

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE)	Docket No. 15-2302-01
APPLICATION OF)	
CARBON/EMERY TELECOM INC.)	Hearing
FOR AN INCREASE IN UTAH)	
UNIVERSAL SERVICE FUND)	Redacted Volume 1
SUPPORT)	
)	
)	
)	

January 26, 2016
9:00 a.m.

Hearing Officer: Jennie T. Jonsson

Location: PUBLIC SERVICE COMMISSION
160 East 300 South, Room 451
Salt Lake City, Utah
Job No: 281110R

Reporter: Melinda J. Andersen
Certified Shorthand Reporter and Notary Public

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A P P E A R A N C E S

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1 P R O C E E D I N G S

2 HEARING OFFICER: Good morning. Today is
3 Tuesday January 26, 2016. It is 9:00. This is the date
4 and time set for the formal hearing in the matter of the
5 application of Carbon/Emery Telecom Incorporated for an
6 increase in Utah Universal Service Fund Support. This is
7 Public Service Commission Docket 15-2302-01.

8 Let's go ahead and get appearances on the
9 record. Carbon/Emery.

10 MS. SLAWSON: Thank you. My name is Kira
11 Slawson. I represent Carbon/Emery Telecom Inc. as the
12 attorney. With me, starting at the far end of counsel
13 table is Brock Johansen, the CEO of Carbon/Emery Telecom
14 Inc. Next to him, and next to me, is Darren Woolsey, the
15 CFO of Carbon/Emery Telecom Inc. We also have another
16 witness, Douglas Meredith from JSI.

17 HEARING OFFICER: Then you are also
18 representing URTA, the intervener; is that correct?

19 MS. SLAWSON: I am, yes.

20 HEARING OFFICER: Thank you. Is anyone else
21 here from URTA?

22 MS. SLAWSON: No -- well, Douglas Meredith is
23 the witness for URTA, yes.

24 HEARING OFFICER: Thank you. And for the
25 Division.

1 MR. JETTER: Good morning. I'm Justin Jetter.
2 I'm with the Utah Attorney General's office and I represent
3 the Utah Division of Public Utilities. With me at counsel
4 table is William Duncan with the Utah Division of Public
5 Utilities. And the Division intends to present two
6 witnesses today who are seated in the back, Casey Coleman
7 and Joseph Hellewell.

8 HEARING OFFICER: Thank you. And for the
9 Office.

10 THE WITNESS: Robert Moore, Attorney General's
11 office representing the Office of Consumer Services.
12 Seated next to me is our witness Bion Ostrander. We also
13 have a witness David Brevitz who will be testifying. And
14 Michele Beck, the director of the Office of Consumer
15 Services, is also present and she may speak to any policy
16 issues that come up during the hearing.

17 HEARING OFFICER: Thank you. Just as we get
18 started here, a couple of housekeeping matters. We are
19 scheduled to break from the UUSF hearing this morning at
20 noon to take any comments from any public witnesses who
21 might appear. I don't know if any will be here or not. We
22 haven't had any requests to call in, correct? So we'll see
23 if anybody comes. If we don't see anybody for the public
24 witness hearing then I think we could just continue with
25 the UUSF hearing. We do need to be prepared to take public

1 comments for a period of about an hour at least, but then
2 at 1:00 we could take a lunch break. Does that sound all
3 right?

4 Let's talk about witness and exhibit lists just
5 briefly. All parties have filed those and the Office did a
6 little amendment to it yesterday to remove information that
7 related to testimony that's been withdrawn. Does any party
8 have an objection to any other party's witness and exhibit
9 list today? Carbon.

10 MS. SLAWSON: I guess it's not so much as an
11 objection, but I wasn't aware that Ms. Beck was on the
12 witness list for policy issues.

13 HEARING OFFICER: Do you object to her making a
14 statement if she feels it is necessary?

15 MS. SLAWSON: We would obviously want the
16 opportunity to cross examine on any statements.

17 HEARING OFFICER: All right. Thank you.
18 Division, any objection?

19 MR. JETTER: The Division has no objection.

20 HEARING OFFICER: Office.

21 MR. MOORE: That's fine.

22 HEARING OFFICER: And you speak for URTA as
23 well?

24 MS. SLAWSON: I do.

25 HEARING OFFICER: Thank you. So I think it

1 would be appropriate, largely the exhibit and witness lists
2 -- well, the exhibit lists just capture and summarize the
3 prefiled testimony that's been submitted. So I believe all
4 the parties have had a chance to look at all of that. I
5 think it would be appropriate for me to just accept it into
6 the record as filed and as marked and that might save us
7 some time. Is that what the parties were expecting, or is
8 that acceptable?

9 MS. SLAWSON: That's acceptable to the Company.

10 MR. JETTER: It's generally acceptable to the
11 Division. We have some corrections that we would like to
12 make that generally the witnesses will do at the beginning
13 of their testimony. I'll walk through that with them.

14 HEARING OFFICER: Okay. Office, does that meet
15 with your expectations?

16 MR. MOORE: That's fine. I had some exhibits
17 that came up that might not have been on the exhibit list.
18 I guess Ms. Slawson can object to them at that time if she
19 feels.

20 HEARING OFFICER: Sure.

21 MR. MOORE: If she feels they're not
22 appropriate.

23 HEARING OFFICER: But to the extent that we
24 already have filed exhibits that are on that list, we'll
25 accept them to the record as filed subject to correction

1 during testimony and as premarked. Okay. I think that
2 will save us some time.

3 The next thing I wanted to do for housekeeping
4 is just note for the record that many of the exhibits do
5 contain information that the parties have marked as
6 confidential. Generally the confidential sections include
7 financial information and numbers. I just wanted to make
8 the parties aware and put on to the record Utah Code
9 Section 54-3-21(4), which requires this hearing to be open
10 to the public, including all records to be open to the
11 public, except it says that the Commission may withhold
12 from the public any information that it determines needs to
13 be withheld in the best interest of the public. I can give
14 you that. Do you want me to read it exactly what it says?

15 MS. SLAWSON: No, that's fine.

16 HEARING OFFICER: So I anticipate today that
17 the parties will be discussing concepts and principles and
18 polices and leave the numbers where they are, which is in
19 the confident exhibits. If you find it necessary to talk
20 about the numbers today and you want me to close the
21 hearing for the purpose of doing that you're going to have
22 to demonstrate that closing the hearing is in the public
23 interest, which is an interesting concept. I just wanted
24 to make the parties aware of that.

25 Then finally, the Commission issued a notice a

1 few days ago on January 21st asking the parties to be
2 prepared to address threshold questions that are raised in
3 the statute specifically prohibiting any use of UUSF funds
4 for support of unregulated activities or any activities
5 that do not constitute basic telephone service. Do the
6 parties have a preference as to how and when to address
7 these issues?

8 MS. SLAWSON: The Company, Carbon/Emery would
9 prefer that these issues be addressed in post hearing
10 briefing. I think that affords the opportunity to look at
11 the legal aspects of the statute after all the testimony
12 has been entered so we can apply the legal aspects of the
13 statute to the testimony as in the record.

14 HEARING OFFICER: Are you prepared to address
15 it at all today?

16 MS. SLAWSON: I am.

17 HEARING OFFICER: Could you address it at least
18 generally at the outset here, the threshold question, so if
19 the statute isn't satisfied then that is perhaps as far as
20 we need to go. If you could address it at least briefly at
21 the beginning that would be helpful.

22 MS. SLAWSON: Okay.

23 HEARING OFFICER: Division.

24 MR. JETTER: I suppose we have a question for
25 the Commission on this. We have a witness prepared to give

1 a statement responding to those questions, but we weren't
2 certain if you preferred that from counsel or -- it's kind
3 of to some extent mixed questions of policy that may be
4 more appropriate, at least from the Division's perspective,
5 to have one of our policy folks discuss it. But the
6 alternative is also I'm prepared to provide you with our
7 position on it.

8 HEARING OFFICER: Perhaps you could just
9 address it briefly upfront.

10 MR. JETTER: Okay.

11 HEARING OFFICER: And then we'll take your
12 witness whenever you want to bring him or her.

13 THE WITNESS: Okay.

14 HEARING OFFICER: Office.

15 MR. MOORE: We'll address it briefly in the
16 beginning. We also have a condensed written response that
17 we would like to introduce as an exhibit if Ms. Slawson
18 does not object. Also this is the reason we have Ms. Beck
19 available to talk on policy questions if they arise.

20 HEARING OFFICER: All right. Thank you. So
21 that is all that I wanted to discuss here as we get started
22 in terms of housekeeping. Do the parties have any other
23 questions that we need to talk about before we go into the
24 meat of this matter? All right. It doesn't look like it.
25 Are the parties ready to begin then with opening

1 statements?

2 MS. SLAWSON: Basically I would introduce the
3 witness and then each witness has prepared a summary of
4 their testimony, so I didn't prepare any particular opening
5 statement.

6 HEARING OFFICER: All right. The Division or
7 the Office, you're fine to left Carbon just go ahead?

8 MR. JETTER: Yes. I think our general practice
9 has not been to offer -- generally we don't have an opening
10 or closing statement unless requested by the Commission.

11 HEARING OFFICER: All right. Very good.

12 MS. SLAWSON: I guess as a preliminary matter
13 in light of what Mr. Jetter just said, we have requested
14 through an e-mail communication with counsel and the with
15 the ALJ that there be closing argument in this matter. And
16 we suggested that our preference was to have that on a post
17 hearing basis provided in a written form. But we are
18 prepared if necessary and if time permits to do a closing
19 argument also.

20 HEARING OFFICER: I think I responded and said
21 we'll see how the hearing goes.

22 MS. SLAWSON: Exactly.

23 HEARING OFFICER: Very good. All right. Then
24 under the rule Carbon/Emery, which is the applicant, has
25 the burden of proof. Begin. Go ahead.

1 MS. SLAWSON: Thank you. I would like to call
2 Darren Woolsey -- I'm sorry, I mean Brock Johansen to the
3 stand.

4 (The witness is sworn in.)

5 DIRECT EXAMINATION

6 BY MS. SLAWSON:

7 Q. Good morning, Mr. Johansen. Would you please
8 state your name, employer and business address for the
9 record?

10 A. Yes. Brock Johansen. I'm the chief executive
11 officer of Carbon/Emery Telecom Inc. My business address
12 is 445 East Highway 29, Orangeville, Utah, 84537.

13 Q. On behalf of the applicant Carbon/Emery you
14 have participated in this record, correct?

15 A. Yes.

16 Q. Have you prepared and caused to be filed
17 testimony in this record?

18 A. Yes.

19 Q. If you were asked those same questions here
20 today that you prepared in written form, would your answers
21 be the same?

22 A. Yes.

23 Q. Do you have any correction to the testimony
24 that you gave in your prefiled testimony?

25 A. Yes, just one. Through this process the amount

1 that Carbon/Emery has requested in UUSF distribution has
2 changed. So lines 59 and 141 should be corrected to
3 reflect the accurate amount of \$570,643 which is the amount
4 of Carbon/Emery's UUSF request.

5 **Q. Do you have a summary of your testimony that**
6 **you would like to give today?**

7 A. Yes.

8 **Q. Go ahead.**

9 A. I filed direct testimony in support of
10 Carbon/Emery's amended application for an increase in Utah
11 Universal Service Fund distributions. The purpose of my
12 testimony is to demonstrate that Carbon/Emery is a
13 telephone corporation qualified to transact business and
14 operate as a local exchange carrier providing
15 telecommunications services within the State of Utah under
16 authority issued to Carbon/Emery by the Utah Public Service
17 Commission, which I will refer to as the Commission, and to
18 testify that Carbon/Emery is an eligible telecommunications
19 carrier pursuant to 47 U.S.C. Section 214(e) and is in
20 compliance with Commission orders and rules.

21 I testify that Carbon/Emery conducted a
22 thorough review of its operational expenses and revenues
23 for test year 2014, adjusted for known and measurable
24 changes, and determined that Carbon/Emery has a revenue
25 deficiency, which pursuant to Utah Code Annotated Section

1 54-8b-15 and Utah Administrative Code R746-360 Carbon/Emery
2 is entitled to receive additional disbursements from the
3 Utah Universal Service Fund (UUSF). I testify that the
4 increase of UUSF support will enable Carbon/Emery to
5 continue providing affordable service to its customers, and
6 to engage in construction of capital projects, while
7 earning a reasonable rate of return as permitted by Utah
8 Code.

9 I indicate in my testimony that Carbon/Emery's
10 current rates for basic residential and commercial services
11 are set at the current affordable base rate as determined
12 by the Commission.

13 I identify Darren Woolsey, Carbon/Emery's Chief
14 Financial Officer, and Douglas Meredith of John Staurulakis
15 Inc. as individuals who will be providing additional
16 testimony on behalf of Carbon/Emery. And I indicate I have
17 reviewed the testimony and exhibits filed on behalf of
18 Carbon/Emery in this case and that the testimony and
19 exhibits filed on behalf of Carbon/Emery accurately reflect
20 the financial and operational situation of the company.

21 I also present testimony that Carbon/Emery has
22 not implemented any significant changes in its accounting
23 procedures. I describe the collection and write-off
24 policies for bad debt. And I identify immaterial penalties
25 assessed to the company. I testify that the company has

1 not received any revenue ruling requests, IRS responses or
2 had any correspondence from the IRS other than periodic
3 filing of payroll and tax forms.

4 Finally, I testify that the increase in UUSF
5 support requested by Carbon/Emery is in the public interest
6 and is just and reasonable to permit Carbon/Emery to
7 continue to provide telecommunications services at just and
8 reasonable rates to its customers. This concludes the
9 summary of my testimony.

10 MS. SLAWSON: Mr. Johansen is now available for
11 cross examination questions.

12 HEARING OFFICER: Mr. Jetter, anything?

13 MR. JETTER: No questions from the Division.

14 HEARING OFFICER: Mr. Moore?

15 MR. MOORE: No questions. Thank you.

16 MS. SLAWSON: Carbon/Emery would now like to
17 call to the stand Darren Woolsey.

18 (The witness is sworn in.)

19 DIRECT EXAMINATION

20 BY MS. SLAWSON:

21 Q. Would you please state your name, employer and
22 business address for the record?

23 A. Yes. My name is Darren Woolsey. I'm employed
24 by Carbon/Emery Telecom Inc. since April of 2006. The
25 address of our corporation is 445 East Highway 29 in

1 Orangeville, Utah, 84537.

2 Q. Did you prepare and cause to be filed direct,
3 supplemental rebuttal, surrebuttal and sur-surrebuttal
4 testimony with attending exhibits in this case?

5 A. Yes.

6 Q. Do you have any substantive changes to the
7 answers that you gave in the questions asked in the
8 prefiled testimony?

9 A. I have no substantial changes, but there are
10 three small corrections that I would like to make. At line
11 746 of my revised rebuttal testimony, which was dated
12 September 4, 2015, there is a reference to aerial cable
13 plant life which is dated at 20 years. And the correct
14 life for that aerial cable plant should read 10 years.
15 There is no subsequent calculations or additional testimony
16 that rely on that correction.

17 The other two corrections are related to lines
18 402 in the sur-surrebuttal testimony dated December 18,
19 2015. There is a number here which needs to be corrected
20 that was originally marked as confidential.

21 MS. SLAWSON: It's a number that was originally
22 marked as confidential in the testimony. He just wants to
23 make a change to that number. I'm not sure what the best
24 way of making that change is since we want it to remain a
25 confidential number.

1 HEARING OFFICER: If you want to give it to me
2 in this matter you have to make some sort of explanation as
3 to why we close the hearing for that purpose. Otherwise,
4 you're going to have to provide it outside of this open
5 meeting.

6 MS. SLAWSON: We would argue that the hearing
7 should be closed for this limited purpose to state the
8 number so that the confidential record would accurately
9 reflect the correction that needs to be made. We think
10 that the number that is being changed is a calculation with
11 regard to depreciation expense, which is a confidential
12 number which should remain confidential in this hearing.

13 HEARING OFFICER: And why is it in the public
14 interest?

15 MS. SLAWSON: It's in the public interest
16 because the confidential financial information of the
17 company allows -- if in the hands of competitors it could
18 cause a competitive advantage to the competitors and a
19 competitive disadvantage to Carbon/Emery.

20 HEARING OFFICER: Does the Division agree or
21 disagree?

22 MR. JETTER: I think it's generally been our
23 practice to close these hearings when similar issues have
24 come up for the same reasons that we would, I guess, allow
25 the confidentiality of these type of numbers for purpose of

1 encouraging the Company to be as forthcoming as possible
2 with providing at least the Division with as much
3 information as we request without having extensive
4 discovery fights over that.

5 HEARING OFFICER: Mr. Moore.

6 MR. MOORE: We have no objection to going
7 confidential. If it's simply a number that needs to be
8 corrected there doesn't seem to be any strong public reason
9 to have that information provided publically. The public
10 won't gain much in weighing it against the loss of
11 confidential information.

12 HEARING OFFICER: I'm persuaded by Mr. Jetter's
13 argument that allowing any company to keep its financial
14 information confidential is in the public interest because
15 it fosters open disclosure to the Division and to the
16 Commission, which allows for better decision making in
17 these matters. So I will grant the request to close the
18 hearing briefly in order to correct the number in Darren
19 Woolsey's sur-surrebuttal testimony at line 402.

20 Ms. Slawson, is there anybody that you want to
21 leave the room?

22 MS. SLAWSON: No.

23 HEARING OFFICER: Can you pause the stream?

24 Okay. Go ahead.

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HEARING OFFICER: Okay. We are back in the
open portion of this hearing. Go ahead.

1 Q. (By Ms. Slawson) Do those two changes that you
2 have identified confidentially affect the conclusions that
3 you arrived at in your testimony?

4 A. They do not affect the conclusions we arrived
5 at in the testimony.

6 Q. Do you have a summary of your testimony that
7 you would like to give today?

8 A. I do.

9 Q. Go ahead.

10 A. Carbon/Emery Telecom filed an amended
11 application for increase in UUSF support on April 2, 2015.
12 Accompanying this filing was my direct testimony which is
13 provided today to introduce the application and the
14 associated exhibits. The application is based upon a
15 calendar 2014 historical base year and ties directly to the
16 Carbon/Emery 2014 trial balances and annual report
17 submitted to the Public Service Commission of Utah. This
18 is true with only four adjustments needed. One of them is
19 a rate base exclusion. There are two known and measurable
20 adjustments. Then there is the associated tax adjustments
21 needed for these other changes. Based upon this
22 information I recommend that the Commission adopt 2014 with
23 the recommended adjustments as a representative test year
24 for the effective period.

25 I testify that Carbon/Emery complies with FCC

1 rules guiding the measurement, gathering, and allocation of
2 the costs necessary to provide regulated telecommunications
3 services, including the FCC rules contained in Part 32 and
4 Part 64 as well as Public Service Commission Rule
5 746-340-2.

6 My direct testimony includes a general
7 description of the process used in the application for
8 Carbon/Emery's calculation of cost of capital. My
9 testimony regarding this calculation describes the process
10 by which costs are assigned to the interstate or intrastate
11 jurisdiction, the imputation of 35 percent debt through use
12 of a hypothetical capital structure, and the calculation of
13 the authorized rate of return and revenue requirement.

14 I also provide additional testimony addressing
15 various concerns identified by the Division and the Office
16 in their prefiled testimony. Specifically, with the
17 benefit of hindsight and to address concerns raised by the
18 Office and Division with which I do not object, I accept
19 four adjustments to Carbon/Emery's initial UUSF request.

20 These adjustments included a reduction in the
21 original landline loss adjustment proposed by Carbon/Emery
22 to reflect additional actual loss data experienced in 2015.
23 The second item was an increase for nonregulated affiliate
24 revenue projected for the anticipated migration of
25 customers from cable internet to fiber to the home internet

1 as our fiber to the home project progresses. So this is
2 basically a move of customers from our nonregulated plant
3 to our regulated plant. The third item is an increase in
4 interstate revenue to Carbon/Emery related to interstate
5 services provided by Carbon/Emery to its affiliate ET&V.
6 This adjustment was evidenced on the July 2015 cost study,
7 which was unavailable at the time of our original
8 application. And finally, a decrease in rate base for the
9 exclusion of long-term healthcare obligation liabilities
10 consistent with FCC handling of these same liabilities.

11 The combination of the adjustments result in a
12 decrease in the UUSF request of \$246,266.

13 HEARING OFFICER: Can you give me that number
14 again?

15 THE WITNESS: \$246,266, which brings our
16 revised UUSF request to \$570,643.

17 I would like to briefly summarize key disputed
18 issues that I think are remaining in this proceeding.

19 First of all, depreciation. Carbon/Emery's
20 method of depreciation and calculated depreciation expense
21 are at issue in this case. I have testified to the
22 appropriateness of Carbon/Emery's group asset methodology
23 in accordance with the FCC's Uniform System of Accounts,
24 which is contained in Part 32. Specifically, Part 32
25 Section 32.2000(g)(i) promulgates depreciation expense be

1 calculated using a group plan of accounting. This
2 methodology has been consistently applied since
3 Carbon/Emery's beginning in 2001 and is an industry
4 accepted method of calculating depreciation. I testify
5 that Carbon/Emery's test year depreciation expense
6 contained in its application is representative of the
7 effective UUSF period. As support, I testify that
8 historical depreciation has remained consistent with recent
9 increases reflecting plant replacement which is anticipated
10 to continue for the next five to seven years.

11 Though the Division acknowledges that there are
12 many different acceptable methods to calculate
13 depreciation, the Division recommends that the Commission
14 use a single asset depreciation method to calculate the
15 appropriate depreciation expense in this case. I do not
16 agree with the Division's recommendation, nor do I agree
17 with their calculation under that method because the
18 Division's method does not result in a depreciation expense
19 number or a rate base number that is representative of the
20 realized and effective period.

21 The Office does not question the group method
22 of depreciation, but takes exception to the calculation of
23 depreciation expense for certain accounts because of the
24 asset lives of the group. I testify that the depreciation
25 expense in the application is representative of the

1 effective period, and that a switch of depreciation method
2 is not needed. Any concerns raised by the Office or the
3 Division with regard to depreciation expense can be
4 addressed with adjustments to the remaining asset lives in
5 certain groups used by Carbon/Emery as prescribed by the
6 FCC method.

7 In the alternative, if the Commission decides
8 to abandon group depreciation, I testify that such action
9 should be taken on a prospective basis for assets added
10 after the Commission establishes a different methodology.

11 The next outstanding issue that I would like to
12 discuss briefly is the cost of capital used to calculate
13 the required rate of return. With respect to cost of
14 capital, and capital rate structure, I defer to Douglas
15 Meredith who has provided testimony on this issue. My
16 testimony on this issue is limited to using the 12.13
17 percent return on equity, which has been used by the
18 Division in recent cases that we have been involved with.

19 My next topic is the exclusion of certain rate
20 base items. Carbon/Emery's application for additional UUSF
21 includes telephone plant under construction and materials
22 and supplies as rate base items. These inclusions are
23 allowed by the FCC in rate base at their full value, and I
24 testify that the PSC has historically matched this
25 treatment by recognizing these inclusions at their full

1 rate value. The Office proposes a 50 percent reduction to
2 both plant under construction and materials and supplies to
3 which Carbon/Emery remains opposed.

4 I testify that Carbon/Emery's telephone plant
5 under construction account represents the actual plant
6 expenditures with no inclusion of future purchases or known
7 and measurable adjustments. These plant expenditures, like
8 any other properly documented actual plant expenditures,
9 should be included in both federal and state base rate.

10 With respect to the materials and supplies, the
11 Office argues that the materials and supplies account needs
12 to be normalized because it is higher than historical
13 levels. I testify that the increase in materials and
14 supplies represents real purchases of materials and
15 supplies, which are inventoried onsite, and that the
16 increased levels are needed for current operations,
17 including current construction projects. I also testify
18 that the current level of materials and supplies will be
19 needed for at least the next five years. No normalization
20 adjustment is needed to this account.

21 The next issue I would like to discuss is
22 expense allocations, including the CSR allocator and the
23 accounting and general allocator. The Office proposes an
24 adjustment to Carbon/Emery's CSR expense allocator between
25 regulated and nonregulated operations, but the Office's

1 proposed adjustment is based on faulty assumptions. CSR
2 costs are allocated between regulated and nonregulated
3 companies based first on the direct coding of CSR time to
4 the regulated or nonregulated companies. The remaining
5 time that is not direct coded is allocated using four cost
6 allocation factors, including the CSR distribution
7 currently at issue as well as three other allocators
8 including the dispatch distribution, directory
9 distribution, and Moab CSR distributions.

10 I testify that when all CSR coding is
11 considered, more CSR labor in 2014 was coded to the
12 nonregulated affiliates of Carbon/Emery Telecom than to the
13 regulated affiliates -- that was 52 percent versus 48
14 percent -- and that the final disposition of CSR labor and
15 associated other department costs are the result of direct
16 coding as well as the use of these four different cost
17 allocators and we feel that allocation is correct.

18 The Office also takes issue with the CSR
19 distribution allocation factor because it was based on a
20 time study from 2010. I have testified to changes in the
21 CSR department, including the addition diagnostic tools and
22 an advanced internet troubleshooting group. These changes
23 have greatly reduced the amount of time spent by CSR's
24 related to nonregulated customer service functions that
25 they perform. And these changes have corresponded with

1 increased internet customers from that 2010 date. So we
2 feel like the original costs of our time study is still
3 valid in this case.

4 With respect to the accounting and general
5 allocator, I testify that the use of billing records as an
6 indicator of costs is appropriate and results in a
7 representative allocation factor. However, I also testify
8 that with proper weighting and application, the use of
9 plant, labor, and billing records could also be considered
10 representative cost drivers. My testimony includes a
11 recalculation and proper weighting and use of these three
12 identified cost drivers, the billing records, the labor
13 dollars, and the plant costs. The results of this
14 calculation evidence essentially the same allocation
15 percentages for Carbon/Emery as was determined by using
16 just the billing records.

17 The next item with which we take issue is
18 interest synchronization. In this issue I testify that
19 interest synchronization in the Carbon/Emery proceeding is
20 inappropriate. Because Carbon/Emery has no debt, the tax
21 deductions related to interest expense therefore do not
22 exist. We have no debt. No amount of debt imputation in a
23 hypothetical capital structure is going to create that tax
24 deduction. In the absence of any actual interest to
25 synchronize, I maintain that this adjustment is not needed.

