the Office**
719 **believes are either fully depreciated or will be fully depreciated in about 2**
720 **years (BCO-8). Do you agree with this depreciation adjustment?**

721 A. No. Mr. Ostrander refers to his adjustment of BCO-8 as "remove depreciation
722 expense on fully depreciated assets". Carbon has not depreciated any asset in
723 excess of the book value of the asset. We assume that what Mr. Ostrander is
724 attempting to describe is the effect of group asset depreciation. As indicated in the
725 testimony of Douglas Meredith, group asset depreciation is an FCC prescribed
726 method of depreciation which can have an accelerating effect on depreciation in
727 cases where there are older assets included in the group subject to a depreciation
728 calculation. However, group asset depreciation only accelerates depreciation; it
729 does not result in over-depreciation (depreciation in excess of the book value) of
730 any asset.
731

732 **Q. What errors has Mr. Ostrander made in his depreciation adjustment**
733 **contained in BCO-8?**

734 A. Mr. Ostrander's BCO-8 claims to reduce "depreciation expense by ████ (and
735 corresponding increase in accumulated depreciation in rate base of ████ on
736 assets that are either fully depreciated or [sic] will be fully depreciated within about
737 ██ years." Mr. Ostrander provides no rationale for his recommendation to
738 exclude depreciation expense in the amounts ████ for Other Work Equipment
739 and ████ for Interexchange Circuit Equipment. He states that these accounts
740 became fully depreciated in 2014 so he just excludes the entire amount. This
741 position assumes no continuing investment which would result in the continuation
742 of depreciation. Continued investment is anticipated since the company is a going

743 concern, and I assert that the depreciation levels projected in the base year are
744 representative of expected levels for at least the next five years based upon this
745 investment.
746
747 **Q. Are there other accounts that Mr. Ostrander adjusted besides "Other Work**
748 **Equipment" and "Interexchange Circuit Equipment"?**
749 A. Yes. Mr. Ostrander concludes that the deprecation in accounts for Subscriber
750 Circuit Equipment and Aerial Cable is currently overstated and that it will largely
751 disappear in four years [REDACTED] years for the accounts subject to his adjustment).
752 This position again erroneously assumes no continued investment and no
753 disposals. Additionally, there is no determination whether the current depreciation
754 level of the chosen account groups is materially accelerated or is a representative
755 amount. A summary of data for the two targeted adjustment accounts is as follows:
756 [CONFIDENTIAL TABLE REDACTED]
757
758 Source: From Confid. - 15-2302-01 Ostr. WP 1.8 - Adj. BCO-8 - DPU 1-11 Deprec.
759 Exp.xlsx – tab Dep Calc. and FCC 481 filing.
760
761 **Q. What does the above table show with regard to Subscriber Circuit**
762 **Equipment?**
763 A. The first targeted account, Subscriber Circuit Equipment [REDACTED], with a GBV and
764 NBV of [REDACTED] and [REDACTED] respectively and a depreciation life of [REDACTED] years is

765 completely appropriate at its current depreciation level. The Subscriber Circuit
766 Equipment Account consists largely of legacy DSLAM type equipment which will
767 be replaced by FTTH network interface device equipment beginning in earnest in
768 2017. Taking the Gross Book Value (GBV) of [REDACTED] and dividing it by the asset
769 life of [REDACTED] years results in [REDACTED] of depreciation expense per year, which
770 evidences little acceleration from the current year actual depreciation at [REDACTED]
771 Because the legacy equipment is being disposed and replaced in the same year
772 the old equipment will be fully depreciated the current level of depreciation is
773 appropriate. This also shows that depreciation will remain very similar to current
774 levels in the short run, but will actually increase after five years based upon the
775 projected five year investment. The adjustment proposed by Mr. Ostrander is
776 entirely inappropriate.
777
778 [CONFIDENTIAL TABLE REDACTED]
779 Source: FCC 481
780
781 **Q. What does the above table show with regard to the Aerial Cable Account?**
782 A. With respect to the Aerial Cable, Carbon anticipates fixed asset additions to this
783 category of [REDACTED] over the next two years which will more than outpace the
784 depreciation expense levels currently projected by Mr. Ostrander in the five year
785 period. Though depreciation will not drop as projected by Mr. Ostrander, the
786 acceleration effect is present in the Aerial Cable account and can be maintained