1 In doing that I want to be clear here, I concede that the
2 imputation of hypothetical debt on Carbon/Emery will reduce
3 its taxable income because they're going to get less tax in
4 that calculation. So as a result there is less income
5 taxes to be paid because there is less income made there.
6 With interest synchronization, however, there is not any
7 real tax deductions created by that synchronization. What
8 this results in is a change in the amount of tax without
9 having an actual or possibility of an actual interest
10 deduction for tax purposes to offset that. So we have no
11 possibility to ever recover through the UUSF process that
12 interest synchronization. That concludes my summary really
13 on that.

14 Q. (By Ms. Slawson) Thank you. Mr. Woolsey, in
15 Carbon/Emery's application the Company requests that the
16 reasonable costs incurred by Carbon/Emery in the UUSF
17 application be recovered in a one time lump sum
18 distribution to Carbon/Emery from the UUSF. Do you know
19 what those costs are?

20 A. I do not at this time. The costs are
21 continuing at this point. I would anticipate that
22 Carbon/Emery could submit a bill for the costs of this
23 proceeding, that we could submit those to the Commission
24 much like an attorney would do for attorney's fees at the
25 conclusion of a trial.

1 MS. SLAWSON: Mr. Woolsey is now available for
2 cross examination.

3 HEARING OFFICER: Mr. Jetter.

4 CROSS EXAMINATION

5 BY MR. JETTER:

6 Q. Good morning, Mr. Woolsey. I do have a few
7 questions.

8 A. Okay.

9 Q. I would like to ask you a few questions this
10 morning related to depreciation and the depreciation method
11 used by Carbon/Emery. I believe an accurate representation
12 of the testimony both of yours and Mr. Meredith that you
13 would agree that the method of group depreciation proposed
14 by Carbon/Emery does in fact accelerate the depreciation of
15 the assets in many of the listed groups?

16 A. Yes.

17 Q. I'm looking at Confidential Exhibit 1 that was
18 filed by Carbon/Emery in the application. I'm going to
19 avoid using the confidential numbers, but if you could take
20 a quick look --

21 MR. JETTER: Could I have just a moment off the
22 record to ask counsel for Carbon/Emery whether ratios
23 between a few of these numbers would be something they
24 consider confidential?

25 HEARING OFFICER: Sure.

1 (Off the record.)

2 MR. JETTER: I would actually request -- I
3 think it's going to be a little bit more convenient for us
4 to go off the record briefly for this. I shouldn't say off
5 the record, but to go into a confidential mode here.

6 HEARING OFFICER: Go ahead.

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10 HEARING OFFICER: Would you repeat your
11 question, Mr. Jetter?

12 MR. JETTER: Yes.

13 Q. (By Mr. Jetter) I asked if the ratio of those
14 two values indicate that the requested depreciation annual
15 value results in a specific time period in which the entire
16 proposed rate base currently in service would be fully
17 depreciated?

18 A. I agree from that calculation that would be
19 roughly five and a half years if that were a straight up
20 calculation. There are certain components of that
21 calculation which will extend out into the future,
22 including conduit and buildings. The expenses that would
23 become fully depreciated are going to be our cable
24 accounts, both aerial and buried cable, as well as our
25 subscriber equipment. This is actually very appropriate

1 and it's a good starting point I think for discussion.

2 Our subscriber equipment only has an eight year
3 life. We are into this equipment six years at this point
4 from when we purchased the equipment shortly after Brock
5 and I began our employment back in 2006. This equipment is
6 no longer supported by our vender. It needs to be
7 replaced. What we're doing with this replacement is we're
8 corresponding this replacement with the fiber to the home
9 upgrade. So the equipment will be upgraded with fiber to
10 the home type of equipment.

11 Similarly, our buried and aerial cable plant is
12 being significantly overhauled. Fiber to the home, we're
13 actually doing drops to each of our existing customers, not
14 to all homes that currently have copper to them, but to our
15 existing customers. This process is anticipated to
16 continue for the next five years, a little bit longer. We
17 have some outlining areas that we will end up picking up
18 past that point.

19 But this kind of demonstrates the fact that our
20 plant is at the end of its life and it needs to be replaced
21 and we're in the process of doing that. It's not as if
22 this depreciation is the end of the depreciation, the 10
23 million, is scheduled to be replaced. We provided data
24 showing that replacement in a methodical and a very
25 measurable approach to a fiber to the home type

1 replacement.

2 HEARING OFFICER: Can you help me understand
3 what you mean when you say that your existing equipment is
4 no longer supported by your vender?

5 THE WITNESS: I may not be the best person to
6 describe this because I'm an accountant and not the plant
7 guy. But it's electronic equipment that has software
8 capability to it. And at some point the support for that
9 equipment is no longer -- the equipment is no longer
10 supported by the company that originally created the
11 equipment so it requires upgrades to the existing equipment
12 or replacement to the existing equipment. In this case
13 we're moving specifically from the traditional copper based
14 equipment to fiber equipment.

15 HEARING OFFICER: So it's the software
16 component that is no longer supported?

17 THE WITNESS: Right. It's hardware as well. I
18 guess it's a combination of hardware, software that works
19 together to allow the copper -- the phone line at the end
20 of the loop to talk back to the switch at the CO or to
21 allow the transmission of IP data back for internet
22 purposes, that kind of thing. So it's that software,
23 hardware combination that allows that communication to
24 occur.

25 HEARING OFFICER: Thank you. Mr. Jetter.

1 Q. (By Mr. Jetter) Thank you. I would like to
2 ask you just a little bit more about that actually. The
3 software you're discussing no longer being supported and
4 the upgrades needed. Are the upgrades needed necessary for
5 future service for the telephone service?

6 A. Yes.

7 Q. Are they also necessary for faster internet
8 service?

9 A. They do both.

10 Q. Okay. Is part of your telephone service
11 provided on essentially an internet type service than a
12 switching done at -- I guess, through an IP type service
13 rather than a traditional switch telephone service?

14 A. It is a packet base protocol. It is digital.
15 But it isn't internet protocol phone, it is traditional
16 phone.

17 Q. Are you aware of any other vendors that may
18 continue to support the equipment that you have going
19 forward for other companies who are also using that same
20 equipment?

21 A. The equipment could be updated, but it would be
22 a cost similar to the fiber to the home equipment that we
23 decided to replace it with.

24 Q. I'll ask a little bit more about this. The
25 equipment that we're discussing is specifically items that

1 would be in a central office, such as your -- I guess,
2 essentially they're computers that do the switching in a
3 central office; is that right?

4 A. Yes.

5 Q. And that's not the actual cable itself?

6 A. No.

7 MR. JETTER: I would like to, I think, go back
8 into a confidential hearing for another brief time to
9 discuss some more numbers.

10 HEARING OFFICER: Okay.

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HEARING OFFICER: Would you recap where we are and what we're talking about?

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Q. (By Mr. Jetter) To recap for those who were not available to participate in the confidential portion we just returned from, we're discussing the projected capital expenditures through 2019. We're discussing what those expenditures are for and what type of expected life the capital assets that will be acquired and put into service through those expenditures would have.

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A. I do agree with the capital expenditures that are shown on this sheet. We do have again the benefit of hindsight. In 2015 our expenditures are going to come in above \$2 million, so \$1.8 million is a little bit light on capital expenditures there. But otherwise this is representative.

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One thing that we need to be careful -- I indicated about 90 percent of the fiber to the home project would be completed by 2019. The remaining 10 percent is our outlining areas. It is costly. There will still be capital expenditures there to be incurred.

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Then there is additional events that we can see coming. Our soft switch will need to be replaced. We actually -- because those are software based equipment,

1 it's much cheaper than the traditional switch, but it does
2 require updates and replacement on that type of equipment.
3 Similar to the subscriber switching equipment, a 10 year
4 life is actually -- 8 to 10 years is probably pretty
5 representative of what that equipment will do. So it's
6 fair to say that this is representative of what our five
7 year plans are, but it's not the end of capital
8 expenditures.

9 Q. Thank you. Most of the dollars that would be
10 capitalized in those years are going to the actual
11 installation of the fiber lines, the fiber drops to the
12 customers, the needs of the customer premise, that type of
13 thing?

14 A. That's correct.

15 Q. Do you expect that portion of these capital
16 expenditures to last more than eight years?

17 A. The actual cabling?

18 Q. Yes.

19 A. The actual cabling will, yes.

20 Q. Do you have any estimate of what you think a
21 typical lifespan of your fiber network, the fiber drops to
22 the home is?

23 A. For the aerial plant we have a life of 10
24 years. For the buried plant we have 20 years. We're on
25 the front side of this. So each of these asset lives are

1 subject to examination each year. I would say it would at
2 least last the prescribed lives that the Commission has
3 established for these assets.

4 **Q. In fact it would be pretty surprising, wouldn't**
5 **it, if you are 10 years down the road and you're going to**
6 **go out and replace all of your fiber again?**

7 A. I would say that's true.

8 **Q. And even then, it would be surprising probably**
9 **if it was 20 years, wouldn't it?**

10 A. I would disagree with that statement. The
11 reason why is there are so many events that occur in the
12 life of the fiber. What we found -- without working on our
13 fiber to the home project we have averaged \$1.8 million in
14 capital expenditures each year, and that's to maintain our
15 existing plant. We're going to see similar type of
16 expenditures in the future on our fiber plant. We hope
17 that they're less in some respects, but you always have
18 fiber cuts. You have issues that are kind of beyond
19 control of management to prevent. So there is always going
20 to be a portion of the plant that needs to be replaced or
21 upgraded as needed or subject to obsolescence in the case
22 of subscriber equipment and that kind of thing.

23 **Q. Do you expect your fiber network to be as**
24 **reliable as your copper network?**

25 A. More reliable.

1 Q. How old is the average age of your current
2 aerial copper?

3 A. I don't have that calculation in front of me,
4 but I think in the testimony we provided, that detailed
5 list, and it is significantly aged.

6 Q. Significantly longer than 10 years?

7 A. Yes.

8 Q. And the same with your buried cable?

9 A. Yes.

10 Q. And the fiber should be more reliable than that
11 infrastructure you currently have?

12 A. Yes.

13 Q. You have just testified a few minutes ago that
14 you would expect through 2019 capital expenditures that
15 would build out about 90 percent of this network upgrade?

16 A. Correct.

17 Q. So if we were to use the depreciation amount
18 you have proposed here, and I'm going to try to avoid the
19 numbers so we don't back into the confidential mode. You
20 would in fact depreciate practically all of that by, it
21 looks like it would be, a ballpark of 2021. Would you
22 accept that subject to doing your own calculation?

23 A. Which plant are you referring to?

24 Q. All of the capital expenditures that you're
25 going to be making in 2015, 2016, 2017, 2018, 2019,

1 continuing at the depreciation expense that you have
2 proposed in your application.

3 A. No, I would disagree with that statement. The
4 reason why is you excluded your existing asset base in that
5 assumption. So maybe to shed some light on this, you have
6 roughly \$2.3 million a year on average that you're adding,
7 and you're only taking out \$2 million a year in
8 depreciation based upon what I've testified. So you
9 actually have a plant increase over that period of time.
10 It won't be gone. It will actually be greater than it is
11 now.

12 Q. I'm concerned that with some of your answers
13 you're getting into confidential information that I'm
14 trying to avoid.

15 A. Sorry.

16 Q. Ultimately, what you're saying is that the
17 capital expenditures you have planned with the current
18 depreciation estimate you've used have a slightly growing
19 rate base through the end of 2019. And then that would
20 begin to trail off fairly significantly at that point,
21 would it not?

22 A. That is correct. I do want to point using the
23 table you have referenced here that the majority of the
24 expenditures in this project are subscriber equipment.
25 It's not the aerial cable or the buried cable. Fiber

1 cabling is much cheaper than copper cabling. And because
2 we're not doing an entire overlay of the existing plant
3 we're able to save significant amounts of money in the
4 cable aspect of that project.

5 So if you're looking at what it is that we're
6 spending money on, we have nearly \$8 million in -- sorry.
7 You have a large amount of dollars in subscriber equipment
8 that has a very short life. We currently have two-thirds
9 of that amount roughly on the books in subscriber equipment
10 with that same eight year life. So the cycling of that
11 equipment is actually very appropriate. It's matched what
12 we have historically done. We don't foresee any real
13 change in that account going forward.

14 So the rapid acceleration that is being alluded
15 to, I think, in this question is very appropriate for the
16 types of expenditures that we are projecting in the table
17 that is being referenced.

18 **Q. The types of subscriber equipment that you're**
19 **referencing with very short life span, that's directly**
20 **related to the choice to move to fiber; is that correct?**

21 A. Correct. But as I've -- without using specific
22 numbers, it's real similar to the expenditure we incurred
23 to place that equipment in place, the existing copper
24 equipment in place.

25 **Q. If you will indulge my hypothetical here.**

1 Hypothetically if your fiber network is rolled out by 2019
2 and your depreciation remains the same and your capital
3 expenditures beyond 2019 drop significantly as you're not
4 rolling out any new product or new network, approximately
5 -- let's do the math here. You go about five years beyond
6 that. So you're looking at about 2025, 2024. Is that
7 where you would expect to see effectively a depreciation
8 cliff?

9 MS. SLAWSON: I'm going to object to the
10 question it calls for a speculation on a hypothetical.
11 It's not based on the facts in evidence in this case.

12 HEARING OFFICER: I noted your objection. I
13 think the information is useful and I'm going to ask the
14 witness to go ahead and answer the question.

15 THE WITNESS: Can we go confidential again for
16 a minute?

17 HEARING OFFICER: Are you going to talk about
18 actual numbers?

19 THE WITNESS: Yes, as presented in the
20 schedule.

21 HEARING OFFICER: Can you avoid talking about
22 actual numbers, especially whether there will be a
23 depreciation cliff in 2024, 2025 due to there being no
24 further expenditures for infrastructure and basically
25 having everything fully depreciated?

1 THE WITNESS: I would say no. The assumption
2 that there is no additional capital expenditures is a
3 faulty assumption.

4 HEARING OFFICER: Why is that?

5 THE WITNESS: You have to continue to maintain
6 your telecommunications plant. Just because an upgrade is
7 done doesn't mean that there will never be a future need
8 for plant expenditures. There is a myriad of aspects to
9 our plant, including our internal core network that
10 consistently needs upgrades. We have the switching
11 equipment that will need upgrades. The plant itself will
12 require additional maintenance and repair over time. The
13 subscriber equipment we anticipate will last eight years.
14 If we're installing some of this equipment in 2016, it's
15 possible that in 2022 or 2024 this equipment becomes
16 obsolete and needs to be replaced again. So it's short
17 sided to say that you do one upgrade and that's it.
18 Historically we have averaged an amount slightly less than
19 that projected in our application on average, and that was
20 without a significant plant upgrade. And that's just to
21 maintain and replace equipment as needed.

22 HEARING OFFICER: On a copper network?

23 THE WITNESS: On a copper network.

24 HEARING OFFICER: Thank you. You anticipate
25 the costs will be essentially the same on a fiber network

1 beyond --

2 THE WITNESS: During the build out period it
3 jumps up. So for sure we see an increase in the activities
4 of these accounts. We've also focussed the dollars on the
5 replacement rather than the maintenance, so you see a
6 shifting of dollars to that project. Once the project is
7 completed there will be a shift back to normal maintenance
8 and repair costs that have a life more than a year so we
9 capitalize it. So there is an ongoing cost there. We hope
10 it will be less, but in some respects there is always going
11 to be additional maintenance and repair and upgrades to
12 that equipment to maintain it.

13 HEARING OFFICER: How much fiber do you have
14 laid currently?

15 THE WITNESS: That question may be better for
16 Brock.

17 HEARING OFFICER: But there is some?

18 THE WITNESS: There is some, yes.

19 HEARING OFFICER: How long has it been in
20 place?

21 THE WITNESS: Well, depending on the sections
22 we actually started laying fiber to what we call fiber to
23 the node or fiber to the curb three or four years ago. So
24 some of the capital expenditures that we've incurred up to
25 this point have been part of the future plan to take that

1 all the way to the customer homes. So it's been quite some
2 time since we really replaced copper. Unless there is a
3 direct need it doesn't make sense to do that. Like trunk
4 copper is about a sixth of the cost of the -- sorry. Fiber
5 is a sixth of the cost of the equivalent copper. On a
6 fiber drop it's about half the cost of a copper drop. So
7 when that ages it doesn't make sense to replace it with
8 copper anymore.

9 HEARING OFFICER: I guess what I'm struggling
10 to understand is the cost to install the fiber in year one
11 versus the cost to main it in year two. Are those costs
12 the same?

13 THE WITNESS: No.

14 HEARING OFFICER: That's what I'm trying to
15 understand as I listen to your testimony and you say that
16 these costs that you're projected to due to build out will
17 basically become costs to maintain the build out in
18 subsequent years and there is no real change in the number.
19 That's what I kind of hear you saying. Have I heard you
20 incorrectly?

21 THE WITNESS: I've provided testimony that our
22 historical average is --

23 HEARING OFFICER: Meaningful.

24 THE WITNESS: -- meaningful, yes. And it is
25 increased by about \$600,000 during this phrase. I

1 anticipate that we'll probably go back down to that average
2 prior to this phase. So our historical capital
3 expenditures will probably remain consistent for this
4 period of time. For the build out it's going to go up by
5 about \$600,000 for each of those years.

6 HEARING OFFICER: I'm sorry for jumping in.
7 Mr. Jetter, please continue.

8 MS. SLAWSON: Your Honor, if it would be
9 helpful to the process Mr. Johansen will probably be able
10 to answer some of those questions.

11 HEARING OFFICER: He seems very eager to say
12 something. Is that all right, Mr. Jetter?

13 MR. JETTER: I'm happy to recall -- I think I
14 would prefer the best information from the best witness to
15 answer this.

16 HEARING OFFICER: All right. That's fine. Go
17 ahead.

18 MR. JOHANSEN: Do you want me to answer the
19 same question?

20 HEARING OFFICER: I want you to say what is
21 burning to be said.

22 MR. JOHANSEN: I don't know the confidential
23 information. Darren knows that. The only other person
24 probably in this room that understands this is Bill because
25 we're the plant guys, right. We're getting things confused

1 here from a plant standpoint. So let me back everybody up.
2 When Darren says we're going to be 90 percent down, he's
3 talking customers. But that's not 90 percent of the
4 project. And everybody needs to understand that.

5 The first phase of the project is East Carbon,
6 Wellington, Price and Helper. It's the main customers.
7 Then we're going into Miller Creek, and Miller Creek is
8 spread out. So you're not going to see the capital budget
9 fall like Mr. Jetter is saying. Those customers have to be
10 served too. And that's going to be an increase in cost
11 because those customers are a lot further out. So we're
12 not going to be serving -- if you know the Price area at
13 all. Right now we're building -- and we have to separate
14 trunk versus drop. Drops are most expensive. They cost us
15 a lot of money.

16 There are a whole bunch of things going on
17 here, and this is for your clarification in your question
18 you asked Darren. When you go build a network it's not all
19 -- you go out and you put the trunk in and then you have to
20 drop to the customers and then you have the electronics,
21 right. Different parts of that can go bad.

22 For those of you that have computers, they
23 don't last very long. Seven, eight years and processors
24 start failing, the hard drives start failing. That's what
25 is on the end of this. That's your electronics. A seven

1 year old electronic computer is old. It's going to get
2 replaced. It's not going be supported. That's what is
3 hanging on the end of this fiber and it's what is hanging
4 on the end of the copper. It's a computer. And that
5 computer will end life in about seven or eight years, which
6 is exactly close to what is prescribed by the Commission
7 for depreciated life.

8 Now you talk about the actual going out in the
9 future. The Division is trying to say there is a cliff.
10 We get done with these projections that Darren has out
11 there and it is a cliff. It isn't. They only go into the
12 hard reach areas. You have North Coal Creek -- and I would
13 have loved to have had the Division or the Office come down
14 and talk about this. None of them wanted to do a plant
15 tour. They didn't come down to inspect --

16 HEARING OFFICER: I don't want to talk about
17 those things.

18 MR. JOHANSEN: Okay. But if they want to talk
19 about this issue and what's going to happen on our build
20 out, we can talk about that. But the point I think that is
21 important here is it's not going to drop. We're going to
22 go into North Coal Creek. That's going to be one customer
23 per half mile. That's an exaggeration probably. Then
24 you're going to go into Miller Creek. Then you're going to
25 go up above West Wood. Then you're going to go up into --

1 there are a bunch of outlining areas. So this project
2 doesn't end in year five.

3 Then after that, Darren said there are a bunch
4 of other parts of the network. Our core is getting
5 dilapidated. We don't have money to put into the core.
6 The core is a 10 year core that we updated a few years ago.
7 It needs to go to a 100 gig core. It does. You're hanging
8 all of this off from your output. So right now our money
9 is going towards fiber deployment, we haven't gone back to
10 the router. So now you're back to the core. So those have
11 to be upgraded. Then there is fiber between some of the
12 towns that needs to be upgrade that is old. It's 10, 15
13 years old now and we're starting to see errors on it. It's
14 old -- there are actually different types of fiber, and
15 it's an old fiber that we put in back in the day. So that
16 needs to be replaced. So we have these lists of projects.
17 They go out a lot further than what the Division is asking
18 right here. It's not a cliff and we're just going to stop.
19 There is a lot of capital expenditures to keep the network
20 going and we're going to keep making those capital
21 expenditures as long as we have the funding and they're
22 necessary to provide telecommunications services. They
23 are. That network is going to get old. The electronics
24 are going to get old.

25 And then one other thing I think is important

1 is -- I think everybody thinks when you put fiber in it's
2 golden forever, especially on drops. That's not the case.
3 Drops are a huge cost. Aerial drops get caught in the
4 wind, they blow, they -- if you picture we have our strand
5 that holds it pretty solid out on the trunk, but on the
6 fiber drop it's kind of waving there because you don't have
7 a strand holding it, it's just going from a pole over
8 there. Those come, those break, and within about 10 years
9 you're going to replace them. These are well established
10 principles that I'm sure somebody took into account when
11 the Commission gave us the lives. They should have. But
12 the point is the fiber doesn't just stay there and is good
13 forever. It doesn't. That's not how the plant works.

14 And the other point is there is not a cliff
15 where, boom, we're not going to do anymore capital
16 expenditures. We might have 90 percent of the customers,
17 the last 10 are going to take years.

18 CROSS EXAMINATION

19 BY MR. JETTER:

20 **Q. I would like to ask you some followup**
21 **questions.**

22 A. Sure.

23 **Q. Those customers that you're discussing, the**
24 **sort of the end of the line customers, are you currently**
25 **servicing those customers?**

1 A. We are.

2 **Q. And they currently have telephone service?**

3 A. They do. On buried and copper networks it
4 requires a lot of maintenance because -- especially since
5 you figure a lot of those are going out. It's really
6 interesting on how the plant works. A lot of buried
7 copper, and because it's buried you're out in fields where
8 moisture gets in, the lines get old, more moisture gets in.
9 Those are our hardest to maintain, but we're trying to do
10 the biggest bang for the buck. We're cutting the towns
11 first and then we'll go into those areas, but they need to
12 be cut because it's hard to provide telecommunications
13 services when their lines aren't as good of quality, but
14 they're hard to reach.

15 **Q. When you say telecommunications service you**
16 **mean internet and telephone?**

17 A. No, I'm referring to basic telephone service.
18 Even basic telephone service to serve these you've got to
19 think the net plant. Of course you can put internet across
20 it also, but for this rate increase purpose we're talking
21 basic telephone services.

22 **Q. And you testified though that you currently are**
23 **providing that to all of those customers?**

24 A. All of them?

25 **Q. The customers that you're intending to replace**

1 **that with funding?**

2 A. Yes. The project is only to replace current
3 customers. We're not just going to run lines out to
4 locations that aren't taking our services if that's what
5 you mean, Mr. Jetter.

6 **Q. I'm just talking about where you're rolling out**
7 **your fiber.**

8 A. We're going to roll out fiber -- I mean, the
9 plan will be to everybody if possible to fiber eventually
10 and get rid of those old copper lines that are hard to
11 maintain.

12 **Q. So the fiber should be cheaper; is that right?**

13 A. Fiber is cheaper and it's actually -- the FCC
14 said if we're going to replace something put fiber in
15 because it is cheaper. If I went and ran new copper lines
16 to Miller Creek it's going to cost me a lot more than
17 running fiber to Miller Creek.

18 **Q. And fiber is a lot cheaper to maintain; is that**
19 **also correct?**

20 A. I can't testify to that. The studies show that
21 it should be, but we're just cutting. So I don't have a
22 lot of data personally on that.

23 **Q. But you don't project any reduction in the**
24 **costs of maintaining it?**

25 A. Well, those costs -- again, I think we're

1 getting a little off topic here in that some of those will
2 be realized way outside the effective time period of this
3 rate case if at all. So you've got to remember this cut is
4 going to take a couple years. If all of a sudden our
5 expenses go down, when the Division is reviewing our costs
6 then they can pull us back in. But there is no reason to
7 say, okay, we'll -- we know that's not going to be until we
8 get fiber project done, which is years out. So if at that
9 point our costs of operation goes down pull us back in.
10 That's the process. But we don't need to say in five years
11 you're going to have decreased operations, so right now
12 you're going to get penalized. I mean, pull us back in in
13 five years. But I can't even project. They do say that
14 those costs should go down dramatically, but we're not
15 going to realize that for years. And Mr. Jetter, if the
16 Division -- they review our numbers every year, and if they
17 want to pull us back in, they can do it.

18 **Q. Are you familiar with an accounting term called**
19 **the matching principle?**

20 A. No, I'm not an accountant.

21 **Q. Maybe this is a question back for Darren.**

22 A. Do you want to jump back? Your Honor, do you
23 have any other questions about the plant?

24 **Q. I do have some more questions about the plant.**

25 HEARING OFFICER: Go ahead. I have one as well

1 which is why the 10 gigabyte -- did you say core? Is that
2 the term you used, 10 gigabyte --

3 THE WITNESS: Yes, core. There is --

4 HEARING OFFICER: -- is needed?

5 THE WITNESS: Yes. So there --

6 HEARING OFFICER: My question is is it needed
7 for basic telephone or is it needed for --

8 THE WITNESS: Sure.

9 HEARING OFFICER: -- all of the other things?

10 THE WITNESS: No, definitely it is needed for
11 that. The core -- again, it's an upgrade issue. So
12 whether you upgrade to a bigger core or not you still have
13 to upgrade those because those routers are still -- and
14 they're expensive. They're -- I don't know. I think we
15 just bought one and it was \$120,000. But the core is again
16 a computer, and that core is about six years old now. My
17 IT guys have put in the capital budget every year, hey, the
18 core is starting to take errors, we're having outages
19 because of this. And I say, well, the project right now is
20 fiber to the home. We'll put that behind fiber to the
21 home. So it's just like other electronics. You're going
22 to have to maintain it. These things you don't just put
23 them in and they drive forever. You don't buy one computer
24 and it lasts for your whole lifetime. It's not going to do
25 that.