787 near current levels if disposals of the older assets at levels similar to additions are
788 made. Carbon's current use of group asset depreciation does not result in an
789 inappropriate base level of depreciation, and (based upon anticipated additions
790 and disposals) future depreciation levels will not differ significantly from the current
791 2014 base year levels. A more appropriate and encompassing discussion of
792 depreciation methodology, potential acceleration, and both the expense and rate
793 base implications of changing the methodology is included in the Rebuttal
794 Testimony of D Meredith filed in this Docket.
795
796 **Q. Describe how Carbon calculates depreciation expense.**
797 A. Carbon calculates depreciation expense using a straight line calculation in
798 conformity with a group plan of accounting as prescribed by Federal
799 Communications Commission (FCC) in the Code of Federal Regulations, Title 47,
800 Chapter I, Subchapter B, Part 32. FCC part 32.2000 which states "(iii) Charges for
801 currently accruing depreciation shall be made monthly to the appropriate
802 depreciation accounts, and corresponding credits shall be made to the appropriate
803 depreciation reserve accounts. Current monthly charges shall normally be
804 computed by the application of one-twelfth of the annual depreciation rate to the
805 monthly average balance of the associated category of plant."
806
807 "Group plan" is defined as follows in FCC Part 32.9000; "Group plan, as applied to
808 depreciation accounting, means the plan under which depreciation charges are

809 accrued upon the basis of the original cost of all property included in each
810 depreciable plant account, using the average service life thereof properly
811 weighted, and upon the retirement of any depreciable property its cost is charged
812 to the depreciation reserve whether or not the particular item has attained the
813 average service life."
814
815 **Q. Does a group asset plan calculation of depreciation expense result in higher**
816 **depreciation?**
817 A. No. Using a group asset method to Calculate depreciation expense will always
818 result in the same total depreciation expense as calculated under any other
819 accepted method. Group asset depreciation is an accelerated depreciation
820 method. This means that group asset depreciation tends to produce a higher
821 depreciation expense in earlier years, and a lower depreciation expense in later
822 years. Conversely the rate base (NBV of associated assets subject to
823 depreciation) will be reduced more quickly resulting in a lower total disbursement
824 of UUSF based upon applying a rate of return on a lower NBV and over a shorter
825 (accelerated) asset life.
826
827 **Q. Is group asset an acceptable method of depreciation?**
828 A. Yes. Group asset depreciation is an acceptable method of depreciation that is
829 used for, and approved by the FCC. Carbon/Emery Telcom is using an accepted
830 methodology in the calculation of depreciation in accordance with the guidance

831 provided by the FCC, consistent with Carbon's historical practice, and consistent
832 with the method of depreciation used by many other rural ILEC's in the State of
833 Utah.
834
835 In the absence of rulemaking at the state level dictating the method of depreciation
836 to be employed by rural telecommunication providers in the State of Utah, group
837 asset depreciation should continue to be allowed by the Commission. Carbon's
838 base year depreciation calculated using the group asset method is not abnormally
839 high and is consistent with anticipated investment levels and should not be
840 modified.
841
842 **Q. Mr. Hellewell from the Division of Public Utilities proposed an adjustment of**
843 **[redacted] to reduce depreciation expense. Can you speak to the**
844 **appropriateness of this proposed adjustment?**
845 A. The calculation is essentially a "worst of both worlds" approach to applying what
846 otherwise would be an acceptable depreciation methodology if consistently and
847 historically implemented.
848
849 Depreciation effects rate of return calculations in two ways: first by the depreciation
850 expense recorded in any given period; and second by the allowed rate of return
851 applied to the NBV of these associated assets. In addition to these two
852 components there are two sources of potential return – State and Federal. These

853 two jurisdictions as well as the methodology have to be closely examined when
854 any change is considered to ensure proper jurisdictional return (no loss of recovery
855 or double recovery).
856
857 **Q. How did the DPU calculate its depreciation adjustment?**
858 A. The DPU's proposed depreciation adjustment was calculated by applying single
859 asset straight line depreciation to individual asset detail provided in DPU DR1-11
860 Emery & Carbon – Assets and CY 2014 Depreciation.xlsx. Carbon recalculated
861 the DPU's single asset adjustment to within reasonable rounding differences of
862 ███, and has supplied our calculation in Carbon Emery Rebuttal Testimony of
863 Woolsey–Depreciation-Exhibit 4.xlsx. This exhibit also contains additional
864 calculations which will be discussed latter.
865
866 **Q. Are there issues with the DPU's proposed adjustment?**
867 A. Yes. The DPU proposed adjustment provides single asset straight line
868 depreciation as if had occurred from the in-service date through 2014, then
869 compared the 2014 recalculated expense to the expense recorded by Carbon to
870 arrive at a difference of ███████. The DPU methodology which resulted in lower
871 depreciation expense was applied to all depreciable assets (not just intrastate
872 assets). This ignores the fact that Carbon in fact used a higher depreciation
873 expense amount in its interstate filings upon which rate of return will be established
874 for interstate recovery mechanisms. On the associated rate base side of the

875 depreciation transaction, the DPU used the NBV which reflects the accelerated
876 group asset methodology (lower) then added back only the current year
877 depreciation difference of [REDACTED] as a proposed adjustment to NBV. Thus the
878 "worst of both worlds" occurred where the lowest possible NBV was used for rate
879 base and the lowest possible depreciation calculation (single asset straight line)
880 was used for expense.
881
882 **Q. Couldn't you just adjust the NBV to reflect historical application of the single**
883 **asset straight line depreciation proposed by the state to arrive at the correct**
884 **amount of return on rate base associated with their proposed adjustment?**
885 A. No. Because recovery of both depreciation expense and return on rate base has
886 already been received on the interstate portion of these assets in prior years. Any
887 calculation by the state would have to consider this effect.
888
889 **Q. How would you address the DPU's concern regarding depreciation**
890 **methodology?**
891 A. The preferred course of action, which results in an overall lower total UUSF
892 distribution (as discussed in testimony provided by Douglas Meredith), would be
893 to allow companies to continue to use group asset depreciation as an acceptable
894 methodology as prescribed by the FCC. This would not preclude other companies
895 from using a different methodology it would just be one of the acceptable methods
896 of calculation.

897

898 As an alternative, if the State feels strongly about a particular methodology for
899 calculating depreciation and wishes to establish rules regarding this, the best
900 approach would be to avoid the complications and recovery concerns of retroactive
901 application and apply the new methodology going forward on new asset
902 investments. If a company chooses to not follow the State methodology at that
903 point then they would be subject to reconciling and adjusting their books for state
904 rate making purposes as necessary.

905

906 **Q. If single asset straight line methodology was prescribed by the State and**
907 **adopted by Carbon on a go-forward basis, how would depreciation expense**
908 **compare to the base year**?

909 A. I performed an analysis of the effects of making a prospective change to single
910 asset straight line depreciation as of January 1, 2014. In this analysis, Carbon
911 assumed that group asset depreciation would continue on historical assets as of
912 12/31/13, and single asset straight line methodology would apply to all 2014
913 additions and projected additions through 2019. For purposes of this analysis
914 Carbon used the projected capital improvements filed July 1, 2015 on FCC Form
915 481. From these assumptions, the analysis provided the following results:

916 • 2014 depreciation expense would have reduced by [REDACTED] from [REDACTED]
917 to [REDACTED] in the 2014 base year.