1 HEARING OFFICER: You say it's six years old
2 currently?

3 THE WITNESS: I would have to go back and look,
4 but I think we actually started the core project about the
5 same time as some -- it might actually be a little older.
6 Some of them might be -- I would have to go back. The
7 router it's kind of -- you don't go in and replace the
8 whole core. You'll say okay, I'm going to replace the main
9 router. These are the main routers that are connecting the
10 town and creating the core. So we'll say this year we're
11 going to replace the Price router, this year we're going to
12 replace the Helper router, this year we're going to replace
13 the -- these are \$120,000 to \$150,000 computers. It's not
14 cheap. And so there are things like that. There is the
15 old DWM equipment. We can go on and on. The network isn't
16 just the fiber. The DWM equipment is the actual -- across
17 the fiber you split it into light weight lengths, and that
18 DWM input is getting old and we're starting to have trouble
19 maintaining it too. So it's all throughout. You maintain
20 a network.

21 The point here that I want to make is, one, the
22 project doesn't end when we get 90 percent of the towns
23 done. We still have to go out and serve the hard to reach
24 areas that are really the hardest for us to serve even with
25 basic telephone services. Point number two is there are

1 other projects. And point number three is if at any point
2 they need to pull us back in that's the rule, they can.

3 HEARING OFFICER: Go ahead.

4 Q. (By Mr. Jetter) Thank you. When you're
5 talking about 10 gigabyte or 100 gigabyte core we're
6 talking about bits per second; is that correct?

7 A. Yes. In testifying again to what you asked
8 Darren a minute ago, basic telephone now is packet based.
9 So you're putting packets across that and that's all that
10 goes across the core is IP network.

11 Q. Of the network that you're using now, and the
12 one you intend to use, do you have an idea about what
13 percentage of the bit rate is being taken up by basic
14 telephone service?

15 A. I would not know that number.

16 Q. Do you think across your entire network you've
17 ever used 10 gigabytes per second of basic telephone
18 service transfer?

19 A. No. But again, Mr. Jetter, you're -- this is
20 when it gets to be attorneys and lawyers talking about
21 networks that they don't understand. A 10 gig core does
22 not mean that you need a full 10 gigs because you're going
23 to be using every core. It's called an MPLS network.
24 Mr. Jetter, you probably don't know what an MPLS network
25 is. But an MPLS network is put in so you actually create

1 the circuit across an IP -- you have one 10 gig core and
2 you're creating individual circuits between it. So even
3 though you might not be maxing out the full 10 gig, you
4 need the 10 gigs to create the different circuits. Those
5 circuits used to run across old copper T1's, those T1's are
6 now converted on to -- or DS3's or converted on to IP and
7 they run across that. So we're not talking full capacity
8 when you're saying do I need a 10 gig core. You have to
9 look at the number of circuits inside that core and what
10 they're carrying and how they're configured. So it's
11 completely different than to just say -- you can't think of
12 it like a -- a normal resident would say I have 10 meg at
13 my house. That's not how these networks run. And it's a
14 complete lack of understanding when people look at them
15 that way. MPLS 10 gig core is completely different than
16 just a 10 gig pipe.

17 **Q. Are you expanding the number of circuits in --**

18 **A.** Definitely. Everything single one of these --
19 every one of these nodes that is served by the fiber has to
20 have an IP port back. It's a separate circuit back.
21 That's how you talk to the switch out to an area where
22 you're going to hang out these fiber OLT. The ONT is at
23 the house. The OLT you could have a circuit between the
24 core and each one of those is a different circuit. So that
25 MPLS, the reason why that technology is developed is

1 because as you add more and more of those on you need more
2 and more circuits.

3 **Q. And that's --**

4 A. Don't look at it as a total capacity is what
5 I'm saying. Don't say, oh, it's 10 gig. It's a lot more
6 complex than that.

7 **Q. Let me ask you this question. As you increase**
8 **your core capacity does it increase your ability to sell**
9 **higher band width internet?**

10 A. Sure.

11 **Q. The more internet you want to sell the larger**
12 **capacity core you're going to need?**

13 A. Sure. The internet definitely drives usage.
14 But I'm saying don't look at as simple as that. You have
15 to remember this includes specials also, specials are
16 circuits across that, special access circuits.

17 **Q. But ultimately the majority of the computation**
18 **that is being done in the routing of those packets is**
19 **primarily on a band width level for the internet services?**

20 A. It kind of depends on which leg you're on that
21 core. Some of those would be, some of those will be
22 special circuit. It just kind of -- again, you can't look
23 at one area. You can say on the Price router or on -- and
24 I don't have the stats on that immediately. But you could
25 say okay the Price router, what is the primary going across

1 that and then you could look at the whole mountain or you
2 could look at whatever, it might be special circuits or it
3 might be customer voice. It just depends on what it is and
4 where it's located.

5 MR. JETTER: I think that's the questions I
6 have about the network upgrade.

7 THE WITNESS: Thank you, Mr. Jetter.

8 HEARING OFFICER: Mr. Moore.

9 MR. JETTER: I have more questions for
10 Mr. Woolsey.

11 HEARING OFFICER: Go ahead.

12 CROSS EXAMINATION Resumed

13 BY MR. JETTER:

14 Q. Are you familiar with the matching principle in
15 accounting?

16 A. Yes.

17 Q. Would you describe what that means to you
18 generally?

19 A. The matching principle generally requires that
20 events that occur within a period are matched to their
21 associated expenses. So if you have a revenue transaction
22 that occurs, you have a point of sale. We sell a computer
23 or we sell phone service, you would match that to the
24 associated costs for the same period. So if there is a
25 cost of goods sold or an inventory transaction, those would

1 also be recorded in conjunction with that.

2 Q. Thank you. So with respect to building out,
3 for example, a fiber network would the matching principle
4 generally suggest that the depreciation method chosen would
5 be one that would spread the cost, if you will, spread the
6 recognition of those costs through depreciation expense
7 over effectively as close as you can get the life of that
8 asset that you're capitalizing? I suppose being more
9 specific, the period of time in which that asset that
10 you're capitalizing being used to produce revenue?

11 A. That's correct. That really becomes the
12 question that we're dealing with today. What is
13 representative, what is the life of the asset.

14 Q. It is your testimony though that the
15 depreciation rate that you have chosen is relatively in the
16 ballpark of the annual capitalization of the network on an
17 annual basis is appropriate?

18 A. Yes.

19 Q. One final followup question. If hypothetically
20 you had reached a point of zero on your depreciation
21 account head, taking your company's proposed rate plan of
22 service to a value of zero before you had started to
23 install the fiber network, so say you're starting from zero
24 today, would it be appropriate to expense the fiber network
25 costs annually as you go forward?

1 A. The portion that is related to depreciation
2 expense for that matching principle, yes.

3 **Q. I mean the expense -- the entire costs on an**
4 **annual basis?**

5 A. No.

6 MR. JETTER: Thank you. Those are all the
7 questions I have, Mr. Woolsey. Thank you.

8 HEARING OFFICER: Mr. Moore.

9 MR. MOORE: Yes, I have a few questions.
10 Before we get on to depreciation I would like you to
11 quickly clear up some confusion I have in the record. I'm
12 going to pass down to you Carbon/Emery's response to the
13 Division's sixth set of discovery requests.

14 MS. SLAWSON: Mr. Moore, is this identified in
15 your exhibit list?

16 MR. MOORE: It's not in the exhibit list. I
17 can make it an exhibit if you would like or I can just ask
18 questions of it.

19 MS. SLAWSON: I'll look through it.

20 CROSS EXAMINATION

21 BY MR. MOORE:

22 **Q. I just have a quick question on this. Could**
23 **you turn to the second page on request 6.2. Do you see**
24 **that?**

25 A. Yes.

1 **Q. Could you read the question for the record**
2 **please beginning, Mr. Woolsey states that a single asset**
3 **straight line system?**

4 A. Mr. Woolsey states that a single asset straight
5 line system would be too burdensome for Carbon/Emery to use
6 and implement. However, a single asset system is used by
7 Carbon/Emery for all their nonregulated plant. Why is it
8 too burdensome for the regulated sites, but not for the
9 nonregulated sites?

10 **Q. Thank you. Can you switch down to the second**
11 **paragraph of your response and read the first two**
12 **sentences?**

13 MS. SLAWSON: Your Honor, I'm going to object
14 at this point because there is a portion of the response
15 before that that includes an objection to the question. So
16 I think that should be part of the record too.

17 **Q. (By Mr. Moore) Fine. Could you read from**
18 **response to the first paragraph into the record and then go**
19 **down to the second paragraph and read down until the first**
20 **three lines, group asset depreciation?**

21 A. Carbon objects to this data request because the
22 premise of the question mischaracterizes Mr. Woolsey's
23 surrebuttal testimony. Line 76 to 77 of Mr. Woolsey's
24 surrebuttal testimony did not include the phrase too
25 burdensome, but rather Mr. Woolsey testified that to treat

1 these assets as individual units would be administratively
2 burdensome. Carbon further objects to this data request as
3 it implies that Carbon/Emery uses the single asset method
4 of depreciation in its nonregulated plant. This is not
5 accurate. The nonregulated company does use group asset
6 depreciation.

7 **Q. Can you now turn to page 20 of your revised**
8 **confidential rebuttal testimony filed September 4, 2015.**
9 **Could you read the question and the first part of the**
10 **answer starting on line 407 and ending on line 413 with the**
11 **words straight line depreciation?**

12 A. So you want me to read from 309 to 313?

13 **Q. I think it would make more sense if you would**
14 **read from 407 to 413.**

15 A. Do you agree that plant can be used as an input
16 for developing cost allocators?

17 Yes. Carbon/Emery Telecom could consider plant
18 as a possible cost driver to determine the accounting and
19 general allocator. If plant were to be used, gross plant
20 would be a better indicator than net plant because the
21 regulated entities use group asset depreciation per FCC
22 Part 32, whereas the nonregulated entities use single asset
23 straight line depreciation.

24 **Q. Is that sentence consistent with Carbon/Emery's**
25 **response on 6.2?**

1 A. It's a good question. We've had to define
2 single asset depreciation for the term used by both the
3 Division and ourselves, and now we need to probably clarify
4 it with the Office. It appears to be in conflict. The
5 methodology that we use doesn't take individual assets down
6 to a minute separation. A good example may be the
7 subscriber equipment that we talked about previously and
8 that Brock discussed briefly. Part of that subscriber
9 equipment is individual ONT's. It's the end piece of that
10 communication network. We don't capitalize every single
11 individual ONT. Similarly, on the nonregulated side the
12 equivalent may be set-top boxes. We wouldn't capitalize
13 individual set-top boxes, but we might capitalize a group
14 of them that were purchased in a year. So when you use the
15 term single asset, it may refer to a group of similar
16 assets that were purchased in a period. So the difference
17 between nonregulated and regulated side may be it's more of
18 a difference in the nature of that group than it is
19 strictly single assets.

20 So when we make the comment in this section of
21 the testimony, we're saying single asset, describing that
22 process that our nonregulated end uses. It doesn't get
23 down to minute single assets, which is where it becomes
24 burdensome and that's what the other testimony refers to.
25 But in this case it refers to a period of time or a group

1 of assets. And they're not -- that group doesn't span
2 multiple years and constitute a functioning network like it
3 would on the regulated side.

4 That may not have clarified it well for you. I
5 don't know if I'm answering the question fully the way you
6 want.

7 Q. Well, as Mr. Johansen said I'm just a lawyer
8 here and this is accounting. But it seems to me that you
9 stated in section 6.2 you use the term group asset
10 depreciation, saying it does use group asset depreciation.
11 And in your testimony you said that they don't use group
12 asset depreciation. Is this just being uncareful with your
13 terms?

14 A. No. I guess I feel like I've answered the
15 question. We've done the same thing with the Division in
16 pointing out their use of the term single asset doesn't
17 really result in a true single asset reputation and it's
18 the same clarification for us. The level that the Division
19 goes down to in defining single asset is really what is in
20 question here, but it's not a true single asset approach.
21 To get to the separation of every single asset is where it
22 becomes burdensome.

23 HEARING OFFICER: When you used the term single
24 asset separate line depreciation in your prefiled
25 testimony, is it equivalent or fairly equivalent to what

1 you've described as vintage group depreciation?

2 THE WITNESS: It would be vintage, but it would
3 be to a year level rather than to a two or three year
4 level. If you look at depreciation on -- if we can use the
5 term gray scale -- you could have a very theoretical and
6 pure single asset straight line method and then you could
7 get to the group method. Vintage, depending on how many
8 years you choose and how you group it, it would be
9 somewhere within that gray scale. Vintage is some level of
10 in between, between those two levels.

11 So the difference in definition here is to the
12 level it gets burdensome if it's very detailed minute
13 single assets approach, and it's not even what the Division
14 got to. It's more of a group of assets in a particular
15 year or -- generally it's a project. So it might be a
16 three month project where we have -- I don't know what a
17 good example would be. Say we have a small construction
18 build in one of our small towns and we capitalize that as a
19 project to -- it might have a couple different categories,
20 but it might need so many feet of fiber. So some of it
21 goes to buried cable and some to subscriber equipment so we
22 capitalize that. But we don't go down and capitalize every
23 single piece of subscriber equipment, we capitalize it as a
24 group on that project.

25 HEARING OFFICER: Mr. Moore.

1 Q. (By Mr. Moore) Just one more question. Is it
2 your testimony that what you termed in your written
3 testimony as single asset straight line depreciation is
4 equivalent to what you said in your discovery requests, you
5 described it as a group asset depreciation? Which one
6 would be a closer description to what the Division uses in
7 the single asset depreciation? Would it be closer to --
8 I'm sorry. Let me start over again.

9 For your nonregulated plant which you say does
10 use group asset depreciation, is that the same group asset
11 depreciation that you use in your general depreciation
12 adjustment?

13 A. If I understand the question you're asking, the
14 regulated -- I'm sorry. The nonregulated methodology that
15 we're using would be similar to what the Division is
16 proposing as single asset.

17 Q. All right.

18 A. So it's not --

19 HEARING OFFICER: And why do you not use the
20 same method for regulated?

21 THE WITNESS: This goes back to industry
22 practice and what has typically been prescribed by the FCC
23 and what is common in the industry. We view certain assets
24 in the network as a unit, as an operating network, and the
25 components of that network don't operate separately from

1 the other units of that network. So it operates as a
2 telephone network or as a buried cable plant network. So
3 we view it as one asset rather than pieces, a whole bunch
4 of pieces. This really kind of bears itself out.

5 There is copper and fixes that we may have done
6 in the last five years that will end up being replaced with
7 the fiber project that we're doing now. They may not last
8 the 20 year life that would be assigned to it. So when you
9 look at it as an operating network, if that operating
10 network becomes obsolete or it's replaced that entire asset
11 becomes obsolete and replaced.

12 HEARING OFFICER: I think I understand that.
13 You're going to have to forgive me because like many in the
14 room I'm an attorney and not an accountant. But you're
15 using the same network for both regulated and nonregulated
16 activities, correct?

17 THE WITNESS: We do cost separations to prevent
18 that from happening. The plant is used for -- so go back
19 to maybe Justin's question. It's not just internet and
20 phone. It's not that simple. The network carries a lot of
21 data. And basic local service isn't our largest revenue
22 source on the regulated side. We have special access. We
23 have data circuits. They are not internet circuits, they
24 are large circuits for Utah Division Network or for cell
25 phone providers. We have special access and switch access

1 transport where we provide a transport path for data and
2 phone calls coming out of Moab, and yet that isn't revenue
3 or those aren't customers directly in our area. So the
4 regulated plant provides service in a lot of different
5 capacities. That's why the core is required. I guess
6 maybe -- did I misunderstand what you're saying?

7 HEARING OFFICER: I'm going to speak just very
8 simply. I apologize if I'm oversimplifying. But when you
9 talk about, for example, a machine that might have some
10 older components and some newer components but it has to be
11 depreciated as a whole, my question is aren't you using
12 that machine for both regulated and unregulated activities,
13 and if you are then why do you depreciate it in one way for
14 your regulated activities, but depreciate it in another way
15 for your nonregulated activities?

16 THE WITNESS: It would only be capitalized on
17 one set of books. So it would be either a regulated asset
18 or a nonregulated asset. We don't split that asset in the
19 capitalization process. Then we have --

20 HEARING OFFICER: But in your testimony one of
21 your primary objections is that the Division's recommended
22 method of depreciation doesn't account for that split.

23 THE WITNESS: Maybe I'm not following the
24 question. I'm sorry.

25 HEARING OFFICER: Go ahead.

1 THE WITNESS: One of the things that you need
2 to be aware of too is our regulated plant has a much --
3 there is a different capitalization threshold. There are
4 items that we would normally expense on the nonregulated
5 side of our business that we may capitalize on the
6 regulated side of the business. That's dictated by the
7 FCC, and there are certain capitalization rules that we
8 follow there. To the extent that we don't have the
9 oversight in our nonregulated entities we may expense items
10 that don't need to be tracked to that individual level and
11 that minute level as well. So there is a difference in our
12 capitalization process and I testified to that as well.

13 HEARING OFFICER: Mr. Moore.

14 Q. (By Mr. Moore) Moving to your -- we're going
15 in this direction anyway -- to your cost separation
16 procedure through your CAM. Can you explain to the judge
17 what a CAM is?

18 A. It's a cost allocation manual. It provides the
19 basis for the allocation of shared costs.

20 Q. In your CAM you use only one -- in your
21 accounting and general -- can you describe what your
22 accounting and general driver is in your CAM?

23 A. It's originally based upon billing records.

24 Q. That's applied to the CEO, board of directors,
25 public relations and marketing?

1 A. Correct.

2 Q. And that led to dividing up the costs of 74
3 percent to the regulated operations and 26 percent to the
4 nonregulated operations?

5 A. The results of that allocation -- yes, that's
6 true, but only the costs that are subject to that
7 allocation. So it's a little bit misleading to say that
8 all the costs are allocated that way when you are only
9 dealing with the costs that are subject to that allocation.

10 Q. The costs that are subject to allocation are
11 your cost pools of the CEO, the board of directors, the
12 public relations and marketing; isn't that correct?

13 A. Correct.

14 Q. And the OCS has proposed a change allocation to
15 a 50/50 for the CEO and the board of directors and a 75
16 percent regulated and 75 nonregulated for public relations
17 and marketing, is that correct?

18 HEARING OFFICER: I think you said 75 and 75.
19 Did you mean 75 and 25?

20 MR. MOORE: It was 25 regulated -- it was 75 --
21 we changed it to 25 percent regulated and 75 percent
22 nonregulated.

23 HEARING OFFICER: Right.

24 THE WITNESS: It's a good question. Why I want
25 to separate or make a distinction on the costs subject to

1 the allocation, payroll and marketing may be a good one to
2 just to highlight one of the examples. This is true also
3 in the CSR area, which we'll discuss I'm sure here in a
4 minute.

5 We have certain areas of our serving area that
6 are only nonregulated in nature. So we have all of our
7 Moab area, it's a CLEC, it's nonregulated. The first step
8 in the allocation process is if there is cost directly
9 related to nonregulated operations we separate those out
10 and code them directly to nonregulated entities. This is
11 true whether it's CSR or marketing and public relations or
12 whatever the allocator may be. So there are different
13 levels of allocation that occur prior to what I would call
14 the leftover costs that are allocated.

15 When you look at any of these allocators you
16 have to look at what the end result is. Did we allocate
17 enough cost to the nonreg side or not. If we pulled out
18 certain sections of it and direct coded it, it's a little
19 bit misleading to look only at what is left in the
20 allocation and say we didn't do our job I guess. So you
21 need to say okay what was the final results of all the
22 costs and is it reasonable. And I think sometimes we get
23 so focussed on one allocator that we forget the allocation
24 process. We throw out the whole process instead of looking
25 at what the process resulted in rather than just what that

1 one allocator did.

2 **Q. Did you direct code any expenses for the CEO**
3 **cost pool?**

4 A. I would have to check. I'm not sure. I think
5 I could probably produce that number for you given 15
6 minutes or so if you want to take a -- the majority of the
7 board and the CEO are allocated.

8 **Q. Are allocated through --**

9 A. But I don't know that for sure how much is
10 direct coded.

11 **Q. But the majority of the amount?**

12 A. Yes, the majority.

13 **Q. Is that true of public relations and marketing?**

14 A. I wouldn't dare guess the exact number, but
15 probably 70 percent is subject to allocation. We do have
16 our Moab operation that are direct coded. So I'm not sure
17 exactly what that percentage would be.

18 HEARING OFFICER: The answer is some of
19 marketing is direct coded, but not all; is that right?

20 THE WITNESS: That's correct.

21 **Q. (By Mr. Moore) I'm a little confused. Your**
22 **allocation of 74 percent regulated and 26 percent**
23 **nonregulated, that's done after direct coding?**

24 A. Correct.

25 **Q. This direct coding, your CAM, you relied on a**

1 single cost driver of a number of billing records; is that
2 correct?

3 A. In the original application, yes. I've also
4 provided testimony to an examination of three different
5 cost drivers.

6 Q. That includes direct billing records?

7 A. Yes.

8 Q. But that's not part of your CAM. That's
9 something you just did after you read our testimony?

10 A. My CAM calculation, no. But the use of the
11 three resulted in essentially the same percentages that we
12 arrived at with using the billing records.

13 Q. Are you familiar with Mr. Ostrander's testimony
14 that 35 years experience he's never seen a single cost
15 driver of a number of billing records used for corporate
16 overhead in a CAM?

17 A. I read the testimony.

18 Q. Do you acknowledge -- isn't it true that no one
19 from Carbon was able to provide an example of a UUSF case
20 where a regulatory commission issued an order using a
21 single cost driver of billing records in their CAM?

22 A. I don't think we were asked to do so.

23 Q. Well --

24 A. Rephrase the question.

25 Q. Let me restate the question. Sitting here

1 today you can't point to a UUSF case where a regulatory
2 commission has issued an order using the single asset
3 driver of billing records in their CAM. Can you?

4 A. No, but the question is still vague to me. So
5 you're saying am I aware of any other case where there is a
6 single point CAM allocation -- actually I think it would be
7 fairly common. I can't cite cases, but the CAM -- there
8 may be an allocation that is based upon direct labor hours,
9 and that's a single point of allocation, or it may be it's
10 based upon -- I can't imagine that other companies don't
11 identify their drivers and make some sort of allocation and
12 that could be a single point driver.

13 Q. Yes, but that's not a billing record, the
14 driver that you used, is it?

15 A. The one I used was billing records, yes.

16 Q. Right. The example you just gave me you were
17 not using billing records in that example?

18 A. No, I agree.

19 Q. Isn't it true that data from the billing
20 records on the cost -- the data you receive from your
21 billing records is arrived from data from 2011, and not the
22 test year 2014?

23 A. That's correct.

24 Q. Are you aware that FCC Part 64 Section 46.903
25 of the FCC cost allocation procedures requires the

1 **allocation be current and updated annually on a consistent**
2 **basis?**

3 A. I am familiar with that section. And maybe a
4 point and important distinction needs to be made here. We
5 are actually exempt from the requirements of the CAM by
6 that section. So to the extent we have a CAM it's in --
7 actually it goes further than what is required in that
8 section for our size of company. The fact we don't have a
9 glossy manual or an index or cover page is not relevant to
10 the process which we have undertaken here.

11 Q. **So your testimony here is that your CAM is**
12 **exempt from Part 64 Section 54.903 of the cost allocation**
13 **procedures?**

14 A. I'm not saying that we don't use a similar
15 methodology or that we don't follow the affiliate
16 transaction rules described in that and the allocation
17 process described in that section. We do follow those.
18 I'm just saying the mechanics of the actual CAM are not a
19 requirement that we're -- we're not required to file that.
20 We do follow affiliate transaction rules.

21 Q. **Would you agree there has been significant**
22 **changes that have occurred in Carbon's operations since**
23 **2011?**

24 A. With Carbon's operations directly?

25 Q. **Yes. Including nonregulated, DSL, fiber**

1 **operations and increased revenues and expenses and plant**
2 **assets?**

3 A. Yes, there are changes every year. Some of
4 those changes are offsetting. We've seen continued
5 decreases we've demonstrated in our landlines, but we've
6 maintained steady or actually increased in some instances
7 in our special access, which has offset some of those
8 losses? So there is give and take in those. And our
9 billing records are somewhat reflective of those changes.

10 **Q. But you do not use the test year 2014 billing**
11 **records?**

12 A. No. We do testify the allocation is
13 representative.

14 **Q. You think it's representative. All right.**

15 MR. MOORE: I have some questions that may go
16 into some numbers related to the distinction between the
17 changes that occurred between 2011 and 2014. Would anybody
18 object if I took about five questions?

19 HEARING OFFICER: About numbers, dealing with
20 the confidential numbers?

21 MR. MOORE: Yes.

22 HEARING OFFICER: That's fine. We'll stop the
23 streaming. Go ahead.

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HEARING OFFICER: Go ahead.

Q. (By Mr. Moore) Those changes are not going to be reflected in your billing records, the number of billing records that constituted your allocation driver; is that correct?

A. That would be correct.

Q. In the billing records you have two types of billing records, general billing records and CAB records, which has a 25 percent gross; is that correct?

A. That's correct.

1 **Q. Could you explain what is meant by CAB records?**

2 A. It's carrier access billing records. We had to
3 weight those a little bit differently and there is a reason
4 why. If we included each line item of the accounts billing
5 it would overweight the CAB section significantly and
6 result in too much cost being allocated to the CAB side of
7 the house. So when you look at a CAB records in detail it
8 includes both terminating and originating special -- or
9 switch access records and these records are in the
10 millions.

11 So instead what we have done is we went back to
12 a summary bill for purposes of weighting the CAB records.
13 But because of the significant amount of time spent in CAB
14 related issues we weighted those records by 25 percent.

15 So what we did is look at them and said what
16 percentage of time do we spend in the tariff and rate
17 making process for our special access, how much time do we
18 spend working with interconnection agreements with long
19 distance or cellular phone service providers, how much time
20 do we spend looking at the regulated issues related to
21 CAB's and special access which is your 499 reporting with
22 the FCC and there is a great deal of compliance there.

23 To make sure CAB's gets a fair share of costs
24 we had to weight that a little bit more heavily. That was
25 a judgment call. Again, this is our cost allocation. We

1 try to do the best we can to determine what drives our
2 costs. And if we see a deficiency or a significant
3 overstatement in the driver that we're using, we'll try to
4 adjust that to be more reflective of what we feel is the
5 appropriate level of cost allocation.