918 • The six year average depreciation expense is projected at [REDACTED] which is
919 [REDACTED] (4.3%) lower than the base year.
920 • The base year is materially representative of anticipated depreciation
921 expense levels as projected in this change scenario.
922 See Carbon Emery Rebuttal Testimony of Woolsey - Dep Est Single Asset 2014
923 to 2019 - Exhibit 5.xlsx
924
925 **Q. Is there another solution?**
926 A. The last solution would be an attempt to apply the DPU methodology in a way that
927 considers all aspects of the proposed change including depreciation expense, rate
928 base (NBV), and jurisdiction. Carbon has performed this calculation which is
929 included in Carbon Emery Rebuttal Testimony of Woolsey – Depreciation -Exhibit
930 4.xlsx. In this Exhibit Carbon starts by recalculating individual asset depreciation
931 using the single asset straight line method through 12/31/2013. This allows the
932 NBV at the beginning of the rate base period to be presented. 2014 depreciation
933 expense is then calculated in the same manner, and a resulting NBV for
934 12/31/2014 is calculated. These numbers are then totaled to see the current 2014
935 depreciation effect and cumulative NBV effect of the proposed depreciation
936 change. (See summary in rows 2531 to 2541 on the Carbon tab of the
937 spreadsheet). The depreciation change is calculated at [REDACTED] essentially the
938 same as the DPU calculation of [REDACTED]. In this section you can also see the
939 effect of adding back the cumulative NBV difference on rate base, which would

940 result in a UUSF impact of [REDACTED] (using 10.50001% Carbon rate of return).
941 Carbon has already described the fault of using this calculation as a NBV/rate base
942 adjustment because it does not consider interstate return previously received on
943 these asset differences. The next step in the calculation is contained in rows 2543
944 to 2553 in which the two methodologies are applied to the asset mix with the group
945 methodology applied to interstate assets and the single asset methodology applied
946 to the intrastate assets. This results in a 2014 depreciation reduction adjustment
947 of [REDACTED] and a corresponding rate base/NBV increase adjustment of
948 [REDACTED] with an estimated corresponding UUSF impact of [REDACTED]. The net
949 decrease in the UUSF request resulting from this theoretically correct analysis
950 would be $[REDACTED] ($-[REDACTED] + [REDACTED].
951
952 **Q. Are there any downsides to the mixed calculation performed above?**
953 A. Yes. The intrastate/interstate mix of assets can and does change over time
954 making this calculation slightly inaccurate at any given point in time. Also, any
955 change from existing methodology (unless the books could be restated) will cause
956 differences in federal and state reporting that would not be easily tracked and
957 would result in less transparency from a reporting standpoint.
958
959
960 Again the best course of action is the choice of an acceptable methodology that is
961 then applied consistently over a single asset or group asset life for both interstate

962 and intrastate rate of return recovery. In the absence of agreement on
963 methodology by all parties in this proceeding, the focus should be on whether the
964 amount presented in the initial filing is a representative base year amount. I assert
965 that the base year amount is materially representative whether Carbon continues
966 to use the group method, or if a change to single asset straight line methodology
967 were made as of the beginning of the 2014 base year.
968
969
970 **Q. Mr. Hellewell describes six reasons why group asset depreciation is not**
971 **recommended. What is your response?**
972 A: I will address each of the six reasons:
973 - Depreciation by computer: The ease of calculation was not a determining
974 factor in the original choice of Carbon to use group asset depreciation. In
975 fact until our recent system upgrade, Carbon's accounting system would not
976 handle the group calculation.
977 - Asset Tracking: This argument is not really an issue for Carbon because
978 individual assets are tracked. Only our oldest assets are an issue (think
979 Qwest acquisition). Either method could be deployed with adequate
980 tracking.
981 - Disposal: With appropriate individual tracking the methodology has no
982 impact on disposals.