6 One thing with respect to CAB is we also have a
7 CAB allocator specifically to address time spent that I
8 would say was more direct coded to CAB. So this is one of
9 the administrative functions. This would be myself and
10 Brock, the CEO time, the board time. That's to deal with
11 these additional issues related to special access and to
12 our carrier access billing system.

13 **Q. My understanding when you talk about the CAB**
14 **billing section, you're talking about billing from other**
15 **carriers using your plant, your equipment? If someone is**
16 **calling from Paris to Carbon there would be a CAB bill in**
17 **regards to that?**

18 **A. Yes. To clarify, it's not us billing for other**
19 **carriers. We don't do billing and collection for other**
20 **carriers. I think we stopped that 15 years ago. But it's**
21 **the billing to the carrier to access our network. So if**
22 **AT&T carries that call from Paris to Price, Utah there is a**
23 **portion of our network that AT&T had to use to access our**
24 **customer. So we would bill AT&T for the use of our network**
25 **for that small portion that we have within that call**

1 stream.

2 Q. That's the basic concept of CAB?

3 A. Correct.

4 Q. All right. You do not -- as I understand your
5 testimony you do not have any specific time or motion study
6 or any other study to come up with the 25 allocator or
7 gross number?

8 A. Specifically related to Brock's time and CEO
9 time, that's correct.

10 Q. Did you provide any specific information about
11 how you developed your net weighing factor?

12 A. The CAB weight function?

13 Q. Yes.

14 A. No. I didn't provide support to that. Just my
15 verbal text within the CAM and then as asked or -- I guess
16 it's not part of this proceeding, but we have discussed
17 that with the Division and Office.

18 Q. Do you agree an allocation factor or driver
19 must have a direct causal relationship to the expenses they
20 are allocating to?

21 A. That they should or that they do?

22 Q. That they should. That's the purpose of it;
23 isn't that correct?

24 A. Ideally, yes. If it's direct causal effect
25 that is a better allocator than an indirect causal effect.

1 **Q. What is your understanding of the term direct**
2 **causal relationship?**

3 A. If it's directly related my understanding it
4 would be either directly tied or close enough of a tie to
5 be considered direct. I don't know what the best example
6 to use here would be. But if we're talking about billing
7 records, and there are certain line numbers on a phone bill
8 that represent significant compliance or significant work
9 for the CEO or our board, then I would say that cost is
10 fairly reflective of the work that is being performed. Is
11 it the only driver of cost, no. Is it possible that direct
12 coding could be done in some instances, yes. But to say
13 that it doesn't relate is not true. To say that it's the
14 best allocator basis is probably also not true. But we do
15 the best we can to determine a method of allocation. So we
16 go through the process to try to do that and then we step
17 through it.

18 There is a hierarchy described in Part 64 that
19 we discussed of how to approach these matters and we apply
20 that. We look at the ability to direct code. We look at
21 direct association of costs. Lower on the hierarchy is the
22 use of the general allocator, like revenue or expenses.
23 It's lower on the threshold. So we do examine those when
24 we're making our cost allocators.

25 **Q. Now let's look at the CEO cost pool.**

1 Mr. Johansen doesn't keep daily timesheets indicating how
2 much time he spends on regulated and nonregulated
3 operations; isn't that true?

4 A. That's correct.

5 Q. If he did it would make this much easier?

6 A. If he direct coded?

7 Q. Yes.

8 A. Yes. Then there would be no need for an
9 allocator, that's correct.

10 Q. The CEO cost pool has various types of expenses
11 associated with it, including salary, benefits, cost, cell
12 phone, NECA and URTA dues; is that correct?

13 A. Correct.

14 Q. By way of example, how would an increase in CAB
15 bills in 2011 have direct causal relationship to NECA and
16 URTA dues?

17 A. I guess if we're looking at NECA and URTA dues
18 those should probably be direct coded 100 percent reg.
19 We've probably given too much nonreg side on those to begin
20 with. So let's start from that standpoint. We may have
21 included cost in the pool that should have been 100 reg.
22 So I'll have to look at that. We may need to either adjust
23 for direct cost on some of those that we see or -- but the
24 answer to your question, what is the direct causal
25 relationship, the amount of billing line items associated

1 with the phone bill versus an internet bill -- I don't know
2 that -- just picture in your mind what you get at home on
3 your phone bill maybe. But under the phone section you'll
4 have 911 --

5 **Q. Excuse me. I don't know if this is responsive.**

6 A. I guess what I'm saying though is that all
7 those regulatory matters, a lot of them are dealt with in
8 the NECA arena and allocate interstate costs and compliance
9 and FCC compliance and tariff and rate making with each of
10 those line items that are reflected in the billing there is
11 a relationship there. Now is it the best relationship, I
12 don't know. I testified that there are other methods that
13 we can use. I'm saying they're not unrepresentative or
14 they're not unreflective.

15 **Q. They're not unreflective. All right. The same**
16 **would be true for an increase in CAB bill and possibly the**
17 **CEO phone bill, mobile phone bill?**

18 A. Yes. So if we have -- we have to file tariffs
19 with the FCC every two years. A significant amount of time
20 is spent by myself and Brock. We file -- we deal with
21 regulatory change issues constantly and those are reflected
22 on our bills in the form of CAB surcharges or subscriber
23 line charges. Again, we deal with interconnection
24 agreements that affect those phone bills on the CAB side of
25 the house as well. And Brock spends time on those issues.

1 And those are the issues, especially recently with all the
2 regulatory changes that are going on. A high percentage of
3 Brock's time is associated with those types of changes.

4 We spent a significant amount of time in
5 Washington trying to push through a waiver with the FCC
6 this year. I would suggest that 74 percent is pretty
7 reasonable for the amount of time that is spent on
8 regulated operations.

9 Our fiber to the home project similarly is
10 taking a lot of attention in our --

11 **Q. I'm sorry. I'm going to have to object again**
12 **for being nonresponsive. I'm trying to get specific here**
13 **about your specific -- how your billing records**
14 **specifically relate and constitute cost causative**
15 **relationships between the number of expenses in the CEO**
16 **pool and --**

17 **A.** If I bill a tariff cost, then that means I've
18 had to prepare a tariff. If I bill a tax, that means I
19 have to prepare a tax return. If I bill a 499, a USAC, I
20 have to prepare those forms. And that's all regulated.
21 There isn't any tax on an internet charge. There is very
22 little compliance associated with that. I don't have to
23 file a tariff every two years on my internet charges. I
24 rarely have to address that ever.

25 **Q. Do you have to file the tariff every time you**

1 **have a CAB bill?**

2 A. No.

3 **Q. Do you have to go and work with -- what was the**
4 **other example you used?**

5 A. I'm saying that it's representative of the time
6 we spend regulated versus nonregulated on all the issues
7 that are related to those billing line items. So to me it
8 is the causal relationship. I don't understand I guess how
9 it couldn't be. I guess -- is there testimony that shows
10 that there is no relationship there? You guys say there
11 isn't, but why wouldn't there be? We have the burden of
12 proof and we've tried to demonstrate and describe why we
13 think those are related and I think we've done that.

14 HEARING OFFICER: Mr. Moore, I think --

15 THE WITNESS: I can go into more detail. We
16 can throw a photo up on the wall. I can throw up the exact
17 billing records and we can see what is involved with them.

18 HEARING OFFICER: I think it might be easier
19 for me to understand the point that you're trying to make
20 through the questioning of your own witness.

21 MR. MOORE: All right.

22 HEARING OFFICER: All right.

23 **Q. (By Mr. Moore) Mr. Ostrander testified that**
24 **the CEO, and for that matter the board of directors, would**
25 **most likely spend a significant amount of time on forward**

1 **looking projects. Do you dispute that?**

2 A. It's a combination of both. In any -- I would
3 say the board time is directly tied to Brock's time because
4 the issues that Brock deals with are the issues we discuss
5 in our board meetings. So if time is spent in a particular
6 area basically that time is reflective in our board
7 meetings. So those two are very closely tied together.

8 There is an aspect to forward looking projects,
9 yes. That is also reflective of billing records. They've
10 gone a little bit of a lag. But when we build a new
11 circuit, let's say a CAB circuit out to a cell phone tower,
12 the weighting of that would probably -- if it's in our
13 area, in our regulated area, it's going to pull a little
14 bit of cost to the regulated side. If it's in an
15 nonregulated area it pulls costs to the nonregulated side.
16 But associated with that build is the actual construction
17 that Brock is intimately involved with with the plant side
18 to make sure that construction occurs, and again with
19 forward looking plans as well. So yes.

20 **Q. So yes, you do spend a significant amount of**
21 **time, the CEO and the BOD board, reviewing future plans?**

22 A. We do spend time. The definition of
23 significant I guess we would have to define that.

24 **Q. So it would depend on year to year I guess?**

25 A. Right.

1 Q. And from 2011 to 2014 it would be different?

2 A. Correct.

3 Q. If the CEO spends time on forward looking
4 projects that don't come to fruition until another year,
5 there would be no billing records to reflect that in the
6 test year; isn't that correct?

7 A. Yes, but is the existing customer reflective of
8 that effort. I guess you're demonstrating that we're not
9 keeping that up to date enough; is that correct?

10 Q. Yes.

11 A. I guess if this is the only issue that we're
12 dealing with I can rerun the records and we could look at
13 it. We updated that allocator in 2015, this year, and it's
14 not significantly different. I can give you updated
15 numbers if that's what you're getting at.

16 Q. Why don't we just stick with the record we have
17 right now.

18 A. That's fine, but I'm saying we do adjust these
19 allocators from time to time. And I can pull up our
20 existing one and it would be based on newer records. It's
21 not going to be a huge shift from what we have now. I
22 would be happy to do that if that's where we're headed on
23 this.

24 Q. I'm sorry. Are you saying you want to use a
25 different allocator than the allocator you have in --

1 A. No, I think it's representative. I'm just
2 saying there is not a big smoking gun here. If we change
3 from 74 percent to 72 percent I would be surprised. I can
4 pull that number if we need to. I don't know. It changes
5 over time, it does. But this number was based upon the
6 fall of 2011. The allocator that was in place at the
7 beginning of 2014, there is a two and half years separation
8 there. Is it significant? If we update it to the 2015
9 records and took a look at it, it wouldn't be significantly
10 different.

11 **Q. But you haven't done that?**

12 A. I have done that. I don't have them with me
13 today. But that's what I'm saying, I can pull that and
14 give it to you and give it to the court today if we need to
15 if that satisfies the concern here.

16 **Q. Let me turn to your public relations and**
17 **marketing allocator. You list 74 percent of your total**
18 **hour costs to regulated service and only 26 percent to**
19 **nonregulated service; is that correct?**

20 A. That's not correct.

21 **Q. What is correct?**

22 A. The correct is we direct allocate a significant
23 portion of costs before we get to that allocator. The
24 costs that are left with that allocator are then allocated
25 upon the percentages you just stated.

1 Q. What are the costs that are left?

2 A. It would be costs that are in the shared areas
3 of service. So that would be within the combined service
4 areas of Carbon/Emery Telecom, Emery Telecom and
5 Hanksville.

6 Q. In your response to OCSDR34 you said your
7 allocation factor was reasonable because regulated services
8 benefit from the company's advertising for bundle services;
9 is that correct?

10 A. Correct.

11 Q. You have one regulated service of basic phone
12 service and two regulated services of internet and another
13 regulated -- nonregulated service, excuse me, of internet
14 and another nonregulated service IPTV; is that correct?

15 A. That is not correct.

16 Q. Why is that not correct?

17 A. We don't provide IPTV services.

18 Q. But for bundle services of regulated phone
19 service, and let's take your position of internet, you
20 still charge the 74/26 percent for that?

21 A. I'm sorry. Please repeat the question again.

22 Q. When you advertise your bundle services, which
23 according to you, your testimony here is bundling regulated
24 phone service with unregulated internet, you still use the
25 74 percent allocation to regulated service, the basic phone

1 services, and the 26 nonregulated services, the internet
2 services, correct?

3 A. If that service is offered to our regulated
4 area, yes, that would be true.

5 Q. But internet is not in your regulated area? I
6 mean, internet is a nonregulated operation?

7 A. Service provided within that same area,
8 correct, inside the serving area.

9 Q. Most of these customers in the service area --
10 let me just go back here. Does Carbon have any competition
11 for basic phone services in the service area?

12 A. With the exception of cell phones, no.

13 Q. Isn't it true these customers that you're
14 advertising your bundle services for generally already have
15 local phone, basic phone service?

16 A. No, that's not necessarily true.

17 Q. But the majority of them?

18 A. No.

19 Q. Who do you advertise to?

20 A. We advertise to basically all the residents of
21 the Carbon/Emery counties and Moab. Again, the Moab
22 serving areas are directly coded to our nonregulated
23 entities. Moab services include phone, internet, cable TV.
24 Then in our regulated areas we have similar services that
25 are offered both on our nonregulated plan and on our

1 regulated plan. Those services are all advertised to the
2 residents and businesses of that serving area.

3 HEARING OFFICER: I'm sorry. You said the
4 direct allocators are done by geographic area?

5 THE WITNESS: By serving area, yes. We operate
6 as an incumbent local exchange carrier in Carbon/Emery
7 counties and in the Hanksville area. We operate as a
8 competitive local exchange carrier in the Moab area as well
9 as those services we also provide internet and cable TV.

10 HEARING OFFICER: In the areas where you're the
11 ILEC you do the 74 percent allocation to regulated, and the
12 areas where you're CLEC you do 100 percent to nonregulated?

13 THE WITNESS: That's correct.

14 HEARING OFFICER: And there is no additional
15 allocation?

16 THE WITNESS: No.

17 Q. (By Mr. Moore) Isn't it true that the internet
18 is significantly more profitable to Carbon than basic phone
19 service?

20 A. Yes.

21 Q. So when you advertise the bundle service you
22 have two services, one regulated which is not as profitable
23 as the other nonregulated, correct?

24 A. That's correct.

25 Q. But you allocate the costs associated with this

1 bundle approximately three times higher on the nonregulated
2 side than you do to the -- backward, to the regulated side
3 than you do to the nonregulated side?

4 A. We do those allocations at 74 percent, yes.

5 Q. Do you think it's reasonable that the
6 advertising -- let's take one step back. If you have two
7 services, phone and internet, wouldn't it make more sense
8 to divide them up at least 50/50?

9 A. Is the phone being provided over regulated
10 plant or nonregulated plant?

11 Q. Let's take the regulated plant first.

12 A. Okay. We closely tie those. And the reason
13 why is is the loop used by the customer to provide phone
14 service to that customer. The regulated side benefits from
15 the internet usage of that phone line. It actually sures
16 up the phone line. The phone line has become super
17 critical for us to maintain both federal and state funding
18 and it is critical to our customers and our ability to
19 serve the customers is dependent upon the healthiness of
20 that. We continue to promote those lines, continue to tie
21 the bundles closely with the phone line and the reason why
22 we do is because we understand that there is -- out of the
23 two products, the internet definitely would be the most
24 desirable or the most popular thing to have versus the
25 traditional phone line. But all of our advertising -- the

1 majority of the advertising I should say includes that
2 bundle to tie to that regulated plant. So I guess it's not
3 an easy question to answer because the ads aren't
4 separated, they're tied together.

5 Q. That's my problem with your separation. It
6 seems if we take the position you have of two services and
7 you're advertising primarily for the internet, which is the
8 more profitable aspect, why would the cost for that
9 advertising be allocated 76 percent to regulated plant and
10 24 percent to nonregulated when you're advertising for the
11 nonregulated and that's where your profit is going to come
12 from?

13 A. Let's switch that example up a little bit.
14 Let's move that to cable TV. Cable TV we don't make money
15 at.

16 Q. I'm sorry. I'm going --

17 A. Are you saying --

18 Q. -- to object as nonresponsiveness again. We'll
19 be here forever.

20 A. The ability to pay shouldn't be the basis for
21 the allocation. So if the company is profitable it doesn't
22 mean they should get more allocation cost.

23 Q. The cost --

24 A. Let's take profitability out of the question
25 and then reask the question. It's not based upon the fact

1 that the cable company makes no money and the internet
2 company makes money. I mean if we switch up the example
3 and say can our cable company afford advertising, no. They
4 don't make any money. So it's not an ability to pay that
5 drives the cost. It's the actual advertising. If we're
6 getting to the root of the question, let's make sure we do
7 that.

8 **Q. But you're advertising primarily for internet?**

9 A. We advertise for both.

10 **Q. But primarily for internet. That's what the**
11 **people want to purchase?**

12 A. No, no. Internet kind of sells itself. We
13 have to focus on -- we have to focus on telephone, to keep
14 telephone numbers up. We have to show our customers why
15 it's important to maintain the phone, for safety a line
16 power in an emergency situation is going to be more
17 reliable than cell phone. We spend significant time
18 educating our customers that way. We also have
19 requirements annually and ongoing to advertise life line
20 services which is promoted by the state. There is no
21 requirement for life line internet services. So we have
22 additional advertising that has to be done separately and
23 distinctly for life line. We do that through newspaper.
24 We do that through our website. We have to post posters
25 and --

1 **Q. Objection, nonresponsive. I didn't ask about**
2 **life line. I asked about advertising for bundle services.**

3 A. It's phone service. Life line is phone service
4 and we have to advertise for it. This is all part of that
5 cost we're allocating. It goes to the question what are we
6 doing with our advertising dollars. There is a lot of
7 things that go to the advertising dollars.

8 MR. MOORE: I have no further questions.

9 HEARING OFFICER: Ms. Slawson, any followup?

10 MS. SLAWSON: Would it be possible to have a
11 quick break?

12 HEARING OFFICER: Sure, that's fine.

13 (Off the record.)

14 HEARING OFFICER: We're back from our break and
15 back on the record.

16 MS. SLAWSON: Thank you. Time for redirect?

17 HEARING OFFICER: Yes, go ahead.

18 REDIRECT EXAMINATION

19 BY MS. SLAWSON:

20 **Q. Let's see. My first question is can you tell**
21 **me what you consider the affected period of the UUSF**
22 **application that Carbon/Emery has made in this case?**

23 A. I would say between three and five years.

24 **Q. You talked a little bit about -- this is back**
25 **on the first question that was presented by Mr. Moore with**

1 regard to the testimony on single asset versus group asset
2 depreciation. You testified briefly there is a
3 capitalization threshold difference. Can you explain to us
4 why does the capitalization threshold differ between the
5 regulated and nonregulated companies?

6 A. The threshold is established a little bit lower
7 in regulated cases generally to allow for or prevent I
8 should say, prevent the expenses from spiking in one year.
9 If you were to expense certain items rather than capitalize
10 them, you may have a year that is overstated by that
11 expense. Whereas, capitalizing that same item, spreading
12 it over a useful life, would smooth that expense. So to
13 prevent spikes in the operations and the reporting of that
14 operation.

15 With respect to the nonregulated entities
16 that's not as big of a concern because it's not subject to
17 a rate making process. A spike that would be material to a
18 regulated entity could be considered nonmaterial for this
19 nonregulated entity. Maybe a good example would be modems
20 for the internet on the nonregulated side. We have
21 significant purchases of those modems. They do have a
22 three to five year life on them. But rather than
23 capitalize those and track those in our asset records for
24 five years each one of those modems, or even groups of
25 modems, we go ahead and expense those groups of modems.

1 And because there is no associated rate making or reason to
2 kind of normalize those expenditures, if that expense
3 policy spikes our cost for modems in any one given year
4 it's not material to the financial statements as a whole
5 and so it's not considered necessary to track down to that
6 level.

7 So that's kind of how we apply the
8 capitalization policy. Once we meet that threshold then we
9 get into that gray scale area that I talked about how you
10 group those assets, whether it's single asset or a group of
11 assets and what constitutes those groups and what point do
12 you segregate the groups based on vintage or based upon the
13 type of plant, that type of thing.

14 So I think there is a distinction there, first
15 in the policy, and then within the policy, is it true
16 single asset or is it a group. And so when I compared our
17 nonreg entity capitalization similar to what the Division
18 shows, there is a little bit of distinction, you have to
19 get past that first capitalization threshold first. So we
20 just capitalize less on the nonreg side. Then when we do
21 it it follows somewhat close to what the Division is
22 recommending on their straight line policy. I think maybe
23 -- you might go ahead with the questions. Sorry.

24 **Q. I guess what I'm wondering is could the**
25 **regulated company, Carbon/Emery, adopt the Division's**

1 proposed method of depreciation, this kind of single asset,
2 maybe vintage, not true single asset, but method of
3 depreciation?

4 A. It could. And generally what it requires from
5 the interstate side is permission from FCC we found that
6 the FCC has been a little bit lenient in granting to the
7 states some leeway in the methodology. So we feel like it
8 is a methodology that could be adopted. The issue that we
9 take with the methodology isn't necessarily the method
10 itself, but the implementation of it. We have provided
11 testimony that if we're going to go that direction what the
12 Division is proposing then we need to have a transition to
13 that methodology. It can't just be a calculation of a
14 historical number and then use that number. We need to say
15 okay this has changed and we're going to transition to it.
16 So we've provided some testimony to what we think that
17 transition would look like.

18 Q. How do you see that transition?

19 A. What we have proposed is that -- our books are
20 still open for 2015. So we have a little bit of leeway on
21 how we report depreciation. We could do some extent of
22 restatement, but what we've proposed is that -- basically
23 from the time frame that we knew that the Division had a
24 concern with our methodology, if we restated the assets
25 from that point going forward it would be basically January

1 1, 2014. So if we at that point cut to a single asset
2 straight line methodology as promulgated by the Division at
3 this point and then allowed our existing groups as of
4 12/31/2013 to continue and run their course, let the
5 depreciation finish out on those assets, and then project
6 that forward, that would be the transition that we would
7 suggest. And the projection forward is somewhat necessary
8 to determine what the correct number is in this proceeding
9 because it is a change from the methodology that we're
10 using now.

11 Now I guess without getting into the
12 confidential numbers again, that number would be slightly
13 less than what we projected in our application, but it is
14 materially close to that number. So there may be a slight
15 reduction there, but not significant.

16 We think that satisfies the concerns of the
17 Division going forward, but it also allows us a transition
18 period into that. A lot of our decisions with respect to
19 how we manage our books are based upon the certainty that's
20 provided by the FCC and by the state. So if those things
21 change it would change the decisions that we would make
22 regarding the timing of the investments or how we -- I
23 guess how we would make decisions based upon rate of return
24 and weigh those decisions against similar decisions that
25 we're making on our nonregulated plant.

1 So it's a choice scenario for us. Where do we
2 put our new capital dollars this year. What type of rate
3 of return are we going to get. Is that rate of return
4 guaranteed or how much risk is involved with that rate of
5 return. These capital type decisions are dependent upon
6 some consistency. That's what we're --though we're not
7 opposed to the methodology, we are opposed to the way it is
8 being proposed in the findings. We would like some sort of
9 transition or methodology to get to where they want us to
10 be.

11 **Q. We had a series of questions about the cost**
12 **allocations, the various allocations that you have made. I**
13 **want to ask you the allocators that you have identified,**
14 **those are used to allocate costs; is that correct?**

15 A. Correct.

16 **Q. Does revenue correlate or is it representative**
17 **of costs?**

18 A. No.

19 MS. SLAWSON: I have no other questions.

20 HEARING OFFICER: Any recross?

21 MR. MOORE: No.

22 MR. JETTER: No recross from the Division.

23 Thank you.

24 HEARING OFFICER: We just have a couple of
25 minutes before the public witness portion of this hearing

1 is supposed to begin. It's only been a few minutes since
2 our last break, but let's go ahead and break until noon and
3 we'll see if anybody appears. If not, we'll go ahead and
4 continue unless someone appears.

5 (Off the record.)

6 HEARING OFFICER: We are back on the record and
7 I am ready to begin the public witness hearing, which is
8 scheduled for today at noon. Is there anyone here in the
9 room who would like to give comments or provide testimony
10 as a public witness today?

11 We are going to go ahead then and resume with
12 our UUSF hearing for the next hour or so. We'll kind of
13 keep a watch to see if anybody comes in to give a comment
14 as a public witness. Then at 1:00 we will break for lunch.
15 So Ms. Slawson, go ahead and you may call your next
16 witness.

17 MS. SLAWSON: Thank you. Carbon/Emery calls
18 Douglas Meredith.

19 (The witness is sworn in.)

20 DIRECT EXAMINATION

21 BY MS. SLAWSON:

22 Q. Good after, Mr. Meredith. Would you state your
23 name, your employer and your business address for the
24 record?

25 A. Yes. My full name is Douglas Duncan Meredith.

1 I am employed by the firm John Staurulakis Incorporated.
2 That is spelled S-T-A-U-R-U-L-A-K-I-S. My business address
3 is 547 Oakview Lane, Bountiful, Utah. That's my office.
4 The headquarters for JSI is in Greenbelt, Maryland.

5 Q. On behalf of the applicant Carbon/Emery Telecom
6 Inc. have you participated in this record?

7 A. Yes.

8 Q. Did you prepare prefiled rebuttal and
9 surrebuttal testimony and exhibits in this case?

10 A. Yes.

11 Q. Do you have any substantive changes to the
12 answers you gave to the questions asked in the prefiled
13 testimony?

14 A. No.

15 Q. Do you have a summary of your testimony that
16 you would like to present us with?

17 A. Yes.

18 Q. Please go ahead.

19 A. Thank you. In my rebuttal and surrebuttal
20 testimonies I address two topics: Carbon/Emery's
21 authorized rate of return and the appropriate depreciation
22 method to use, and in the alternative of using that method
23 what transition should be used to move to a new
24 depreciation method for Carbon/Emery.

25 Topic one, rate of return. I will summarize

1 first the authorized rate of return for Utah USF purposes.
2 My testimony and the exhibits I supply support
3 Carbon/Emery's proposed overall authorized rate of return
4 of 10.5 percent. For comparison, the current authorized
5 interstate rate of return for Carbon/Emery is 11.25
6 percent.

7 I examine in my testimony the following items
8 related to the calculation of the overall rate of return.

9 Item one, capital structure. The overall rate
10 of return is calculated using a hypothetical capital
11 structure. The Division and Carbon/Emery recommend that
12 the Commission adopt the Division's sliding scale capital
13 structure result. This method was developed by an industry
14 task force that has been used frequently by the Division.
15 This method represents a reasonable balancing of competing
16 interests. The capital structure for Carbon/Emery assumed
17 by the Division's sliding scale is 65 percent equity and 35
18 percent debt. The Office takes exception to the Division's
19 long-standing practice and recommends a 50 percent equity
20 and 50 percent debt capital structure. I recommend the
21 Commission continue to use the Division's sliding scale
22 method and adopt a 65 percent equity and 35 percent debt
23 capital structure for Carbon/Emery in this proceeding.

24 Item two, the appropriate interstate rate of
25 return. By Commission rule, companies are instructed to

1 use in its application the applicable NECA form 492A for
2 the most recently available year. I supply the NECA form
3 492A as an exhibit and the applicable form for Carbon/Emery
4 yields a 11.45 percent interstate rate of return. The
5 Division initially proposed an incorrect rate and
6 subsequently revised its number. The Office recommends
7 using a NECA form 492A that does not apply to Carbon/Emery.
8 NECA applies two forms 492A based on individual company
9 participation in NECA cost pools. I recommend the
10 Commission use the applicable form 492A in my exhibit for
11 Carbon/Emery which reports a 11.45 percent overall rate of
12 return for interstate purposes.

13 Item three, the appropriate intrastate rate of
14 return. Carbon/Emery, the Division, and the Office agree
15 on the cost of debt used for intrastate rate of return
16 calculations. This leaves the intrastate cost of equity or
17 return on equity as a disputed item. The Division uses an
18 unadjusted capital asset pricing model, CAPM, to calculate
19 an intrastate rate of return for Carbon/Emery. The
20 Division does not see any other model alternative available
21 for use. I rebut the Division's claims suggesting that an
22 unadjusted CAPM is not appropriate. I provide facts from
23 credible capital finance authorities which support the need
24 to adjust the textbook version of CAPM in the telecom
25 sector. In the exhibits I provide that address telecom

1 issues specifically, Drs. Heaton and Billingsley
2 specifically examine the telecom industry and address this
3 issue. These authorities recommend adjusting the textbook
4 version of CAPM for telcos.

5 Dr. Heaton, in Exhibit 1, states that a small
6 company premium is the minimum adjustment that should be
7 applied when using the CAPM for real world applications.
8 Dr. Billingsley, in Exhibit 2, recommends a small company
9 premium developed by well established financial service
10 research firms, such as Ibbotson & Associates or Duff &
11 Phelps. These exhibits are unrebutted in this proceedings.

12 I provide another analysis filed at the FCC in
13 Exhibit 3 which the Office takes exceptions to based on its
14 author.

15 I explain on alternative to the CAPM that was
16 proposed by Dr. Glass, formerly of NECA and now of Rutgers
17 University, to overcome the common pitfalls of the
18 discounted cash flow method. This method proposed uses a
19 free cash flow approach instead of the discounted cash flow
20 approach. This information is located in Exhibit 2. The
21 benefit of this approach is that Dr. Glass uses actual
22 rural telephone company data rather than large company
23 peers to develop the appropriate discounted cash flow rate.
24 I update this data in Exhibit 5. The Division remains
25 silent on this alternative approach and the Office provides

1 no rebuttal on this method.

2 The Office argues that the Utah Commission
3 should adopt the results from a number of Kansas decisions.
4 I respond by recommending the Commission give them very
5 little, if any, weight.

6 There are serious mechanical problems with the
7 Division's selection of publicly traded companies and the
8 calculation of the risk free return used in its CAPM. I
9 identify these problems and propose solutions for them.

10 All of this data and analysis support the 10.5
11 percent overall rate of return proposed by Carbon/Emery.
12 And I recommend the Commission adopt the proposed and
13 supported 10.5 percent overall rate of return for
14 Carbon/Emery in this proceeding.

15 Topic two, depreciation method. I will briefly
16 summarize the depreciation method proposed by the Division
17 and Carbon/Emery. The Division seeks to change the
18 standard and industry accepted group asset straight line
19 depreciation method used by Carbon/Emery for Utah USF
20 purposes. I observe that this approach will add
21 administrative complexity to Carbon/Emery's accounting
22 procedures. And in making such a change it should be fully
23 vetted to ensure that the public interest is served. The
24 claims made by the Division are not fully explained.
25 Notwithstanding, if the Commission were to adopt the

1 Division's method, I recommend the Commission adopt this
2 monumental policy change on a prospective basis for new
3 assets that are purchased and placed into service. The
4 test year 2014 is representative of forecasted depreciation
5 expense for the next five years and so the transition that
6 I describe is in the public interest. This concludes my
7 summary.

8 MS. SLAWSON: Mr. Meredith is available for
9 cross examination.

10 HEARING OFFICER: Mr. Jetter.

11 CROSS EXAMINATION

12 BY MR. JETTER:

13 Q. Thank you. Good afternoon, Mr. Meredith. I
14 have a few questions and they're a little bit disjointed as
15 far as we'll skip around just a little bit. I would like
16 to just start out discussing the risk free rate of return.
17 I'm looking at CE-4.0R, which is your revised rebuttal
18 testimony dated September 4, 2015. And specifically I'm
19 addressing your discussion of the risk free rate of return
20 beginning on lines 271 through 279. Is it an accurate
21 representation of your testimony there that you believe the
22 better more accurate risk free rate of return to use in
23 calculation of an ROE for this specific purpose is an
24 average from 1990 through today?

25 A. That's what I have used. I observe that the

1 Division proposed a spot rate, which as I understand it was
2 a rate on a particular day. I propose that that be trended
3 a bit. I used 1990, 25 years from when this was prepared,
4 but 20 or 25 would be an appropriate trending of the risk
5 free rate.

6 Q. Were you in this room about 30 minutes to an
7 hour ago when Mr. Woolsey testified about what he believed
8 to be the term for which we would apply the findings of
9 this particular case?

10 A. Yes. The effective period of the findings,
11 yes, I was.

12 Q. Do you agree with him that it would be three to
13 five years?

14 A. Yes, that's my understanding is that it would
15 be a three to five years effective period.

16 Q. And it's still your testimony that using a 20
17 to 25 year trend of Treasury Bill average equally weighing
18 for each year over that time is a better choice than the
19 current actual risk free rate?

20 A. Yes, I do.

21 Q. I would like to jump a little bit now here to
22 the factors that you discussed in promoting the -- in
23 discussing the premium that you would assign as a small
24 company premium to Carbon/Emery. In support of that is it
25 correct, I believe it's lines 120 through 121 of this same

1 **exhibit, that you rely on Morningstar/Ibbotson Annual**
2 **Yearbook?**

3 A. No, my sources for relying on the premium are
4 related to Dr. Heaton and Dr. Billingsley. The
5 Morningstar/Ibbotson Yearbook or the Morningstar/Ibbotson
6 source and also Dr. Billingsley as I mention in the summary
7 used the Duff & Phelps report that is identified on line
8 142 of my testimony.

9 Q. **Let me direct you beginning at line 120 on page**
10 **5. Would you please read the first sentence in that**
11 **paragraph?**

12 A. Yes. The Morningstar/Ibbotson Annual Yearbook
13 routinely reports an adjustment that would be applied to a
14 company based on market capitalization.

15 Q. **Is that publication something that is a**
16 **reliable source for information on this type of item?**

17 A. Yes. Morningstar/Ibbotson or Duff & Phelps are
18 established research firms. Yes, they are.

19 Q. **Thank you. Are you aware of what companies**
20 **that the Morningstar/Ibbotson Annual Yearbook uses to**
21 **calculate its small company premium?**

22 A. Not specifically, no.

23 Q. **To be more specific, are you aware if any of**
24 **those companies have a government run program that**
25 **subsidizes those programs in the event that they're not**

1 **earning their authorized rate of return?**

2 A. No, I don't know any specifics about the
3 companies or their operations.

4 Q. **And such a type of government program would**
5 **produce the risk to those companies; is that correct?**

6 A. Can be, yes.

7 Q. **I would like to hand you a photocopy of the**
8 **2015 Ibbotson SBBI Classic Yearbook and this is page 113.**

9 MR. JETTER: May I approach the witness?

10 HEARING OFFICER: Yes.

11 MR. JETTER: This is not on my exhibit list.

12 We can enter this as DPU Cross Exhibit 1.

13 HEARING OFFICER: Any objection?

14 MS. SLAWSON: No.

15 MR. MOORE: No.

16 HEARING OFFICER: DPU Cross Exhibit 1?

17 MR. JETTER: Yes.

18 HEARING OFFICER: Go ahead.

19 Q. **(By Mr. Jetter) I think this will somewhat**
20 **confirm what you have just answered, but would you please**
21 **read what I have highlighted in yellow, a paragraph which**
22 **is on the upper right hand corner of page 113 of that**
23 **publication?**

24 A. Yes. This is page 113. I don't have the title
25 of the document, but it is page 113. Most criticisms of

1 the use of the size premium do not address the underlying
2 reason for its existence. Small cap stocks are still
3 considered riskier investments than large cap stocks.
4 Investors require an additional reward, in the form of
5 additional return, to take on the added risk of an
6 investment in small cap stocks. It is unlikely that in the
7 future investors will require no compensation for taking on
8 this additional risk. That's the end of the paragraph.

9 **Q. Thank you for reading that. And you testified,**
10 **is that correct, just a few moments ago that a program like**
11 **the State Universal Fund for Utah reduces the risk that**
12 **Carbon/Emery has as compared to the risk it would**
13 **experience were it not eligible for such a program?**

14 **A.** Yes, I did say that but it probably needs to be
15 amplified just a bit that there are lots of risks
16 associated with a telephone company or with a small
17 company, it's not just the size. In fact Roger Ibbotson,
18 and I quote him in my testimony, says that even liquidity
19 risk is also very, very important. And I would argue quite
20 strongly that liquidity risk is just as apparent or more
21 apparent for a small rural telephone company operating in
22 Price, Utah and no government operation is going to solve
23 that liquidity risk.

24 **Q. Let me ask you a few question about liquidity**
25 **risk. Are you familiar the capital structure of**

1 **Carbon/Emery Telephone?**

2 A. Yes, I am.

3 **Q. Could you describe that briefly?**

4 A. The actual capital structure is they are 100
5 equity.

6 **Q. Who are the equity holders?**

7 A. The shareholders, members of the cooperative I
8 don't know. I don't have a list of all the holders.

9 **Q. Are you aware of any recent attempts to
10 increase the equity of the company, any sales of stock?**

11 A. No. That question -- I reviewed the answer to
12 that question that was asked by the Office to the company
13 and there was no -- there have been no issuance of stock in
14 the public sector.

15 **Q. Are you aware of any of the current owners who
16 have had a desire to sell and no ability to do such?**

17 A. A desire to sell and would want to essentially
18 cash out? I do not know of any. To the extent that some
19 of those are cooperative members, I know other cooperatives
20 that people have those desires, but I don't have specific
21 information for Carbon/Emery.

22 **Q. And you're aware that Carbon/Emery in fact
23 makes decisions based on the certainty provided by the
24 Universal Service Fund; is that correct?**

25 A. No. The Company, just like any company, has an

1 array of investment options both regulated, nonregulated,
2 however it goes. And that array of investment options is
3 before the decision makers and they can choose what
4 investments to make.

5 Q. So do you disagree with Mr. Woolsey's testimony
6 an hour or two ago when he said that they in fact do make
7 decisions based on, I believe it's a quote, certainty
8 provided by the FCC and state?

9 A. I didn't hear him say that. So I'll defer if
10 he said that.

11 Q. Do you disagree with that statement?

12 A. Say the statement again please.

13 Q. That Carbon/Emery makes decisions based on the
14 certainty provided by the FCC and state, and that was
15 specifically referring to the subsidy programs for rural
16 telephone.

17 A. Yes, without looking at the full transcript
18 that's possibly one item that they use, but they still have
19 the array of investment options.

20 Q. Based on how much risk is involved do you think
21 it would in fact change the decisions that the company
22 might make?

23 A. Certainly. The risk of a particular investment
24 opportunity or plan to use capital, the risks associated
25 with that endeavor will definitely be a factor in a

1 decision.

2 **Q. You further testified you believe they may also**
3 **be capital constrained in the borrowing process by the**
4 **nature of their size; is that right?**

5 A. Yes. As far as borrowing goes, yes. Small
6 companies are constrained. There are actual boutique
7 lending firms that cater to small rural telephone
8 companies. If you go to ABC bank down on Main Street, it's
9 not likely that they're going to want to lend you money
10 because of the -- because of all of these associated risks
11 and the unmentioned risks that we haven't talked about.
12 Liquidity in small companies are definitely considerations
13 for a bank.

14 **Q. Are you familiar with the most recent long term**
15 **borrowing rate that has been used in this case?**

16 A. No. I reviewed it. It's not a controversial
17 item so I can't remember what the number is. I can look it
18 up. It's on Mr. Coleman's exhibits.

19 MR. JETTER: Counsel, do you consider that a
20 confidential number?

21 MS. SLAWSON: Tell me which one it is again.

22 HEARING OFFICER: The interest rate paid on --

23 MS. SLAWSON: That's not confidential.

24 **Q. (By Mr. Jetter) Would it surprise you to know**
25 **that rate is 5.64 percent?**

1 A. No.

2 **Q. Doesn't that seem like an awfully low amount**
3 **compared to the Treasury Bond rate over the 20 year period,**
4 **or 25 year period that you suggested being more appropriate**
5 **for the term of effects of this case being 5.009 percent?**

6 A. So we're talking about 50 paces points
7 difference.

8 **Q. Yes, between a risk free rate and the small**
9 **company that you say has such a high risk that it needs**
10 **significant risk premium to attract capital.**

11 A. One, this is a cost of debt number that we just
12 referred to. It's not the cost of equity. That's one
13 important consideration. The other consideration when
14 you're talking about debt is -- at least one of the -- the
15 biggest focus of boutique firms is RUS, which is the rural
16 utility service, which is a government lending program that
17 produces rates that are very attractive for purposes of
18 federal public policy. So I don't think you can compare
19 the cost of debt and relate it to the cost of equity or the
20 equity premium that should be applied.

21 **Q. Well, the two of those are both based on risk,**
22 **are they not?**

23 A. Different types. A lender has different claims
24 against a company than a stockholder. For example, if a
25 company like Fairpoint, which is one of Mr. Coleman's

1 examples, goes bankrupt there is a triage or a hierarchy of
2 who has claim against assets that still exist. And the
3 common stock shareholders are the last ones to get any
4 claims. So there is a difference in valuation and
5 weighting of risks and claims.

6 **Q. Just in the abstract just let me ask you, would**
7 **you expect a company with a higher variability in its**
8 **revenue stream to be considered a higher risk company by a**
9 **lender?**

10 A. It really depends on cash flow. You're saying
11 higher variability, but does it have enough cash flow to
12 meet its obligations. And all lenders have certain
13 thresholds, factors if you want to call them, that the
14 companies have to meet in order to not be in breach of that
15 loan. So they have safeguards, lenders have safeguards to
16 address and principally -- a lot of them relate to cash
17 flow, but there are others as well. But it's the ability
18 to pay the loan off. It's just like if we were to buy a
19 car the lender would want to know if you had enough money
20 to pay off that car. The variability of your income may
21 not be a factor because you may have plenty of money above
22 the threshold that they're looking for.

23 **Q. If you had a source as reliable as, for**
24 **example, the State of Utah Universal Service Fund as well**
25 **as the Federal Communications subsidy programs providing a**

1 significant portion of that cash flow, would that indicate
2 to you potentially a lower risk for that company as
3 compared to a similar company without those resources to
4 draw on?

5 A. Not in 2015 because there is great uncertainty
6 in both programs, both the Utah USF dealing with the
7 depreciation method that is now proposed and how it could
8 affect the claim or the request from Carbon/Emery, and even
9 more importantly the flows from Federal Universal Service
10 as we are going through a major transformation at the
11 federal level. There is not much certainty as to what is
12 going to happen in very near terms with Federal Universal
13 Service. So there is quite a bit of uncertainty in a
14 market, I should mention, in a market that is traditionally
15 over the long last 100 years has been relatively calm and
16 stable. But ever since telecommunications back in 1996,
17 and now the reform in 2011 at the FCC, there is quite a bit
18 of uncertainty within the market.

19 Q. I think back to reiterate that question. If
20 you're comparing let's say Carbon/Emery to one of the
21 references that both you and Mr. Coleman have used,
22 Shenandoah Valley Telecommunications, who I believe is in
23 Virginia, which does not have a comparable universal
24 service fund program. Between those two companies would
25 you say is it more or less risky to have those types of

1 **subsidy programs, the Utah Universal Service Fund, at your**
2 **disposal?**

3 A. It's hard to say because Shenandoah Valley it
4 is in Virginia. I have just a small acquaintance with the
5 company. It would be better for a company and for a lender
6 or for an investor to look at the customer base and the
7 customer structure and the stability of that customer base
8 and customer structure rather than a government universal
9 service program that may or may not exist, may or may not
10 be cut. There is quite a bit of uncertainty. It is not a
11 certain thing that USF exists in states, and as you
12 mentioned in Virginia it doesn't exist.

13 **Q. Is there something unique about their customers**
14 **that you think make them more likely to remain customers or**
15 **to remain more reliable than the customers of Carbon?**

16 A. Well, I don't know if you've been to Shenandoah
17 Valley, but it is a fairly dynamic economic space. I mean
18 there is -- I would say, no offense, Brock, but Shenandoah
19 Valley has more economic activity potential than Carbon and
20 Emery counties in Utah.

21 **Q. I'm talking about on a per customer basis. Do**
22 **you think each individual customer is more reliable, more**
23 **predictable?**

24 A. I don't have any information to give you or to
25 inform you on that question.

1 MR. JETTER: Thank you, Mr. Meredith. Those
2 are all the questions I have.

3 HEARING OFFICER: Mr. Moore.

4 MR. MOORE: Just a few questions. Mr. Jetter
5 took most of mine. Just for clarity shake --

6 THE WITNESS: Your Honor, I have a small
7 hearing problem. So could the microphone be drawn a little
8 closer so I can hear better.

9 MR. MOORE: How is this?

10 THE WITNESS: That's good.

11 CROSS EXAMINATION

12 BY MR. MOORE:

13 Q. In your summary you stated that you are not
14 changing your proposed rate of return from your initial
15 application; is that correct?

16 A. Correct. I am -- my recommendation is the
17 Commission adopt the 10.5 percent overall rate of return
18 for Carbon/Emery's application.

19 Q. That's including a 12.13 intrastate rate of
20 return; is that correct?

21 A. Yes. According to the application that was the
22 rate of return used for the intrastate portion.

23 Q. You didn't apply a small company premium?

24 A. What I did is I looked at several different
25 methods, several different items and I'm recommending the

1 Commission adopt the 10.5 because all of those indicators
2 show that if you were to do anything else, look at the
3 different risks, liquidity premium risks, and small company
4 premium risks, you would be in excess of that 12.13, I
5 believe. So, therefore, the 10.5 percent is supported.

6 **Q. How did you arrive at the 12.13?**

7 A. 12.13 I didn't arrive at it. The Company used
8 12.13 because I understand the Division proposed and
9 testified in 2014 that rate was just and reasonable and
10 within the public interest in another case.

11 **Q. Was that case taken to hearing?**

12 A. That case was not taken to hearing. The
13 Commission adopted in full the Division's recommendation.

14 **Q. Through a settlement?**

15 A. No, it wasn't settled. There was no dispute.
16 The Office -- the Division created a petition, created
17 testimony, filed the petition, and the Commission adopted
18 it. That's how I understand the Hanksville case to have
19 happened. There was no settlement because there was no
20 issue in dispute.

21 MS. SLAWSON: Your Honor, if I may, I believe
22 there actually was a hearing in that case, a hearing to
23 adopt the stipulation just as a matter of record.

24 **Q. (By Mr. Moore) But the stipulation didn't end**
25 **from a settlement?**

1 A. I did not participate. My understanding is
2 that the Division prepared, produced, and supported the
3 12.13 percent in 2014, which incidentally is the same test
4 year that we're dealing with today.

5 **Q. But they haven't taken that position in this**
6 **case?**

7 A. No, they have not. They are recommending an
8 adjustment.

9 **Q. Could you turn to page 13 of your rebuttal**
10 **testimony, your revised rebuttal testimony September 4,**
11 **2015?**

12 A. Yes, I'm there. It starts with a graph?

13 **Q. Yes. I have some questions about the graph.**
14 **The fifth column entitled small stocks and lists various**
15 **premiums or additions; is that correct?**

16 A. Yes. This is by Roger Ibbotson from Ibbotson &
17 Associates that we've been talking about, very credible
18 professor at Yale University, or was. I don't know his
19 status now. He is identifying premiums that are looked at
20 in the real world.

21 **Q. The first premium is a small stock premium,**
22 **which is the small company premium we've been referring to;**
23 **is that correct?**

24 A. Yes, that's what I would understand that to be.

25 **Q. Do you know of any USF case that has used a**

1 **small company premium?**

2 A. No, most USF cases don't even address this
3 issue. They use the 11.25 percent authorized rate of
4 return that the FCC uses and that's the end of the
5 discussion.

6 **Q. Do they use an equity risk premium?**

7 A. I'm sorry.

8 **Q. Are you aware of ones that use a equity risk**
9 **premium?**

10 A. Well, the equity risk premium is the premium
11 that is given as a market or risk premium, however you want
12 describe it. That's used with a CAPM model. As I
13 understand it from your witness's testimony that in some
14 cases, although dated, that equity risk premium has been
15 used in a CAPM model in Kansas.

16 **Q. Do you have one from a bond horizon premium?**

17 A. No, I don't know of any application of -- this
18 is getting more into the -- the bond horizon premium I
19 don't have any information on a state universal service
20 program, or federal for that matter, addressing a bond
21 horizon premium.

22 **Q. Did you attempt to compute the required rate of**
23 **return using this graph, adding up these various premiums**
24 **for Carbon?**

25 A. No, I did not. My testimony, I do state the

1 liquidity premium and the small company premium are
2 somewhat intertwined. The range, Dr. Billingsley's range
3 or rate for small company such as Carbon/Emery is 6 or 7
4 percent small company premium. And I did not even go that
5 far. I just took half of it and I took a 3 percent small
6 company premium to address liquidity and small company and
7 it exceeded the 12.3 generated that supported 10.5 so I did
8 not have to extend my analysis further.

9 **Q. Could you turn to page 12 of your testimony?**

10 A. Sure.

11 **Q. You have a table there, table 2. Did you**
12 **prepare this table?**

13 A. I did prepare the table.

14 **Q. What is the source of your spot beta**
15 **information on the table?**

16 A. The spot beta was -- to date the spot beta in
17 trying to replicate the information that Mr. Coleman of the
18 Division used I have went to Yahoo.com and obtained the
19 spot beta for these companies listed.

20 **Q. Can you provide the source documentation?**

21 A. Did I provide source documentation, no. It was
22 the spot beta as of that date at Yahoo.com.

23 **Q. What does the term CAM adjusted mean?**

24 A. That's a very conservative straight -- CAPM.

25 **Q. I'm sorry, CAPM.**

1 A. It's the expected return using a risk free rate
2 and then applying the data to a market premium.

3 **Q. Where did you get the data for this CAPM**
4 **adjustment?**

5 A. The CAPM, the equation is the expected return
6 equals the risk free rate. And the risk free rate in this
7 calculation. Again as I said I used a very conservative --
8 actually not a textbook approach, but I used the T-bill
9 rate, which is the rate that was found below. It's from
10 1990 to today as of the date of filing. So a 3.04 percent
11 T-bill rate. Then I applied the -- then you add to that
12 that risk free rate the beta multiplied by a risk premium.
13 Mr. Coleman used a risk premium of about 6.8 percent. I
14 opted to use an even more conservative number and I used
15 the 5.01 percent number listed here as a T-bond rate trend
16 as my risk premium. So it's a few, maybe a 150 paces
17 points lower than Mr. Coleman. Doing it with the abundance
18 of caution of get the lowest possible unadjusted CAPM.

19 This particular table is really not focussed on
20 getting the CAPM number itself, but rather the adjustment.
21 My whole testimony is there needs to be adjustments to a
22 standard CAPM. You just don't do the standard CAPM for
23 conditions that we have before us. And so that's why the
24 -- so I used a very small -- that's the equation that I
25 used in order to develop the column called CAPM unadjusted.

1 And that's why I think if you were to compare
2 this to Mr. Coleman's those numbers would be different
3 because I did not use his numbers. I used in the instance
4 of the market premium, the equity premium, I used a lower
5 rate than he did.

6 **Q. This is reflected in the third column of the --**

7 A. Yes.

8 **Q. You used the T-bill and the T-bond rates. Can**
9 **you describe where the interest rates are inputted into the**
10 **CAM asset pricing model?**

11 A. Sure. The T-bill rate is a 90 day T-bill.
12 That information was obtained from the U.S. Department of
13 Treasury. They have a series that gives this information.
14 And the T-bond rate is the 20 year T-bond, Treasury Bond.
15 Those numbers go into the column we were just describing.
16 The first one, the T-bill, the 3.04, gives the risk free
17 rate in the CAPM equation. The second one, the 5.01, is a
18 conservatively low proxy for the risk market premium. That
19 number is multiplied by the beta and the sum of that
20 represents the CAPM.

21 **Q. These calculations created the leveraged CAPM**
22 **in the last column?**

23 A. No. The levered -- if we go over to the far
24 right.

25 **Q. The far right.**

1 A. We have taxes and debt and equity percentages,
2 and then we have a levered beta referenced by Dr. Heaton in
3 Exhibit 1 as well. This adjusts for taxes and also debt
4 and equity. So there is a formula that creates the lever
5 and then you apply that lever to the unadjusted beta and
6 you get a levered beta.

7 **Q. The conclusion of the chart is your leveraged**
8 **CAPM on the far right hand column?**

9 A. Correct. That is a leveraged CAPM, which
10 adjusts for taxes and debt and equity structure of the
11 various proxy companies.

12 **Q. You have Verizon and AT&T as your first two**
13 **companies, correct?**

14 A. Yes, Verizon.

15 **Q. Is Verizon the same as --**

16 A. Verizon is a Bell operating company, changed
17 its name to Verizon in the 90's.

18 **Q. Both Verizon and AT&T have very similar**
19 **industry profiles, don't they?**

20 A. Very similar --

21 **Q. Industry profiles.**

22 A. Industry profiles meaning their scope?

23 **Q. Their size.**

24 A. Their capital structure is very, very
25 different. Verizon is highly leveraged and AT&T is not.

1 You can see that in the debt and equity percentage. You
2 can take the percent debt divided by the percent equity
3 which is reported in the third to last column, the Verizon
4 number is 8.9 and AT&T is 0.88.