983 • Group Characteristics: The problem of classification exists in either method
984 of depreciation. Vehicles are not necessarily a problem as they are easily
985 identified and generally disposed at or near their depreciable life thus
986 reducing any possible group depreciation effect.
987 • Standardization: I do not disagree with Mr. Hellewell's general statement
988 here but would argue that we are among a majority of companies that use
989 group asset depreciation.
990 • Volatility: I agree that volatility risk is increased under a group methodology.
991 However this risk is mitigated through proper and timely disposals and
992 balanced continued investment as needed for aging assets.
993
994 **Q. Previously you indicated that Carbon is proposing a revenue adjustment to**
995 **account for the impacts of converting non-regulated cable customers to**
996 **regulated fiber internet customer. Can you tell us what the financial**
997 **statement impacts of this conversion are?**
998 A. This type of migration has two major financial statement impacts. First, there would
999 be a shift in the various components of interstate revenue requirement, and second
1000 there would be an increase in rate base from the additional plant required to make
1001 the conversion. We contacted Moss Adams, LLP, the CPA firm contracted to
1002 produce our annual Cost Study, to do a sensitivity analysis of what would have
1003 happened to our 2014 cost study assuming that all of our December 31, 2014 cable
1004 internet customers in the Carbon ILEC service area had been converted to fiber

1005 internet as of year-end. The following chart summarizes the results of the Moss
1006 Adams Sensitivity Analysis which was performed at our company's cost study area
1007 level (includes Emery, Carbon/Emery, and Hanksville which operates in the
1008 boundary of SAC 502278):
1009
1010 [CONFIDENTIAL TABLE REDACTED]
1011 Source: Carbon Emery Rebuttal Testimony of Woolsey - Cable Internet Migration
1012 - Exhibit 1.xlsx
1013
1014 This analysis shows that the combined effects of the migration of cable internet
1015 customers to fiber internet would have a per customer UUSF impact of
1016 ($██████) per month. In order to make an adjustment to this UUSF proceeding,
1017 Carbon used a three year anticipated conversion average (similar to land line loss)
1018 in which the ██████ remaining cable internet customers in Carbon are
1019 converted to fiber, as projected in 2015 through 2017, with a resulting projected
1020 base year adjustment impact of ██████. Carbon presented this adjustment
1021 along with an updated calculation of the USF impact of landline loss covering the
1022 same period. The summary above and adjustments below are included in Carbon
1023 Emery Rebuttal Testimony of Woolsey - Cable Internet Migration - Exhibit 1.xlsx
1024
1025 [CONFIDENTIAL TABLE REDACTED]

1026 Source: Carbon Emery Rebuttal Testimony of Woolsey - Cable Internet Migration
1027 - Exhibit 1.xlsx
1028
1029 **Q. You also previously referred to a land line loss adjustment. Please explain.**
1030 A. The land line loss projection utilizes the same methodology used in the initial filing
1031 which incorporated a three projection of loss for business and residential
1032 customers and the application of current service rates for basic service. The initial
1033 filing for Carbon utilized 2013 and 2014 actual historical loss to project the loss
1034 forward to create a three year average. The Office rejected this adjustment, and in
1035 BCO-7 suggests that the land line loss projection should not be included as a
1036 decrease in revenue.
1037
1038 **Q. Do you agree with the Office's adjustment for land line loss in BCO-7?**
1039 A. No. It is not appropriate to completely eliminate the land line loss projection.
1040 However, actual land line losses through 8/1/2015 were less than the projection in
1041 the initial filing resulting in an increase in revenue in the amount of [REDACTED], with
1042 a corresponding decrease in the UUSF request of [REDACTED]. Carbon's proposed
1043 adjustment accurately reflects the positive effects of lower than anticipated land
1044 line loss, and is a more appropriate adjustment than the Office's BCO-7
1045 adjustment.
1046