5 **Q. But in terms of size, they're both remnants of**
6 **the Bell company, they're competitors, aren't they?**

7 A. Yes. Verizon and AT&T are competitors for
8 certain services, for primarily their wireless services.
9 They have a couple local exchange carriers, traditional
10 local exchange areas that are not -- I wouldn't call them
11 competitive with each other. There is some overlap. But
12 what we see in the press most of the time is AT&T and
13 Verizon fighting out signal coverage for wireless service
14 across the United States map. So they're highly
15 competitive in that market.

16 **Q. In your last column how would you -- how does**
17 **leveraged CAPM relate to cost of equity?**

18 A. Okay. The leveraged CAPM is produced -- or the
19 leveraged beta is produced by multiplying the beta times an
20 equation or a function that addresses the tax structure of
21 the company, and that tax piece is then multiplied by the
22 debt and equity percentages. So the levered beta takes
23 into account taxes and debt and equity structure all in one
24 calculation.

25 **Q. That's the second to the last column?**

1 A. Correct.

2 **Q. I'm asking about the last column.**

3 A. Yes. Then the last column is the CAPM that
4 uses instead of the spot beta, it uses the levered beta and
5 creates a levered CAPM result.

6 **Q. How does that relate to the cost of equity? Is**
7 **there any relationship whatsoever?**

8 A. Well, in this case the levered beta would
9 reflect the equity premium that market analysts would
10 expect from these companies based on their capital
11 structure.

12 **Q. The leveraged CAPM Verizon has over three times**
13 **the number of AT&T; is that correct?**

14 A. Correct. It's 25.7 and AT&T is 7.4. That
15 again is a function of the very different capital structure
16 of the two companies.

17 **Q. Doesn't a levered CAPM of this magnitude cause**
18 **some problems with competition?**

19 A. With competition?

20 **Q. Between AT&T and Verizon.**

21 A. I don't think so. Competition would be on the
22 demand side for services, seeking market share. And I
23 don't know how the capital structure would be influenced by
24 market share. I mean, investors are looking at market
25 share because that is a risk assessment that they have to

1 take as to whether the company has a desirable environment
2 to operate with the potential for growth. So to that
3 extent the competition could affect it, but I don't think
4 it's direct.

5 **Q. It's a cost though, isn't it? How can Verizon**
6 **compete if they have a cost that is over three times higher**
7 **than AT&T?**

8 A. No, this is not a cost. There is a cost of
9 capital if an analyst is looking at Verizon and AT&T,
10 Verizon is growing a lot more than AT&T in some of its
11 markets, in its wireless markets, for example. So from an
12 investment standpoint you say okay I'll take that growth
13 potential for Verizon. And AT&T is more of a stay company
14 -- I hate to say that if anybody has any AT&T relatives.
15 But they're a little bit more conservative and more of a
16 dividend value company than Verizon is.

17 MR. MOORE: That's all I have. Thank you.

18 HEARING OFFICER: Any redirect?

19 REDIRECT EXAMINATION

20 BY MS. SLAWSON:

21 **Q. Would you take a look at DPU Cross Exhibit 1?**

22 A. Is this the Morningstar page 113?

23 **Q. Yes.**

24 A. Yes.

25 **Q. Mr. Jetter questioned you on this wanting to**

1 know -- I believe his questions were something along the
2 lines of -- I'm not trying to restate them exactly --
3 whether a company that receives USF -- if the company
4 receives USF would that offset a small company premium. Do
5 you recall that?

6 A. Yes, I recall that.

7 Q. How would this size premium relate to the risk
8 that Mr. Jetter was alluding to or the lower risks
9 associated with USF?

10 A. Say that again.

11 Q. How would the risk factor that Mr. Jetter was
12 identifying and the small company premiums that is
13 identified here by Mr. Ibbotson, how would that relate to a
14 company that receives USF distribution?

15 A. As I look at page 113 there is a graph, 7.5,
16 that shows essentially small company premium over time
17 going back to 1945 and it varies. There is some
18 variability there. But I think the two take aways are one
19 is positive, there is a small company premium that is
20 generally applied in the real world, it's just not a
21 straight CAPM, a traditional textbook CAPM. And then the
22 number ranges right now in 2014 it looks like that's at
23 about two and a half, I guess a fair read maybe a little
24 north of two and a half percent small company premium.

25 Dr. Billingsley looked at small company

1 premium, and actually it was one of his criticisms of the
2 FCC method they used in looking at whether they should
3 re-prescribe the authorized rate of return of 11.25 percent
4 and they produced a staff report. Mr. Billingsley used a
5 small company premium in that case, and almost all of the
6 companies that would be affected were federal universal
7 service recipients. So it did not persuade Dr. Billingsley
8 from using a small company premium even when you had this
9 quote or this alleged government program for funds. So I
10 think they are distinct and I don't think they offset one
11 another.

12 MS. SLAWSON: Thank you. No other questions.

13 MR. JETTER: I do have some followup questions.

14 HEARING OFFICER: How much time do you
15 anticipate?

16 MR. JETTER: Ten minutes.

17 HEARING OFFICER: Let's go ahead and break for
18 lunch and do that when we come back. Is that okay? How
19 long do you all want for lunch? We'll come back at 2:00.

20 (Off the record.)

21 HEARING OFFICER: Let's go back on the record.
22 We are picking up where we left off before our lunch break.
23 Mr. Jetter, I believe you had some recross for
24 Mr. Meredith.

25 MR. JETTER: Yes. I have reconsidered and have

1 decided not to recross.

2 HEARING OFFICER: All right. Mr. Moore, do you
3 have any recross?

4 MR. MOORE: No, I do not.

5 HEARING OFFICER: Okay. Then Ms. Slawson, I
6 think what I would do at this point is ask you to please
7 address as well as you can the questions that the
8 Commission posed in its notice.

9 MS. SLAWSON: I would be happy to do that, but
10 I'm just wondering if it might be more appropriate at the
11 end after all of the witnesses have testified so we know
12 what all the testimony in the record is. I think a lot of
13 the testimony, or some of the testimony that we might
14 illicit through cross examination might go to some of those
15 issues and not make those statements based on an incomplete
16 record, but it's up to you.

17 HEARING OFFICER: I would like you to address
18 what you can at this point.

19 MS. SLAWSON: Thank you. In the notice served
20 by the Public Service Commission on January 21, 2016 the
21 Commission notified parties that they should come prepared
22 to discuss three issues. Do you want me to identify those
23 issues for the record?

24 HEARING OFFICER: Sure.

25 MS. SLAWSON: Number one, Utah Code Section

1 54-8b-6 states, a telecommunications corporation providing
2 intrastate public telecommunications services may not
3 subsidize its intrastate telecommunications services which
4 are exempted from regulation with the proceeds from other
5 intrastate telecommunications services not so exempted.
6 Disbursements from the UUSF constitute proceeds from
7 regulated intrastate telecommunications operations. Are
8 the parties satisfied that a continued or increased
9 disbursement from the UUSF would not serve to subsidize the
10 nonregulated operations of Carbon/Emery? Why or why not?
11 Have I identified that issue correctly?

12 HEARING OFFICER: I believe so.

13 MS. SLAWSON: As the Commission has noted this
14 is a threshold issue and the questions that this issue
15 presents are addressed in the voluminous testimony filed in
16 this case. The testimony specifically filed in this case
17 identifies with particularity the uses for which
18 Carbon/Emery will use or utilize its UUSF funds.

19 Each party in this matter has provided
20 testimony on, for example, cost allocation between
21 regulated and nonregulated activities. And so those issues
22 are briefed for the Commission in terms of testimony. The
23 Commission I would say has the obligation at this point to
24 determine how those cost allocations should be made to
25 avoid any subsidization.

1 We believe, Carbon/Emery believes and is
2 satisfied that a continued and increased disbursement from
3 the Utah Universal Service Fund would not serve to
4 subsidize its nonregulated operations, and that the
5 testimony they have provided on this case in this matter is
6 clear on those points.

7 Carbon/Emery filed it's application for Utah
8 Universal Service Fund and its requested revenue
9 requirement has gone through a vigorous review process.
10 The testimony or evidence in this case proves that
11 Carbon/Emery is not using the UUSF funds to subsidize its
12 nonregulated operations.

13 In order to be eligible for UUSF funds the
14 Company must show that it is an eligible telecommunications
15 carrier, that it is in compliance with Commission orders
16 and rules. Did the Company complete a Commission review of
17 its revenue requirement and other telecommunications
18 service rate structure prior to any change in the UUSF,
19 which is what we're doing here today, and then does not
20 charge rates in excess of the affordable base rate. It
21 must also show that it provides lifeline service and it is
22 a facility based provider.

23 The testimony that's been provided in this case
24 through the prefiled written testimony and the testimony
25 illicit here today demonstrates that Carbon/Emery has met

1 the requirements and the statute and rules and there is no
2 evidence of subsidization in the extensive record.

3 Shall I go forward with issue two?

4 HEARING OFFICER: That's fine.

5 MS. SLAWSON: Issue two, Utah Code Section
6 54-8b-15(1)(a) states, a basic telephone service means
7 local exchange service. Utah Code Section 54-8b-15(6)(a)
8 states, the UUSF shall be designed to promote equitable
9 cost recovery of basic telephone services. The question
10 asked by the Commission are the parties satisfied that a
11 continued or increased disbursement from the UUSF to
12 Carbon/Emery would comply with this statutory language?

13 Each party in this case has supplied testimony
14 as to the reasonable costs -- let me back up. Carbon/Emery
15 has provided testimony and an application as to the
16 reasonable costs associated with providing basic telephone
17 services. Each of the other parties have provided
18 testimony on this issue. At this point the record is
19 robust and demonstrates through the testimony of the
20 Company that the reasonable costs of providing basic
21 telecommunications services are not met through rate
22 recovery at the affordable base rate, and the Company is
23 not earning the allowed rate of return.

24 And so we believe that the testimony shows that
25 Carbon/Emery is entitled to additional UUSF funds to meet

1 the reasonable costs of providing basic telecommunications
2 for telephone services.

3 Issue three, Utah Code Section 54-8b-15(5)
4 states, operation of the Utah Universal Service Fund shall
5 be nondiscriminatory and competitively and technologically
6 neutral in the collection and distribution of funds,
7 neither providing a competitive advantage for, nor imposing
8 a competitive disadvantage upon any telecommunications
9 provider in the state. Are the parties satisfied that a
10 continued or increased disbursement from the Utah Universal
11 Service Fund to Carbon/Emery would comply with the
12 statutory language? Why or why not?

13 As indicated previously in my statement, and as
14 demonstrated in the testimonies of Brock Johansen and
15 Darren Woolsey, Carbon/Emery has met the requirements of
16 the statute outlining the eligibility for disbursement from
17 the Utah Universal Service Fund. And therefore, is
18 entitled to continued and increased disbursements from the
19 fund. There has been no testimony, nor has there been to
20 my knowledge any argument that the fund is not being
21 administered neutrally.

22 So based on the testimony provided in the
23 record Carbon/Emery's position is that Carbon/Emery is
24 entitled to additional UUSF distribution from the fund and
25 has met the requirements of the statute.

1 HEARING OFFICER: Thank you. And you have no
2 more witnesses; is that correct?

3 MS. SLAWSON: That is correct.

4 HEARING OFFICER: Does the Division want to
5 call its witness. Just so you know, I figure we'll go at
6 this point until about 3:20, break for 15 or 20 minutes,
7 and then we can go up to 5:00 as needed. Go ahead.

8 MR. JETTER: It's a little out of the order
9 that the Company did, but if you would like I could address
10 the same questions now just back to back.

11 HEARING OFFICER: That's fine.

12 MR. JETTER: Because it might be easier looking
13 back at the record to see. And if it's acceptable I'll
14 rely on Kira's reading on the questions and just address
15 them as questions 1, 2, 3.

16 HEARING OFFICER: That's fine.

17 MR. JETTER: With respect to question one. In
18 practically every incumbent local exchange carrier
19 territory or companies in Utah are receiving Utah Universal
20 Service Fund support. The telephone company receiving the
21 support is under common ownership with its affiliate
22 internet service provider. In most, if not all, cases the
23 ILEC owns the facilities and sells access to the affiliated
24 internet company. Generally the access fees paid by the
25 internet company are based on the National Exchange Carrier

1 Association tariff rate, also referred to as NECA.

2 The NECA tariff rate is a cost based tariff
3 derived from other similar ILEC costs. The Division has
4 relied upon the NECA tariff or prior recommendations
5 because it is a reasonable proxy established by an outside
6 entity. To the extent to which UUSF funds may subsidize an
7 affiliate in such circumstances is difficult to determine.

8 Most of the current plant additions that we're
9 seeing in the ILEC territories are providing fiber to the
10 home. Installation of fiber to the home is not necessary
11 for basic telephone service. However, fiber network can
12 and do provide basic telephone service as well as offer
13 significantly improved availability of high-speed internet
14 access for the affiliate internet provider.

15 In the event that the copper network is failing
16 and must be replaced it is often most economical to replace
17 facilities with fiber. The benefit of fiber is shared
18 between the ILEC as well as the affiliate. Revenue
19 increases generated from and received after the fiber
20 install are likely to be received primarily by the internet
21 and/or television affiliates.

22 What were once telephone companies
23 traditionally that began to provide internet through an
24 affiliate are often now predominantly internet and
25 television companies that also happen to offer telephone

1 service. However, all three services in the case of fiber
2 networks can often use the same facility. And all of them
3 will likely benefit from sharing of the costs of the
4 facility.

5 Whether it can measure the benefit to the
6 company's basic telephone service or to first determine
7 whether the investment was necessary in order to continue
8 basic telephone service is a critical question.

9 If, for example, the Commission were to take
10 the view that the revenue increases or revenue derived from
11 the value of the facility to each affiliate were indicative
12 of whether subsidy were occurring, then the calculation of
13 costs shared based on revenue would indicate that it is
14 likely that an affiliate may be being subsidized. On the
15 other hand, if the Commission views the test as whether it
16 reduces the cost to provide basic telephone service by
17 selling access to affiliates, it may be argued that because
18 the affiliate contributes some dollars to defray the costs
19 of the telephone service the Utah Universal Service Fund is
20 not subsidizing the affiliate if that investment in the
21 fiber or other upgrades was a prudent investment for the
22 regulated ILEC.

23 With respect to the cost of operations the
24 Division of Public Utilities periodically reviews all
25 regulated telecommunications companies receiving Utah

1 Universal Service Fund support. This review includes a
2 desk audit of the annual report filed by the companies with
3 the DPU. If the desk audit indicates issues that need
4 further investigation, the DPU then takes the appropriate
5 action, which may include a more formal audit at the time
6 if the Division has the ability to dedicate time and
7 resources to that investigation.

8 Cases filed with the Commission that are
9 ongoing tends to take precedence over those proactive
10 audits. If a formal audit is conducted then the DPU will
11 receive the cost allocation manual that the company is
12 using to allocate costs between its regulated operations
13 and unregulated affiliates. This has been a standard
14 practice for several years.

15 The cost allocation manuals are normally
16 developed based on the FCC Part 64 guidelines as there is
17 no Utah specific Public Service Commission rules to use as
18 guidance for these cost allocation manuals. If the cost
19 allocation manual seems reasonable to the Division and the
20 company appears to have made a good faith effort to
21 allocate costs between regulated and nonregulated
22 companies, then the Division will test to make certain that
23 the cost allocation manual is being followed and practiced.
24 If there is no cost allocation manual, or the cost
25 allocation manual seems insufficient, then the Division

1 will propose its own cost allocation method.

2 In the case of Carbon/Emery Telecom Inc. the
3 Division has reviewed its cost allocation manual
4 approximately five times in the last six to seven years
5 during various Universal Service Fund requests. The DPU
6 has found that Carbon/Emery Telecom's cost allocation
7 manual seems to be fairly robust and it appears to be
8 followed and practiced.

9 The only criticism of the cost allocation
10 manual is that it is sometimes dated and could be reviewed
11 and updated more often. The DUP recognizes that there are
12 some inherent problems developing accurate cost allocation
13 manuals.

14 If the Commission is interested in developing
15 rules to provide more specific guidance in this area the
16 DPU would welcome such an opportunity and would like to
17 participate in an effort to do so.

18 With respect to question two. Yes,
19 disbursements comply with this language. The DPU views the
20 Utah Universal Service Fund as a cost recovery mechanism to
21 be used were the total cost of providing basic telephone
22 services exceed the revenues generated from those services.
23 The calculation of that support is defined in Commission
24 Rule 746-360-8.

25 If a telecommunications company is charging the

1 affordable base rate as defined in Rule 746-360-2, then the
2 Division believes that the Universal Service Fund is
3 designed to fill in the gap between the total revenue and
4 total expense for providing basic telephone service.

5 If the telecommunications company were not
6 charging the affordable base rate, the Division would
7 impute the revenue it would receive if it were charging the
8 affordable base rate and reduce the Utah Universal Service
9 Fund recommendation by that amount.

10 In this case Carbon/Emery Telecom is charging
11 the affordable base rate and the Division believes that
12 continued disbursement from the Universal Service Fund to
13 Carbon/Emery Telecom for the cost recovery for the basic
14 telephone communication services is appropriate to the
15 extent that the actual cost of providing basic telephone
16 service exceed the revenue generated. However, the
17 Division is mindful of opportunities for effectively
18 recovering for expenses that would benefit parts of the
19 Company's business that are unregulated. Progressive
20 replacement of infrastructure, such as copper cable that
21 remain sufficient to provide basic telephone service, can
22 allow the Company to recover for investments that have not
23 been needed for the service of basic telephone. The
24 Division recognizes that basic telephone service can
25 benefit from these investments even if it did not require

1 them.

2 Further to stave off customer departures,
3 telephone companies attempt to retain customers with more
4 advanced services. Given their affect on reducing customer
5 losses and some incremental benefits, these investments
6 have not been the subject of the Division's adjustments in
7 this case.

8 Nevertheless, when the investment is recovered
9 through accelerated depreciation the Division is unwilling
10 to accept that accelerated recovery and has made
11 adjustments in our recommendations to the Commission.

12 And with respect to question three, eligibility
13 for Utah Universal Service Fund disbursement is defined in
14 Commission Rule 746-360-6. To be eligible the company must
15 be designated as an eligible telecommunications carrier
16 pursuant to 47-USC-214(e).

17 Carbon/Emery Telephone is an eligible
18 telecommunications carrier as described above and is an
19 incumbent rate of return telephone corporation that is
20 described in Rule 746-360-6. The Division, therefore,
21 believes it is eligible to receive Universal Service Fund
22 disbursements in the amounts that would be calculated
23 appropriately.

24 While a variety of rules governing Utah Code
25 54-8b-15(5) might be permissible under the Commission's

1 existing rules, Carbon/Emery Telephone is eligible subject
2 to the establishment of Commission -- subject to the
3 Commission's establishment of an appropriate amount.

4 There are other carriers competing in the
5 Carbon/Emery service territories utilizing other technology
6 such as wireless service. These carriers may be at a
7 competitive disadvantage when competing with a carrier such
8 as Carbon/Emery that receives Utah Universal Service Fund
9 subsidy. However, as of yet these carriers have either
10 chosen not to pursue ETC designation or their applications
11 have been denied by the Commission for this territory.

12 Designation as an ETC may qualify them for
13 Universal Service Fund disbursements. There are several
14 wireless lifeline carriers that have received ETC
15 designations from the Public Service Commission. These
16 carriers as of yet have not requested Utah Universal
17 Service Fund support, and in each instance they have agreed
18 in stipulations to only seek Utah Universal Service Fund
19 support after additional proceedings requesting it before
20 the Commission. And that concludes the Division's
21 responses.

22 HEARING OFFICER: That's very helpful. Thank
23 you. Would you like to call your witness?

24 MR. JETTER: The Division would like to call
25 first Mr. William Duncan.

1 (The witness is sworn in.)

2 DIRECT EXAMINATION

3 BY MR. JETTER:

4 Q. Good afternoon, Mr. Duncan.

5 A. Good afternoon.

6 Q. Would you please state your name and occupation
7 for the record?

8 A. Yes. My name is William Duncan. I am the
9 manager of the Telecommunications and Water Section for
10 Utah Division of Public Utilities.

11 Q. Thank you. In the course of your employment
12 did you have the opportunity to review the application and
13 testimony filed by the applicant in this case?

14 A. Yes.

15 Q. Did you create and cause to be filed with the
16 Commission prefiled direct testimony?

17 A. Yes.

18 Q. I'll just read them all if that's okay. Direct
19 testimony, rebuttal testimony, revised rebuttal testimony,
20 and surrebuttal testimony along with the attending
21 exhibits?

22 A. Yes, I did.

23 Q. If you were asked those same questions today
24 would you answer them the same way?

25 A. Yes.

1 **Q. Do you have some corrections that you would**
2 **like to make to those?**

3 A. Yes. On my rebuttal testimony, revised
4 rebuttal and surrebuttal on page 1, the title page on each
5 of those documents, I failed to change the name of Emery
6 Telephone to Carbon/Emery Telecom Inc. The docket number
7 is correct and the testimony is correct, but I evidently
8 used the same testimony in the Emery case and inadvertently
9 forgot to change the title page. So that's page 1 on each
10 of those.

11 **Q. Do you have any other changes that you would**
12 **like to make?**

13 A. Yes. During our final review of the exhibits
14 prior to the hearing we discovered a calculation error in
15 the rate of return calculation. After correcting the error
16 the Division's position on the rate of return has been
17 revised to 9.97 percent rather than the 9.85 percent that
18 was submitted in previous testimony. Mr. Coleman will
19 testify to the Division's position on that later today.
20 That change has been considered by the Division and the
21 Division has adjusted its recommendation from decrease in
22 Utah Universal Service Fund of \$14,458, which I believe was
23 in my surrebuttal testimony, to an increase in Utah
24 Universal Service Fund annually of \$6,833. This increase
25 would put the Division's position for a total annual UUSF

1 disbursement of \$1,045,547.

2 We have two exhibits that we have developed to
3 replace two exhibits in my surrebuttal testimony. One of
4 them is the template we used for calculating the Utah
5 Universal Service Fund, which Carbon/Emery used in their
6 application and then we used that template to put our
7 adjustments in. So that one has been used before.

8 The second exhibit that we're passing out today
9 -- actually there are two tables in my surrebuttal
10 testimony that -- I didn't know the best way to handle
11 this, so rather than replace them in a written format I
12 just produced some Excel tables. One of them, the first
13 table on line 54 of my surrebuttal, and the second one is
14 on line 81 of my surrebuttal. But they both just show the
15 revenue requirement and revenue deficiency that I
16 previously spoke about of \$6,833. So it's a fairly minor
17 change, but one we had to correct when we found the error.

18 HEARING OFFICER: That's based on the change on
19 the rate of return, correct?

20 THE WITNESS: Yes. The rate of return changed
21 from 9.85 to 9.97.

22 HEARING OFFICER: That's the composite?

23 THE WITNESS: That's the composite, that's
24 correct.

25 HEARING OFFICER: Thank you.

1 MR. JETTER: At this time I would like to hand
2 out another hearing exhibit that is the correction made in
3 another one of our witnesses, Casey Coleman's testimony,
4 but it relates to the same issue so I thought it be
5 reasonable to pass this out at the same time.

6 HEARING OFFICER: Go ahead.

7 MR. JETTER: I intend to have Mr. Coleman
8 address this briefly.

9 HEARING OFFICER: Is there any objection? This
10 is just a replacement of an exhibit on file?

11 MR. JETTER: It is.

12 MS. SLAWSON: I just want to make sure I'm
13 seeing the corrections correctly on Mr. Coleman's
14 testimony. I can ask him about this if there are any
15 issues. We can keep going.

16 HEARING OFFICER: The Office has no objection?

17 MR. MOORE: No objection.

18 HEARING OFFICER: Did you want to ask
19 Mr. Coleman about this now?

20 MR. JETTER: I can ask him about it when he is
21 sworn in and we get it authenticated in the record at that
22 time.

23 HEARING OFFICER: Okay. Go ahead.

24 MR. JETTER: I believe at this time the two
25 exhibits that were first handed out, which are entitled at

1 the top DPU Exhibit 1.1 Hearing and DPU Exhibit 1.2 Hearing
2 and those relate to Mr. Duncan's testimony, that those be
3 accepted into the record?

4 HEARING OFFICER: And there is no objection?

5 MS. SLAWSON: No objection.

6 MR. MOORE: No objection.

7 HEARING OFFICER: All right. We'll accept them
8 as marked.

9 MR. JETTER: And with that that concludes my
10 direct testimony of Mr. Duncan. He is available for cross.

11 HEARING OFFICER: Ms. Slawson, questions for
12 Mr. Duncan?

13 MS. SLAWSON: Yes.

14 CROSS EXAMINATION

15 BY MS. SLAWSON:

16 Q. Good afternoon, Mr. Duncan. You provided
17 summary testimony for the Division in this case, correct?

18 A. That is correct.

19 Q. As I have reviewed your testimony I've
20 identified three issues that remain unresolved between the
21 Company and the Division; is that correct?

22 A. That is correct.

23 Q. Those would be rate of return, correct?

24 A. Yes.

25 Q. The final figure for the adjustment for

1 migration of customers from cable internet to fiber to the
2 home internet service, correct?

3 A. That is correct.

4 Q. And then the depreciation expense?

5 A. That is correct.

6 Q. With regard to the rate of return it's my
7 understanding that the only issue between the Company and
8 the Division at this point is on the appropriate cost of
9 equity; is that correct?

10 A. That is correct.

11 Q. And it's my understanding that Mr. Coleman will
12 be providing that testimony for the Division?

13 A. Yes.

14 Q. And with regard to the depreciation expense Joe
15 Hellewell will be providing that testimony for the
16 Division, correct?

17 A. Yes.

18 Q. Throughout this procedure the Division has
19 propounded several sets of data requests in this matter; is
20 that correct?

21 A. Yes.

22 Q. In addition to the data requests did you have
23 telephone calls with the Company throughout this process?

24 A. Yes.

25 Q. If you were unclear about an issue or response

1 to a data request you would call the Company for
2 clarification; isn't that accurate?

3 A. I don't know if we called them on every issue,
4 but we certainly did on some.

5 Q. You felt as though you could call them on any
6 issue?

7 A. Yes.

8 Q. Because you're providing the summary testimony
9 I just have a couple questions for you. But I wanted to
10 make sure in the testimony of Joe Hellewell there are
11 several references to the proposition that the Utah
12 Universal Service Fund should not be used as an incentive
13 for increased infrastructure investments. Do you recall
14 that testimony from Mr. Hellewell?

15 A. Yes, vaguely.

16 Q. I couldn't find any example when I looked
17 through your testimony of where you testified that
18 Carbon/Emery unnecessarily accelerated its plant investment
19 by replacing assets before the end of their useful life; is
20 that correct?