1047 **Q. Is the adjustment made by Mr. Ostrander to adjust income taxes as a**
1048 **reflection of interest synchronization appropriate?**
1049 A. It is not appropriate.
1050
1051 **Q. Why isn't it appropriate?**
1052 A. With respect to the appropriateness of interest synchronization, I reject the
1053 assertion that this methodology is "common" or appropriate in cases of
1054 hypothetical capital structure. I am not aware of such an adjustment being adopted
1055 in current or historical Utah telecommunications proceedings or any FCC
1056 proceeding. I am also unaware of any such adjustment proposed or in practice in
1057 the traditional FCC rate making/cost study separation processes. The use of a
1058 hypothetical rate structure already penalizes Carbon to the extent the cost of debt
1059 is less than the cost of equity applied to any hypothetical capital structure of debt
1060 percent greater than its actual 0% debt. Effectively Carbon has been forced from
1061 actual capital structure to a lower rate of return hypothetical capital structure then,
1062 begrudging the already lower rate of return on debt, Mr. Ostrander proposes to
1063 take the return "hypothetically" lower again by adjusting for tax deductions that do
1064 not exist. The adjustment is not based upon Carbon's actual capital structure or
1065 tax deductibility. It has no precedence or place in this proceeding. If we are fully
1066 considering a hypothetical debt scenario, the very real result of hypothetical debt
1067 should be considered. In the case of Carbon debt would not be used to reduce
1068 equity, but rather the only reason Carbon would incur additional debt is to

1069 accelerate capital projects thus increasing rate base assets. Carbon has not
1070 projected hypothetical assets or even been aggressive in projecting "known and
1071 measurable" asset additions that have occurred to date in 2015. If all hypothetical
1072 consequences of a debt imputation are honestly considered then the positive
1073 effects of the scenario should be among them.
1074
1075 **Q. If you assume that interest synchronization is appropriate, has Mr. Ostrander**
1076 **calculated it correctly?**
1077 A. No. It was incorrectly calculated by Mr. Ostrander.
1078
1079 **Q. In what ways?**
1080 A. Mr. Ostrander applied a theoretical imputation of interest related to rate base
1081 assets, and then calculated a tax impact of this interest amount of [REDACTED]. In
1082 this calculation he used an incorrect state rate of [REDACTED] (Exh.1D,A-11 Ostr. Tab from
1083 Master – OCS Exhibit 2D – 15-2032-01 Ostrander Rev.Req.xlsx) vs the correct
1084 Utah rate of 5%. ~~Then after specifically calculating this as a "tax effect" of~~
1085 ~~XXXXXX, he includes this amount (see line 12 included in - XXXXXX) in his~~
1086 ~~summary at column "D" of the Exh.1D-2, A-1 Ostr. Tab of Master – OCS Exhibit~~
1087 ~~2D – 15-2032-01 Ostrander Rev.Req.xlsx, and proceeds to inappropriately gross~~
1088 ~~the tax back up by XXXXXX to XXXXXX (included in line 16 – XXXXXX). He~~ Mr.
1089 Ostrander also uses a slightly incorrect tax gross up calculation. The correct gross

1090 up can be accurately represented by the unrounded formula [REDACTED] or rounded
1091 to [REDACTED].
1092
1093
1094 **Q. Have you calculated what the correct interest synchronization would be?**
1095 A. I am reluctant to provide the calculation because I don't think it is an
1096 appropriate adjustment. However, the correct numerical adjustment is not difficult
1097 to calculate. The correct UUSF/Tax amount, if we agreed with the adjustment in
1098 theory, would be [REDACTED] not the [REDACTED] calculated by Mr. Ostrander. I also
1099 disagree with the [REDACTED] debt to equity hypothetical capital structure that is
1100 factored into Mr. Ostrander calculation. If Carbon's actual capital structure were
1101 used this adjustment disappears, and if [REDACTED] debt is used the resulting calculation
1102 would only be [REDACTED]
1103
1104 **Q. In the Division of Public Utilities Calculation of Rate of Return, what is the**
1105 **appropriate input for the interstate rate?**
1106 A. As Mr. Coleman accurately states "The question of which rate to use is really a
1107 matter of whether Carbon participates in the Common Line Pool, or the smaller
1108 subset of companies that participate in both NECA's Common Line and Traffic
1109 Sensitive pools." Mr. Coleman states that he confirmed with Mr. Brandon Gardner,
1110 NECA Western Region Manager, that Carbon is not a Common Line Pool
1111 participant.