21 A. That's correct, I don't believe I testified on
22 that.

23 Q. I just want to identify the last remaining
24 issue between the Division and Carbon/Emery, and that was
25 the cable migration number.

1 A. Yes.

2 Q. As I've reviewed your testimony the final
3 figure with regard to the Division's adjustment for imputed
4 revenue for migration of customers who currently receive
5 their internet services through Carbon's cable affiliates
6 to the new fiber to the home network that is being
7 constructed by Carbon still needs final calculation which
8 is dependent upon the rate of return authorized by the
9 Commission, correct?

10 A. Correct, it's dependent upon the rate of
11 return.

12 Q. So is it fair to say that once that rate of
13 return has been determined by the Commission, the
14 calculation and the methodology for that calculation would
15 be finalized and the adjustment will be made, correct?

16 A. Yes. The adjustment is dependent upon whatever
17 the final rate of return is.

18 Q. With regard to the rate of return the Company
19 has proposed a return on equity of 12.13 percent, correct?

20 A. That is correct.

21 Q. Were you involved in the Hanksville Telecom
22 UUSF proceeding which was filed by the Division in May
23 2014?

24 A. Yes.

25 Q. Did the Division prepare the confidential

1 exhibits attached to its Hanksville application?

2 A. I'm sure we did.

3 Q. Do you recall the return on equity that was
4 used by the Division in that application?

5 A. Not specifically, but I -- if you say it was
6 12.13 I'll accept that.

7 Q. I think the Commission can take judicial notice
8 of what that number was. At the time the Division was
9 preparing the application in the Hanksville Telecom UUSF
10 proceeding was the Division aware that Emery Telecom was
11 also planning to file an application for UUSF?

12 A. I don't remember.

13 Q. In fact, Emery filed an application for an
14 increase in UUSF in September 2014; is that correct? The
15 first one.

16 A. Yes. I would say -- I would accept that's
17 correct. I don't remember the date, but I remember the
18 proceeding.

19 Q. Because you don't remember the proceeding I
20 would just state that the Commission can take judicial
21 notice that the return on equity number that was filed by
22 Emery in September of 2014. Was the return on equity
23 figure an issue that was contested by the Division in the
24 Emery 2014 UUSF application?

25 A. I don't remember.

1 Q. Have you reviewed the adjustments identified by
2 Mr. Ostrander in his surrebuttal testimony relating to
3 allocation adjustments?

4 A. Not in depth.

5 Q. I didn't see it in your summary testimony. So
6 the Division is not recommending that the Commission adopt
7 those adjustments; is that correct?

8 A. No, we're not.

9 Q. With regard to the landline loss projection, is
10 it your testimony that the Division supports and has
11 adopted the calculation provided by the Company for
12 landline loss projection?

13 A. I would say we adopted the amended landline
14 loss numbers that came in, that Carbon/Emery developed and
15 revised I'm going to say during testimony.

16 Q. With respect to the Division and Carbon/Emery
17 there is no issue, remaining issue, as to the landline loss
18 adjustment, correct?

19 A. No.

20 MS. SLAWSON: I have no other questions for the
21 witness.

22 HEARING OFFICER: Mr. Moore.

23 CROSS EXAMINATION

24 BY MR. MOORE:

25 Q. Just a few short questions on the capital

1 structure issue. Mr. Duncan, the Division is recommending
2 on its capital structure 35 debt and 65 percent equity in
3 this case?

4 A. Yes.

5 Q. This capital structure was derived from a 2008
6 capital structure task force; is that correct?

7 A. Yes.

8 Q. In your testimony you stated that prior to 2008
9 the DPU used various hypothetical structures, including the
10 50/50 structure recommended by Mr. Brevitz; is that
11 correct?

12 A. I wasn't here prior to 2008 so I can't -- the
13 information I received is from others that over the years
14 preceding 2008 the Division used a variety of capital
15 structures.

16 Q. The point of the 2008 capital structure task
17 force was to arrive at a capital structure that would
18 provide the ILEC's with certainty making future investment
19 decisions?

20 A. It was to provide some level of certainty in
21 Utah Universal Service Fund applications.

22 Q. Since you've been here the Division has used
23 that capital structure in its UUSF cases; is that correct?

24 A. Correct.

25 Q. In reading your testimony you seem to stress

1 that this was due to a policy of regulatory consistency?

2 A. Yes, it was trying to provide some regulatory
3 consistency.

4 Q. On page 48 of your rebuttal testimony you
5 stated that while DPU understands the OCS concerns with the
6 65/35 hypothetical capital structure, the DPU believes this
7 is not the place to make a major policy change. Does that
8 sound correct?

9 A. Yes.

10 Q. You went on to state, the DPU would support a
11 much broader proceeding to examine the question that could
12 ultimately result in consistent practices that could be
13 applied globally; is that correct?

14 A. Correct.

15 Q. Now the 2008 capital structure task force did
16 not result in a rule from the Commission, did it?

17 A. That's correct.

18 Q. In fact, October 27, 2008 the Commission sent a
19 letter to DPU rejecting a rule?

20 A. Correct.

21 Q. I'm going to hand you -- I believe this is in
22 our exhibit list, but there seems to be some confusion. So
23 I'll just hand these down and just ask a question without
24 putting it in the record unless there is an objection. Is
25 this letter -- have you ever seen this letter before?

1 A. Yes.

2 Q. Is this the letter that I was referring to?

3 A. I believe so.

4 Q. In the last sentence of the major paragraph the
5 Commission writes, it is also concerned that the impact of
6 the rules that sets rates under title 54 where the
7 Commission is required to make a determination based on
8 evidence presented in an adjudicated proceeding based on
9 circumstances facing each company and relevant to time the
10 rates will be effective.

11 A. Correct, that's what it says.

12 Q. Now if you provided a policy based on regular
13 consistency that's been in effect since 2008 and going to
14 go in effect indefinitely, until I guess there is another
15 global change, the capital structure is not as the
16 Commission suggests, the Commission pronounces, relevant to
17 time to which the rates take effect; isn't that true?

18 A. Can you restate that?

19 Q. I'm sorry. The Commission states that they
20 rejected the rule because in part they feel like the
21 capital structure should be based on evidence and
22 circumstances facing each company, and importantly relevant
23 to the time in which the cases will be effective.

24 A. Okay.

25 Q. My question is, if we have a stable global

1 policy that lasts from 2008 indefinitely that policy will
2 run array the Commission's concern about having the capital
3 structure in place relevant to the time with which the rate
4 will be taking effect, won't they?

5 A. I don't think there is any prohibition on us
6 not using this as a policy.

7 Q. No, but it's not the policy of the Commission,
8 is it?

9 A. No, it's not. Obviously the rule was not
10 adopted.

11 Q. Would you agree that there has been significant
12 changes in the telecommunications business since 2008?

13 A. Yes. The telecommunication business is
14 evolving continually.

15 Q. So the circumstances facing each company will
16 evolve over time?

17 A. Correct.

18 Q. Isn't your policy contradictory to this last
19 sentence of the first paragraph of the Commission's letter?

20 A. No, I don't believe so.

21 Q. Could you explain that?

22 A. In the Commission's letter it says in the
23 sentence above that the general parameters of the rule
24 accompanied by the variability attempted to be included in
25 the rule proposed may be applied by the Division itself in

1 its interactions with companies.

2 Q. But it goes on to say the Commission will not
3 provide that as a rule due to concerns of timing and
4 producing and looking at the evidence of a case by case
5 basis?

6 A. That's correct. The Commission certainly has
7 the authority to reject our use of that rule, or not rule,
8 but that policy if they see fit.

9 MR. MOORE: That's all I have.

10 HEARING OFFICER: Any redirect, Mr. Jetter?

11 MR. JETTER: I have no redirect. Thank you.

12 HEARING OFFICER: Your next witness.

13 MR. JETTER: The Division would next like to
14 call Casey Coleman and have him sworn in at this time.

15 (The witness is sworn in.)

16 DIRECT EXAMINATION

17 BY MR. JETTER:

18 Q. Mr. Coleman, would you please state your name
19 and occupation for the record?

20 A. My name is Casey J. Coleman. I'm an utility
21 technical consultant with the Division of Public Utilities.

22 Q. Thank you. In the course of your employment
23 have you had the opportunity to review the application
24 filed by the applicant in this docket?

25 A. Yes.

1 **Q. Did you prepare and cause to be filed with the**
2 **Commission direct testimony of Casey Coleman as well as**
3 **surrebuttal testimony of Casey Coleman?**

4 A. Yes, I did.

5 **Q. Do you have any corrections that you would like**
6 **to make to either of those or the exhibits that were**
7 **attached thereto?**

8 A. Yes, I wanted to put into the record, which has
9 already been provided and labeled DPU Exhibit 3.1 for the
10 hearing, which is an updated calculation for what the
11 Division is recommending for allowed rate of the return for
12 Carbon/Emery which Mr. Duncan talked about earlier changed
13 the rate from the 9.85 to 9.97. And I can go into more
14 detail now or later with whichever makes sense.

15 **Q. I think it would be a great time now to give a**
16 **brief explanation of what was changed and for what reason.**

17 A. Primarily on this, if you look at this compared
18 to what we filed before, the only thing that changed is
19 what would be the separation factor for intrastate and
20 interstate. Previously what I had done before is I had x'd
21 that out because we agreed with the calculation of
22 Mr. Darren Woolsey as far as what that separation would be.
23 When we first did the calculation we were going off of what
24 his first filed numbers were. Then I believe about three
25 weeks later he filed some amended numbers, which had these

1 second set of numbers in there. Because for whatever
2 reason those numbers didn't get translated through
3 originally I went back in and created the confidential
4 exhibit which now shows those numbers, which I believe are
5 accurate. And if you just do the normal calculations
6 across you will see what we believe would be the correct
7 weighted cost and finally get to the 9.97. So that's the
8 only change. We believe it was accurate to reflect the
9 most recent information that was filed by the Company,
10 which is what we were supporting.

11 And our other numbers don't change as far as
12 what we believe the correct debt to be and also our
13 recommendation for the cost of equity for the Company. If
14 there are other questions, it's pretty straight arithmetic
15 from there, but I can explain that further if need be.

16 **Q. Thank you. With that slight change to your**
17 **testimony on that exhibit, if you were asked the questions**
18 **contained both in your direct and your surrebuttal**
19 **testimony would the answers today be the same as they were?**

20 **A. Yes, they would be.**

21 **Q. Do you have any other edits or corrections that**
22 **you would like to make today?**

23 **A. No.**

24 **Q. Have you prepared a brief statement summarizing**
25 **your testimony?**

1 A. Yes. As the witness for the rate of return for
2 the Division, I went through and did a calculation to try
3 to determine what we believe would be the appropriate
4 allowed rate of return. And as discussed by Mr. Duncan and
5 myself the Division believes the Commission should use the
6 9.97 percent rate.

7 We did agree with Carbon/Emery as far as the
8 cost of debt and that is reflected in the information that
9 I have provided. We also believe, as the Division has done
10 in other times, that the policy of a hypothetical capital
11 structure of 35 percent debt and 65 percent equity should
12 be used. Carbon/Emery does not have any debt, but because
13 of the policy we have done before we are recommending that
14 hypothetical of 35/65. And as reflected on the new updated
15 information we do agree with the separation calculations
16 provided by Carbon/Emery for the weight in between
17 intrastate and interstate there.

18 Where we do disagree and believe the number
19 that should be accurate is for the cost of equity. The
20 Division is recommending a 10.75 percent cost of equity
21 with that. We come to that number by using a capital asset
22 pricing model or CAPM, which has been discussed with that,
23 and doing the same type of analysis which has been done in
24 previous cases and for an extensive period of time by the
25 Division.

1 We believe the Commission should continue to
2 follow some of the same policy that has been done before,
3 the same process that has been done before which is what we
4 have done before and accept the 10.75 percent as a cost of
5 equity and ultimately the 9.97 for the allowed rate of
6 return for Carbon/Emery.

7 **Q. Thank you. I would like to address something**
8 **else briefly on direct testimony.**

9 A. Sure.

10 **Q. The Division recommended cost of equity in this**
11 **case has varied slightly from some previous cases. Can you**
12 **briefly explain why that is?**

13 A. Sure. There has been discussion as far as the
14 rate of return that was used in previous cases to now. The
15 most simple way to explain that is we did an analysis
16 according to when the information was filed. We went and
17 looked at the beta rates that would be applicable for those
18 companies, ones that were still in service and the ones we
19 felt made sense, and then looked at what the risk free rate
20 and risk free premium would be for that time. So there
21 would be an adjustment just because the markets have
22 changed and the scenario has changed a little bit. But our
23 methodology and the way we went through the calculation was
24 basically the same as what would have been done in previous
25 times, it's just with updated information that we feel is

1 applicable in this case and scenario to try to represent as
2 I guess as best you can with what the market conditions
3 would be as of the filing date for Carbon/Emery.

4 MR. JETTER: Thank you. Those are all the
5 direct questions I have for Mr. Coleman. He is available
6 for cross examination.

7 HEARING OFFICER: Ms. Slawson, any questions?

8 MS. SLAWSON: Yes. Thank you.

9 HEARING OFFICER: Go ahead.

10 CROSS EXAMINATION

11 BY MS. SLAWSON:

12 Q. Good afternoon, Mr. Coleman. I want to confirm
13 that you reviewed the testimony and exhibits of
14 Mr. Meredith, Mr. Woolsey and Mr. Johansen filed in this
15 proceeding, correct?

16 A. Yes.

17 Q. In response to your direct testimony the
18 Division is recommending that the Commission adopt the task
19 force's hypothetical capital structure framework for this
20 proceeding; is that correct?

21 A. Yes, we are.

22 Q. Just so I understand, and for benefit of the
23 record, the task force's recommendation was not that the
24 hypothetical capital structure of 35 percent debt and 65
25 percent equity should be used in all cases; is that

1 correct?

2 A. Yes, that's correct.

3 Q. In fact, I believe the task force's
4 recommendation was it would be a sliding scale, correct?

5 A. Yes.

6 Q. And if a company has an actual capital
7 structure with less than 35 percent debt, then 35 percent
8 debt would be imputed to that company; is that correct?

9 A. Yes, that's correct.

10 Q. If the company has an actual capital structure
11 of 45 percent debt, then the Division and the task force
12 recommended that the Commission use the actual capital
13 structure, correct?

14 A. Correct.

15 Q. In your testimony you identified NECA, that's
16 the National Exchange Carrier Association; is that correct?

17 A. Yes, that's true.

18 Q. Did you rely on NECA as an authority to
19 determine the interstate rate of return for Carbon/Emery?

20 A. I guess the best way to explain that is I
21 didn't understand the form 492 as well as I would like to.
22 So I called NECA to try to get a better understanding as
23 far as what the information on there was and asked a
24 variety of questions to help me get a better understanding
25 of that. Through the conversations I came to understand

1 why there were two different forms 492 and what that meant.
2 So I don't know that I necessarily relied on their number,
3 but I used their expertise as far as what the form was to
4 help me come to the conclusion of what I felt was the right
5 interstate return for Carbon/Emery in this proceeding.

6 Q. The revised exhibit that you provided here
7 today shows that the interstate rate of return used by the
8 Division in its calculation is 11.45 percent, correct?

9 A. Yes, that's correct.

10 Q. In your testimony, your direct testimony on
11 line 157 you indicated there was no other viable
12 alternative for calculating the appropriate cost of equity
13 other than the CAPM. Do you recall that testimony?

14 A. You said line 157 of my direct testimony?

15 Q. Yes.

16 A. I'm not seeing that exact quote on line 157,
17 but I might -- I said something similar to that. I don't
18 know if the line matters specifically unless I'm looking at
19 the wrong spot. Okay. Yes, I agree. Sorry.

20 Q. When writing your direct testimony were you
21 aware of NECA's method that calculates the return on equity
22 estimates from the NECA rate of return carriers involved in
23 capital transactions using what Douglas Meredith has
24 identified as free cash flow method?

25 A. I'm not aware of that.

1 Q. You weren't when you wrote your direct
2 testimony, correct?

3 A. Yes.

4 Q. Now in reviewing the testimony you're aware of
5 this approach, correct?

6 A. It is something that Mr. Duncan did provide as
7 another alternative.

8 Q. Mr. Meredith?

9 A. Sorry. Yes.

10 Q. Would you agree that NECA's free cash flow
11 method as identified by Mr. Meredith in his testimony
12 estimates the cost of capital based on actual information
13 conveyed by buyers and sellers of rural access lines rather
14 than generalized market data and proxy companies?

15 A. To be honest with you, as I said before I
16 reviewed it, but that doesn't mean that I'm an expert in
17 that area. And part of what I said in my testimony that I
18 think is still accurate is as the Division we're trying to
19 find something where we can have publicly available
20 information that will help us to be able to come to a rate
21 of return that's acceptable. I don't know if all the
22 information in that report, because I'm not an expert, is
23 publicly available that we can get to it or not. I'm not
24 familiar with the discounted cash flow and the different
25 elements of it. But the reality of it is the Company

1 didn't submit that as a proposal to begin with either. So
2 I went with what was done previously before with what I
3 felt was publicly available information that any party
4 coming to this table could look at it and say that's
5 accurate or not accurate.

6 Q. Okay. But after receiving the testimony in
7 this case -- first of all, would it surprise you to know
8 that information is publicly available?

9 A. It is possible that it is publicly available.
10 It wouldn't surprise me.

11 Q. Would you agree that after receiving and
12 reviewing the testimony in this case, particularly the
13 testimony regarding NECA's free cash flow method, that you
14 could have undertaken the evaluation of that approach,
15 correct?

16 A. I could have, but I think the Division is
17 comfortable with the quotes they did and it's the burden of
18 proof of the Company to put forth something, and they could
19 have done that analysis, but didn't.

20 Q. And wouldn't the free cash flow approach be
21 valuable in assessing Carbon/Emery's cost of equity in this
22 proceeding? Do you think that would have been a valuable
23 exercise to undertake? Just yes or no.

24 A. If I had the information, sure.

25 Q. You have identified here in your testimony, in

1 your prefiled testimony and then in your testimony here
2 today, that the Division recognizes NECA as an authority on
3 certain rural carrier issues, correct?

4 A. I don't know that I ever said NECA was an
5 authority on certain rural carrier issues. I understand we
6 have to go to the form 492, which is filed through NECA to
7 get some of that information.

8 Q. Let's look at your CAPM approach. In your
9 surrebuttal testimony you argue that adjustments to the
10 textbook CAPM shouldn't be made because telecommunications
11 carriers, and specifically rural carriers receiving UUSF
12 support or Universal Service Fund support, are different;
13 is that correct?

14 A. Yes, that was part of my testimony.

15 Q. And it's your testimony that small company
16 premium shouldn't apply to small carriers?

17 A. Correct.

18 Q. In forming your recommendation on small company
19 premium did you review Douglas Meredith's rebuttal Exhibit
20 1 where Dr. Heaton from BYU addresses the small company
21 premium?

22 A. Yes.

23 Q. Dr. Heaton's review and address of small
24 company premium, specifically addresses small company
25 premiums for the telecom sector; is that correct?

1 A. I believe so, yes.

2 Q. Doesn't Dr. Heaton recommend that small company
3 premiums be a minimum adjustment for a CAPM use in the
4 telecom sector?

5 A. He might have said that, yes.

6 Q. In forming your recommendation on small company
7 premiums did you review Douglas Meredith's rebuttal
8 testimony Exhibit 2 where Dr. Billingsley addresses the
9 small company premium specifically for rural carriers?

10 A. Yes.

11 Q. Doesn't Dr. Billingsley recommend that small
12 carriers receive a small company premium of 5.56 percent
13 for the entire sample of rate of return carriers?

14 A. I don't know that I could give you the exact
15 number. I reviewed it, but -- I'll agree if that's what
16 number is in there then that's fine.

17 Q. In your surrebuttal testimony -- in your
18 calculation of the CAPM what level of precision would you
19 apply to your recommendation using the CAPM model?

20 A. I think my calculations were 100 percent
21 accurate if that's the level of precision that you're going
22 for.

23 Q. I'm not talking about the calculation itself,
24 but the determination of the return on equity developed
25 from the CAPM model. Is it precise?

1 A. I think as far as what I said in my testimony
2 is we don't have a huge level of comfort with the CAPM, but
3 we also as the Division were not able to come up with
4 something that was publicly available information that
5 would come to a higher level of precision.

6 **Q. And correct me if I'm wrong, but I believe your**
7 **surrebuttal testimony is silent on Mr. Meredith's proposed**
8 **calculation of the risk free rate used in the CAPM; is that**
9 **correct?**

10 A. Yes. I didn't go that specifically to that
11 aspect of this, but I don't think my being silent means I'm
12 for or against it. His calculation and the way he did the
13 CAPM would have been the same I did, and we could argue
14 over if the rates are accurate or not. I don't know that
15 was the substantial element of what we are getting at in
16 this hearing.

17 **Q. Are you aware that the Federal Reserve is**
18 **ending its quantitative policy and is beginning to increase**
19 **the federal funds interest rate?**

20 A. I know that it slowly happens and it's been
21 talked about for a period of time. Sometimes it hasn't
22 happened as quickly as what they had been suggesting.

23 **Q. As the Federal Reserve increases its interest**
24 **rates what is your expectation in the future of interest**
25 **rates?**

1 A. Well, I think we don't know for sure. The
2 beauty of it is the company can come in if the rates change
3 and ask for an increase or decrease according to that. And
4 we're dealing with the facts as far as what is happening
5 now kind of similar to what Mr. Johansen testified earlier
6 in this hearing.

7 Q. I want to discuss the peer group that you
8 selected for your CAPM model. Were you aware that Hickory
9 Tech was purchased by Consolidated in 2014?

10 A. Yes.

11 Q. Were you aware of that when you provided your
12 testimony?

13 A. Yes.

14 Q. Are you aware that before it was purchased by
15 Consolidated its service area included Southern Minnesota,
16 including the Twin Cities, Northwest and Central Iowa?

17 A. I knew generally where it was serving, but I
18 don't know the exact areas of where it was serving. So no,
19 I don't know to that detail.

20 Q. Would you agree if it is accurate that the
21 service areas included Southwest Minnesota, including the
22 Twin Cities, Northwest and Central Iowa, would you agree
23 that service territory is not comparable to Carbon/Emery?

24 A. Yes, that could be a true statement.

25 Q. Are you aware that the majority of Alteva's

1 revenues were generated from its voice operations and
2 wireless partnerships and not its small ILEC operations?

3 A. I know that there was an amount of revenue that
4 came from that, yes.

5 Q. And two of the other companies that you chose
6 for your model, Earthlink and IDT, they don't have ILEC
7 operations and don't provide basic local exchange services,
8 do they?

9 A. That could be accurate, yes.

10 Q. Are you aware that Fairpoint, a company that
11 you added in this proceeding, is a former Bell operating
12 company that operates within three New England states?

13 A. Yes.

14 Q. Would it surprise you to know that Fairpoint
15 provides service in 17 states?

16 A. Yes, that would be surprising.

17 Q. Would it surprise you to know that Fairpoint
18 employs over 3,000 employees?

19 A. Sure.

20 Q. What about its annual revenues, would it
21 surprise you to learn that Fairpoint had over \$900 million
22 in annual revenue in 2014?

23 A. No.

24 Q. You indicate on line 401 in your surrebuttal
25 testimony that you added companies that would be considered

1 rural. But Cincinnati Bell is a dominant telephone company
2 for Cincinnati, Ohio and it's nearby suburbs in the U.S.
3 states of Ohio, Indiana, and Kentucky. Do you consider
4 Cincinnati Bell to be a rural operating company?

5 A. I'm glad you asked that because I want to try
6 to clarify what I tried to do with that.

7 Q. Let's answer my question first. Do you
8 consider Cincinnati Bell to be a rural company?

9 A. I included it in my list, so I believe parts of
10 it was rural.

11 Q. Consolidated Communications is included in your
12 list. This is a family of companies providing advanced
13 communication services in California, Kansas, Missouri,
14 Illinois, Texas, and Pennsylvania; is that correct?

15 A. I'll agree with you. I didn't look at every
16 single state, but sure.

17 Q. I don't think there is any dispute that none of
18 the companies that you looked at were located in rural
19 Utah, correct?

20 A. Correct. I would have loved to use that
21 information, but it wasn't available.

22 Q. In your surrebuttal testimony lines 179 to 180
23 you were asked in that testimony if the Division's rate of
24 return calculation is fair and reasonable. In your
25 testimony in answering that question you refer to Docket

1 08-046-01 and state, in reviewing the details of Manti
2 Telecom and Carbon I find nothing vastly different between
3 those two companies that would warrant using a different
4 methodology in this case; is that correct?

5 A. That was in my testimony, yes.

6 Q. And that docket was in 2008. I believe the
7 hearing was in 2012; is that accurate, 2011, 2012?

8 A. Sounds correct, yes.

9 Q. Why did you consult a Manti Telecom docket to
10 determine the appropriate return on equity rather than just
11 adopting the return on equity proposed by the Division in
12 Hanksville, which was approved by the Commission less than
13 eight months before Carbon filed its application?

14 A. It's not the rate that we looked at, but
15 instead the methodology that we looked at. And the
16 Commission was pretty clear the Manti order they felt using
17 a CAPM approach, which was the same approach we used in
18 this rate, did produce just and reasonable rates. And so I
19 believe because we need to also again find just and
20 reasonable rates, and if the Commission has already said
21 that way is appropriate to use then we should use that same
22 methodology. And as has been asked before, the rates we
23 used in the case before, which I believe was Hanksville, we
24 did a similar type of approach, we just updated it for this
25 time period. So it's not that we changed the approach and

1 I believe the Commission was pretty clear that was an
2 approach that would lead to just and reasonable rates and
3 so that's why we followed that.

4 **Q. So your testimony is that you used the CAPM**
5 **model in the Hanksville case?**

6 A. We looked at a rate of return using a CAPM
7 model or something like that to come up with what we would
8 consider to be a reasonable rate for Hanksville.

9 **Q. And that was developed in 2014, correct?**

10 A. I believe so, yes.

11 **Q. And when the company used that figure, and**
12 **you're eight months later when it filed the application,**
13 **your testimony here today is the rate had changed based on**
14 **the model?**

15 A. Yes, because what we did is looked at --

16 **Q. Just yes or no.**

17 A. Yes.

18 **Q. Are you aware that the Utah Supreme Court has**
19 **stated that the governing standard in determining return on**
20 **equity is the cost of inducing capital markets to invest in**
21 **utility, not the cost of inducing the utility to invest in**
22 **Utah?**

23 A. I'm not entirely sure what that means and I'm
24 not an attorney. But if I could read it maybe I could
25 better understand what it said, but just something that was

1 read there.