1112

1113 **Q. Is Carbon a Common Line Pool participant?**

1114 A. Yes.

1115

1116 **Q. Do you know how Mr. Coleman got this inaccurate information from Mr.**
1117 **Brandon Gardner of NECA?**

1118 A. Carbon/Emery Telcom is one of three ILECS reporting under Cost Study Area
1119 Code "502278 – Emery Consolidated" (together with Emery Telephone and
1120 Hanksville Telcom, Inc.). It is more typical for one ILEC to have multiple study
1121 areas than it is for one study area to have multiple ILEC's. On September 4, 2015
1122 I spoke with Mr. Brandon Gardner, who indicated that he had a follow-up call with
1123 Casey Coleman and that he had clarified the inclusion of Carbon in the Emery
1124 consolidated filing and the participation of Carbon in NECA's Common Line Pool.
1125 With this clarified understanding, it is appropriate to use 11.45% per the September
1126 30, 2014 FCC Form 492 filed by NECA as the interstate input when calculating
1127 allowed rate of return. Mr. Douglas Meredith will discuss this in more detail in his
1128 testimony.

1129

1130 **Q. Did you review the Testimony and curriculum vitae of Bion C. Ostrander?**

1131 A. Yes. Mr. Ostrander in his testimony and his curriculum vitae indicates he has
1132 maintained an uninterrupted permit to practice as a Certified Public Accountant
1133 ("CPA") in the State of Kansas since 1990. However, Mr. Ostrander footnotes

1134 this statement indicating that his permit to practice is pending renewal subject to
1135 meeting professional education hour requirements in Kansas. I reviewed the
1136 Kansas Board of Accountancy's website and database and determined that Mr.
1137 Ostrander has not held a permit to practice as a CPA in Kansas since June 30,
1138 2014.
1139
1140 **Q. Does this lapse in Mr. Ostrander's permit to practice concern you?**
1141 A. Yes. As a CPA myself, I am familiar with the rules regarding the profession.
1142 Kansas is a two-tiered state for CPA's. This means before practicing as a CPA
1143 or holding oneself out as a CPA, the individual must have a certificate of public
1144 accountancy and a permit to practice. Without meeting both requirements, an
1145 individual is not permitted to practice as a CPA in Kansas, or hold oneself out as
1146 a CPA.
1147
1148 **Q. Do you know if Mr. Ostrander is required to be a CPA to provide testimony**
1149 **in this case?**
1150 A. To my knowledge, Mr. Ostrander is not required to be a CPA to provide
1151 testimony in this case, but the fact that he held himself out as a CPA "for
1152 credential" purposes when he does not hold this credential is troubling to me as a
1153 certified public accountant. I believe this is unprofessional conduct and speaks
1154 to Mr. Ostrander's credibility as an expert witness.
1155

1156 **Q. To summarize, what is Carbon's current UUSF request?**

1157 A. $570,643. This amount reflects the effect of the five adjustments (and associated

1158 tax effect) discussed herein. This amount accurately represents the amount that

1159 Carbon is entitled to under Utah law.

1160

1161 **Q. Finally, are there any other adjustments that you have for your filing?**

1162 A: Yes. As is customary, legal and consulting fees are disbursed from the state USF

1163 on a lump sum basis after the proceeding is resolved. I won't know this amount

1164 until after the proceeding but wanted to include these items as a placeholder for

1165 resolution by the Commission.

1166

1167 **Q. Does this conclude your testimony?**

1168 A. Yes.