2 Q. You haven't heard of that governing standard,
3 is that what you're saying?

4 A. No.

5 MS. SLAWSON: I don't have any other questions.

6 HEARING OFFICER: Mr. Moore.

7 MR. MOORE: Yes, just a few questions.

8 CROSS EXAMINATION

9 BY MR. MOORE:

10 Q. Turning to the interstate rate of return for
11 Carbon/Emery. Would you agree that the interstate rate of
12 return is dependent on the proper legal construction in
13 Utah Administrative Code Rule 746-360-8(A)(1)?

14 A. Can you direct me maybe to where that is?

15 Q. I can direct you to page 4 of your --

16 A. Rebuttal testimony or direct testimony?

17 Q. Your surrebuttal testimony.

18 A. Okay. You said page 4?

19 Q. Page 4 you cite the rule starting on line 76.

20 A. Okay. R476-360-8.

21 Q. Yes.

22 A. Now if you want to ask that question again so I
23 know what you're asking.

24 Q. Would you agree that the appropriate interest
25 rate of return is dependent upon proper legal construction

1 of this rule?

2 A. Yes.

3 Q. Now you have taken the position under this rule
4 746-360-8 that the proper rate of return in this case is
5 11.45, correct?

6 A. Yes, correct.

7 Q. Could you explain how you came to that
8 conclusion?

9 A. Yes. I think there is some supporting
10 documents to go along with that, but I can also just kind
11 of tell generally. From our understanding there are two
12 forms 492 that is applicable when four different carriers
13 are going to be participating in the NECA. Some of those
14 would be the ones that are going to be offering the variety
15 of different services, and then there are another subset
16 that would basically be providing -- I'm probably going to
17 get the wording wrong, but in essence they're not providing
18 all the services, they're only providing a certain subset
19 of that. And as I looked at the form 492 and also looked
20 at Carbon/Emery and the tariff that I provided basically
21 shows that Carbon/Emery is only participating in the one
22 pool.

23 Q. The common line pool?

24 A. Yes, the common line pool. I'm just going to
25 grab that exhibit so I can talk about it a little bit more

1 accurately. So there are different pools. There is the
2 multiline business and user common line, there is the
3 special access, Ethernet transport services, local
4 switching, local transport and tandem switch transport. So
5 there is a tariff that I provided in my surrebuttal that
6 basically shows Emery Telephone company that would be
7 participating in just the multiline business and user
8 common line pool, but not the other ones that I said after
9 that.

10 In my phone conversation with NECA in trying to
11 determine what that meant, they basically said that the
12 companies who are only participating in the multiline
13 business and user common line would be the ones that would
14 have the first form 492 that is 11.45 and it doesn't have
15 the different interest rates in the interstate calculation
16 for those other pools. And so that's why we believe that
17 by following what the 492 has and that Emery, Carbon/Emery
18 because the way NECA looks at that, again through the
19 conversation I had, is they look at it as a study error.
20 So they may only list Emery Telephone company, but to them
21 that includes Emery, Carbon/Emery and Hanksville as far as
22 that. So we felt as far as the Division that showed that
23 they should be part of that original or the first form 492
24 that shows 11.45 for interstate.

25 Q. And that's a rate for the common line pool?

1 A. Correct, yes.

2 Q. You are also aware, however, that the common
3 line pool only represents a minority of Carbon's business?

4 A. Correct, yes.

5 Q. They also have traffic sensitive pools and
6 special access services, don't they?

7 A. Yes, they do.

8 Q. So the 11.45 percent rate of return is actually
9 for just a minority of their business?

10 A. I guess the best way that I can explain it, I
11 don't have an intimate knowledge of how NECA works. So do
12 they receive 11.45 on all of it or a portion of it, I don't
13 know. I do believe that that's the reference point on the
14 form 492 that shows that's what they get. But I think also
15 if you look in my surrebuttal testimony I do talk about how
16 there could be a potential for an arbitrage position.
17 Because I do agree with what Mr. Moore was saying, they do
18 have other services that they are providing, but I don't
19 know as far as the Division where we could go to a
20 resource, nor does the rule allow to go to another point
21 other than that.

22 And so that's why looking at the rule and the
23 statute the way we did we felt that was the interstate rate
24 not precluding part of what was brought up by the Office in
25 that discussion. But we did feel that the rule, at least

1 the way it was written at that point, would deal with that.

2 **Q. That's not always been your position in this**
3 **case, has it?**

4 A. No. Originally because I had some
5 misinformation or misunderstanding about the form 492 I
6 thought that Carbon/Emery would be in all of the pools and
7 so they would be applicable. That was our original
8 testimony. And then as I understood the form more and had
9 some discussions with Carbon/Emery and those type of
10 classifications, it was really more of an error where I
11 thought it was applicable only to Emery and not realizing
12 that it was a study area versus that company because to me
13 Emery Telephone means something different than
14 Carbon/Emery. So that's why in my original testimony I
15 suggested that it should be a different rate, and
16 subsequently changed it in my surrebuttal testimony.

17 **Q. Isn't it true that you initially believed that**
18 **Carbon was not in the common line pool?**

19 A. I don't know if I said they were not. I just
20 know they weren't in the other pools. So the letter that
21 was provided, and I don't remember the person's name, but
22 basically from NECA to the FCC saying here is our report,
23 they talk about how there are two different reports. I
24 thought they should be in the second form 492 that includes
25 all of the rates of interstate instead of just the one.

1 **Q. That's right. So how did you reconcile these**
2 **two positions?**

3 A. I think I reconcile it just from how I
4 explained it, that I had a misunderstanding from what Emery
5 Telecom meant in the tariff for NECA that they had provided
6 -- or the FCC tariff, sorry, and that meant something
7 different than what Emery Telecom means to me as someone
8 who works in Utah. They had made an entire study area that
9 would incorporate Carbon/Emery, and Emery Telecom and
10 Hanksville. So that's how I would reconcile it. I don't
11 know that we changed our position, but our understanding of
12 the form and what the information was providing changed and
13 so that's why we went with the 11.45.

14 HEARING OFFICER: Did you change your
15 interpretation of the rule?

16 THE WITNESS: No. And my interpretation of the
17 rule didn't change. I believe we were following the rule
18 as it's prescribed.

19 **Q. (By Mr. Moore) Mr. Brevitz is proposing an**
20 **interest rate of 9.4 percent, which would encompass all of**
21 **Carbon/Emery business appropriate interest rate to use. Is**
22 **that your understanding?**

23 A. I don't have it right here in front of me, but
24 I'll accept that that's accurate, yes.

25 **Q. That's basically the --**

1 A. Are you talking on interstate only?

2 Q. Interstate only.

3 A. I believe if I remember correctly that was the
4 right rate for the blending of everything for interstate,
5 yes.

6 Q. And that was what your initial --

7 A. Correct, yes.

8 Q. And that was when you did not believe that
9 Emery was in the common line pool?

10 A. Correct, yes.

11 Q. So your interpretation of the rule provides
12 that if a carrier is in the common line pool and not in the
13 traffic sensitive pool you use the common line pool rate of
14 return of 11.45 percent, but if the carrier is not in the
15 common line pool and not in the other pools you use the
16 blended interest rate of 9.4 percent?

17 A. This has come up before. Looking at the rule
18 492 when we were going through this discussion with
19 different parties and not having as much knowledge of the
20 492 form, I thought it was just going to be one data point.
21 It would be something that we could go to and look at and
22 say there is the number and plug it into the rule. Having
23 gone through this process a couple other times I now
24 realize that there are more layers and complexity to it. I
25 believe that the rule basically requires we have to use

1 form 492(a), and I would think that it would be the one
2 that is applicable for the company according to which pool
3 is it in.

4 What has happened in other proceedings is if a
5 company had all of those pools that they were getting these
6 rates from NECA then we would use the lower interstate
7 rate. If a company is only in the common line pool then we
8 would use, and as we have recommended for Carbon/Emery
9 here, the higher interstate rate of 11.45.

10 **Q. And if the company is in none of the pools**
11 **would you use the blended interstate rate of 9.4, which was**
12 **what was initially --**

13 A. No, I think the way the rule is read is that
14 would come under a different portion of the rule where they
15 would be like an average schedule company that is not part
16 of the NECA pool. And then at that point we would have to
17 determine an appropriate rate. The form 492 is only for
18 those companies that are participating in the NECA pool and
19 is -- I'll probably get this wrong. They're not an average
20 schedule, they're a different type of company. So we have
21 had -- in Manti Telecom they were not a -- we had to do
22 something slightly different for them because of dealing
23 with it. That may not have answered your question, but
24 that's my understanding.

25 **Q. Just one last question which is obvious,**

1 **neither you, nor the personnel at NECA you talked to are**
2 **Utah lawyers?**

3 A. Correct. I'm not a lawyer. I'm a utility
4 technical consultant and that gets me in enough trouble.

5 **Q. And you would agree --**

6 A. And I don't believe the person from NECA was.
7 I don't know for sure, but he was the Western Regional
8 Representative for NECA. I don't know his background, but
9 I wouldn't believe that he was an attorney.

10 MR. MOORE: I'm done. Thank you.

11 HEARING OFFICER: It is time for a break.

12 Let's break for about 15 minutes. When we come back,
13 Mr. Jetter, if you have any redirect we'll pick up with
14 that.

15 (Off the record.)

16 HEARING OFFICER: Mr. Jetter, any redirect?

17 MR. JETTER: I do have a few questions, Your
18 Honor. Thank you.

19 REDIRECT EXAMINATION

20 BY MR. JETTER:

21 **Q. I would like to first start out by asking you**
22 **if you could explain briefly why the Division relies on the**
23 **65/35 limits on both ends, and briefly describe the policy**
24 **reasons behind that.**

25 A. Sure. Thank you. The reason the Division

1 relies on that is because of the capital structure task
2 force and what we feel was a process that allowed
3 interested parties, rural phone companies, other phone
4 companies, and other players to have an opportunity to
5 discuss -- although I don't know that I take issue, but at
6 least an element that's out there.

7 I mean it is possible that a company like
8 Carbon/Emery could come in with 100 percent equity and say
9 we want to go all equity for our rate of return, which the
10 Division was uncomfortable with because that's probably not
11 -- I'm telling them how to manage their business, but from
12 a financial perspective that may not be the most prudent
13 choice for a company in the normal market. But we also had
14 other companies who maybe had 100 percent debt.

15 It wouldn't be very fair for those companies
16 for us to say, well, you know, we think all you should get
17 is your cost of debt and that's your only allowed weighted
18 average cost of capital. So with this task force and with
19 this discussion what we were able to do was say those who
20 are in a relative middle ground, somewhere between 35 and
21 65 private capital structure that for whatever reason they
22 feel is appropriate for their company and is reflective of
23 the market we would accept that. But for those who may be
24 the outliers we're going to pull the high equity companies
25 in, but also maybe provide a little bit more equity to the

1 debt companies to help provide, one, a benefit to the state
2 because they're not getting the full 100 percent equity of
3 what a company would get, but also maybe for a company that
4 is completely or extremely leveraged have a little bit more
5 coming in from a rate of return that would allow them to
6 get their equity portion to a level that I think everybody
7 would agree in a financial community that would be a little
8 bit more acceptable.

9 So part of the reason why the Division went
10 forward with the proposal, even though maybe the Commission
11 didn't accept it in rule, is that it was something that was
12 widely accepted by all parties and it gave a level of
13 comfort to companies coming in to know, okay, if we are 100
14 equity, this is probably what is going to happen is 65/35.
15 So that's why we have adopted it and used it probably since
16 that task force in most of the other cases where it made
17 sense where we either had highly leveraged or a company
18 that was using a high amount of equity to use that
19 hypothetical structure.

20 **Q. Thank you. I would like to ask you a couple**
21 **followup questions also about the peer group of other**
22 **telephone companies that you chose as comparable. Could**
23 **you briefly discuss why you chose the grouping that you did**
24 **and how you came to, I guess, narrow that group.**

25 **A. I think it's pretty clear in my testimony that**

1 I don't -- I mean I'm not completely in love with the
2 capital asset model because there are a couple challenges
3 with it. But the reason where I think it creates value --
4 and this also comes back to the companies -- is we can at
5 least look at some publicly available information and make
6 a determination with the Commission.

7 In looking at the companies, unfortunately
8 there is not very much small rural phone company that are
9 available who are publicly traded. So what I tried to do
10 in looking at the companies was to pick those that I felt
11 at least would be serving in similar areas of the United
12 States that could be considered rural. I know that's a
13 very broad definition. But at least maybe they would have
14 some of their services that they're providing that would be
15 similar to what Carbon/Emery would be doing. I recognize
16 that some of them may be in different lines than what
17 Carbon/Emery was. But also what I was trying to do is if I
18 only had two or three companies then the capital asset
19 pricing model and getting an average for the company
20 doesn't work very well because I could pick three outliers
21 and come up with a rate that maybe wouldn't give us a
22 certain level of comfort.

23 So even though maybe the companies weren't
24 perfect matches for Carbon/Emery, I at least felt that they
25 had some benefit in the fact they gave us data points and

1 were at least offering some type of service that if you
2 stretch the bounds of the definition a little bit could
3 work to get us to a point to where we had a certain number
4 of companies that would be acceptable. And the flip side
5 of that is I've heard both parties who have been pretty
6 unhappy with maybe my list of companies for somewhat valid
7 reasons, but I've never heard anybody suggest other
8 companies that should be included that would make sense. I
9 mean, other than Mr. Meredith did put in AT&T and Verizon
10 and a couple of those other companies, which I purposely
11 excluded because, let's be honest, they're not anywhere
12 close to what Carbon/Emery is doing.

13 And so if there are other companies that makes
14 sense to include, I would be happy to redo a calculation
15 with that. But I don't know of any of them out there that
16 made sense. So I went off what was available at Yahoo and
17 a few other different resources to try to find companies
18 that were telecommunications companies that were at least
19 serving in areas that may be rural.

20 Now grant it I don't know Cincinnati and the
21 outlining areas very well, but sometimes to me Kentucky
22 could be considered in my mind at least rural or some of
23 the challenges that Carbon/Emery may be facing. So that's
24 why the list was kind of compiled the way that it was.

25 **Q. Thank you. I would actually like to ask you a**

1 few more questions about that and direct you to page 12 of
2 Exhibit CE-4.0R and looking at lines 324 and 325. This is
3 the revised rebuttal testimony of Douglas Meredith. This
4 is the calculation that he had compiled. I believe he had
5 used the comparable companies that you had chosen and in
6 addition added AT&T and Verizon; is that accurate?

7 A. Yes. I believe that's what he did with that,
8 yes.

9 Q. Is it accurate to say that the smallest one on
10 the list of any comparable presented here is the Shenandoah
11 Telecommunications?

12 A. That would seem to be accurate, yes. As far as
13 looking at the access line that would be the one that would
14 be closet to my understanding what Carbon/Emery would have.

15 Q. If we were to walk through the calculations
16 that Mr. Meredith did on that company, is it correct to
17 state in column 4 he calculated an unadjusted CAPM of 8
18 percent?

19 A. Yes, that's correct.

20 Q. If we follow that through the debt to equity
21 ratio in fact with Carbon/Emery it would be a zero; is that
22 correct?

23 A. If I understand the way that he calculated the
24 debt to equity that would be accurate because they are 100
25 percent equity.

1 Q. Using the Division's policy of making that
2 adjustment, would that be approximately 0.538, meaning 35
3 divided by 65?

4 A. 5.38 would be -- for the debt to equity, yes.

5 Q. Would that be among the lowest debt to equity
6 ratios of any company on there?

7 A. Yes, it appears that way.

8 Q. Just following that through with the zero ratio
9 there, using that 8 percent, that would flow through into
10 the leveraged CAPM actually used by Carbon/Emery? It would
11 ultimately result again in 8 percent?

12 A. Yes.

13 Q. And then you would potentially add the 3
14 percent using his calculation of a small company premium;
15 is that correct?

16 A. If you were to add a small company premium that
17 he did, yes, the 3 percent would be added on that.

18 Q. And that would result in 11 percent?

19 A. Yes, 8 plus 3 is 11.

20 Q. And that's very similar or close to the 10.75
21 percent?

22 A. That is close to what we had, yes.

23 Q. Just to clarify to make sure this is accurate,
24 in your calculation you did not add a small company
25 premium; is that correct?

1 A. That is correct.

2 Q. But you also did not adjust for any reduced
3 risk by having a Utah Universal Service Fund make up the
4 gap?

5 A. Correct. Basically what I did is I did a
6 straight CAPM calculation, or a textbook calculation to use
7 the words of Mr. Meredith. I looked at the companies, I
8 looked at what would be the beta and then did the math
9 calculation and came up with an average to say this is what
10 we felt the right rate was for Carbon/Emery.

11 Q. That was the same calculation that you used for
12 Hanksville?

13 A. Yes.

14 Q. Same method?

15 A. Same method, yes.

16 Q. Do you know how large Hanksville is?

17 A. I don't know exact numbers, but I know they are
18 a relatively small ILEC. I mean, we're talking less than
19 100 customers.

20 Q. In comparison Carbon/Emery is significantly
21 larger?

22 A. Yes. That could be the AT&T versus
23 Carbon/Emery, could be Carbon/Emery versus Hanksville
24 analysis if you want to look at it that way.

25 MR. JETTER: That's the conclusion of my

1 redirect.

2 HEARING OFFICER: Ms. Slawson, any recross?

3 MS. SLAWSON: Yes, just a little bit.

4 RE CROSS EXAMINATION

5 BY MS. SLAWSON:

6 Q. We were just looking at the table embedded in
7 Mr. Meredith's testimony on page 12, table 2. This is the
8 one that includes Verizon and AT&T. Do you have that in
9 front of you?

10 A. Yes.

11 Q. In this table Mr. Meredith was focussing on
12 adjustments that needed to be made to the CAPM model; is
13 that correct?

14 A. That's what Mr. Meredith testified earlier in
15 the hearing today, and I'll accept that as accurate.

16 Q. Let's look at your exhibit when you're
17 analyzing that CAPM premium.

18 A. Okay.

19 Q. What is the market risk premium that you used?

20 A. Give me just one second so I can pull that up
21 to make sure I have it accurate. It's Exhibit 3.2?

22 Q. Yes.

23 A. Okay. I have one here in front of me. Which
24 area did you want to look at?

25 Q. The market risk premium that you used.

1 A. There is actually two different columns there.
2 There is a T-bill CAPM and a 30 year CAPM. I did use the
3 30 year CAPM, which is looking at the bond. So that's the
4 risk premium that would be in there that came up with the
5 10.75 percent.

6 Q. That's the 6.81 percent, correct?

7 A. Yes.

8 Q. Mr. Meredith used the T-bond, his rate was 5.01
9 percent; is that correct?

10 A. From what he shows on there I believe that is
11 accurate, yes.

12 Q. Would you need to add the additional market
13 risk premium to Mr. Meredith's numbers?

14 A. If you want to do that analysis you could.

15 Q. So I can compare apples to apples, right?

16 A. Sure.

17 Q. Mr. Meredith -- you just testified about
18 Mr. Meredith's Shenandoah number and it was 10.66. What is
19 the CAPM rate that you show for Shenandoah?

20 A. 13.35.

21 Q. And that's an unadjusted number, correct?

22 A. Yes.

23 MS. SLAWSON: I don't have any other questions.

24 MR. MOORE: No questions, Your Honor.

25 HEARING OFFICER: All right.

1 MR. JETTER: I have one followup question.

2 HEARING OFFICER: It's okay with me as long as
3 there is no objection.

4 MR. MOORE: No objection.

5 MS. SLAWSON: I guess I want to hear the
6 question before I insert my objection.

7 REDIRECT EXAMINATION (continued)

8 BY MR. JETTER:

9 Q. My question is just going to ask if the
10 calculation is different between the two Shenandoah based
11 on the beta used for that.

12 A. Am I okay to respond?

13 HEARING OFFICER: I think we can hear your
14 response. Go ahead.

15 THE WITNESS: That kind of gets back to the
16 heart of the capital asset pricing model because what you
17 do is you take the beta and times that by basically a risk
18 free rate -- sorry. You take the beta, you times that by a
19 risk premium and add that on to a risk free rate. So if
20 you look at what I have here for my beta for Shenandoah at
21 the time period of July 29 versus what Mr. Meredith pulled
22 as his beta for Shenandoah, I believe his is just barely
23 below 1, which means it would be a little bit less risky,
24 and I mine is 1.56. That would explain why there would be
25 a significant difference between what he is showing and I'm

1 showing. And I think it also emphasizes the problem if
2 you're trying to look at just one or two companies, the
3 CAPM starts to lose some of its strength and foundation and
4 that's where with my trying to come up with a list of
5 companies that it gets -- where you need enough reference
6 points to come up with a level of comfort.

7 And that's really what my testimony talked
8 about is with the CAPM is it perfect, no, I don't think so.
9 But it at least gets us to a level of comfort where we
10 think we're getting within the right range of what would be
11 reasonable for the cost of equity for Carbon/Emery. So you
12 can see just in that calculation right there and what we
13 did right here, one company can make a significant
14 difference. So getting enough companies on the list is
15 important as well.

16 HEARING OFFICER: Ms. Slawson, anything you
17 want to add or pursue?

18 MS. SLAWSON: One second please.

19 RE CROSS EXAMINATION (continued)

20 BY MS. SLAWSON:

21 **Q. You testified just now that the difference**
22 **would be accounted for by the beta; is that correct?**

23 A. I'm saying that's one potential reason why. I
24 can tell you from a CAPM and if you do a straight
25 mathematic if you take a beta times the risk free rate and

1 add all that in there where if -- I have 1.56 as a number
2 and I have .9 as a number, then the end result is going to
3 be different. I have done the calculation here, and I
4 don't know all the reasons why, but off the top of my head
5 that would be a very easy thing to point to as far as why
6 those percentages and rates of return are different.

7 **Q. And another easy thing to point to would be the**
8 **difference in the market risk premium provided by you and**
9 **Mr. Meredith?**

10 A. Sure. That would be another element of that as
11 well, yes.

12 MS. SLAWSON: That's it for me. Thank you.

13 HEARING OFFICER: Still okay, Mr. Moore?

14 MR. MOORE: Still okay.

15 HEARING OFFICER: All right. Mr. Jetter, your
16 next witness.

17 MR. JETTER: The Division would next like to
18 call Mr. Joseph Hellewell.

19 (The witness is sworn in.)

20 DIRECT EXAMINATION

21 BY MR. JETTER:

22 **Q. Mr. Hellewell, would you please state your name**
23 **and occupation for the record?**

24 A. My name is Joseph Hellewell. I'm a utility
25 analyst for the Department of Public Utilities.

1 Q. Thank you. In the course of your employment
2 with the Division of Public Utilities have you had the
3 opportunity to review the application as well as the
4 testimony filed by the applicant in this docket?

5 A. Yes, I have.

6 Q. Did you create and cause to be filed with the
7 Public Service Commission direct, rebuttal, surrebuttal,
8 and sur-surrebuttal testimony in this docket?

9 A. Yes, I have.

10 Q. Do you have any edits or corrections that you
11 would like to make to your testimony?

12 A. No, I do not.

13 Q. If you were asked the questions that are
14 contained in your prefiled written testimony that you filed
15 today would your answers remain the same?

16 A. Yes, they would.

17 Q. Thank you. Have you prepared a brief statement
18 summarizing your testimony in this docket?

19 A. Yes.

20 Q. Please go ahead.

21 A. At the time of Carbon/Emery Telecom's
22 application I along with other DUP analysts reviewed the
23 application and conducted our normal audit. During this
24 time we reviewed the depreciation method used by
25 Carbon/Emery Telecom and found it to be distorting annual

1 depreciation expense. At this time an adjustment was made
2 to Carbon/Emery's application based on a single asset
3 straight line depreciation method. In our initial direct
4 testimony we outline reasons why Carbon/Emery's group
5 depreciation method was distorting and suggested
6 alternative methods to remedy this. In addition to this
7 depreciation adjustment we also made adjustments for
8 customer migration and under collection based upon
9 Carbon/Emery's tariff process.

10 MR. JETTER: Thank you. I have no further
11 questions for Mr. Hellewell and he is available for cross
12 examination.

13 CROSS EXAMINATION

14 BY MS. SLAWSON:

15 Q. Thank you. Good afternoon, Mr. Hellewell.
16 I'll just jump right in. On lines 259 to 269 of your
17 direct testimony you discuss the DPU adjustment for imputed
18 revenue for migration of customers who currently receive
19 their internet service through Carbon's cable affiliates to
20 the new fiber to the home network that is being constructed
21 by Carbon. Do you recall that testimony?

22 A. Yes, I do.

23 Q. Mr. Woolsey in his rebuttal testimony on lines
24 986 to 1017 describes an increase in revenue to
25 Carbon/Emery that results from the migration of cable

1 internet customers to the fiber to the home network. My
2 question is this, in performing the analysis of the impact
3 per customer per month Mr. Woolsey uses a rate of return of
4 10.5 percent, which includes the Company's requested rate
5 of return on equity of 12.13 percent. Am I correct in
6 reviewing the Division's testimony that the Division agrees
7 with the methodology employed by Mr. Woolsey, but does not
8 agree with the rate of return used by Mr. Woolsey in his
9 calculation?

10 A. Yes, I believe so.

11 Q. And so is it accurate that the Division of
12 Public Utilities is no longer proposing the adjustment
13 amount set forth in lines 259 through 269 of your direct
14 testimony?

15 A. Yes.

16 Q. And is it fair to say that except for the rate
17 of return element involved in this calculation this cable
18 migration issue is not an open issue in the case?

19 A. Yes.

20 Q. The Division in your testimony has used what
21 you call a single asset straight line method; is that
22 correct?

23 A. Yes.

24 Q. And you have provided testimony on that
25 calculation, which results in a depreciation adjustment --

1 I don't want to go into closed session here, so I'm going
2 to say that adjustment found in column G of the Division of
3 Public Utilities Exhibit 1.2SR. That's the exhibit offered
4 by Mr. Duncan. Does that accurately reflect your
5 depreciation adjustment?

6 MR. JETTER: May I have a moment to provide my
7 witness with that?

8 MS. SLAWSON: Sure.

9 THE WITNESS: Yes, that's accurate.

10 Q. (By Ms. Slawson) And this reduces
11 Carbon/Emery's depreciation expense for the test year,
12 correct?

13 A. I'm sorry. Say that one more time.

14 Q. This adjustment decreases Carbon/Emery's
15 depreciation expense for the test period, correct?

16 A. Yes.

17 Q. Is it your testimony that Carbon's reduced
18 depreciation expense will remain constant at that number in
19 2015 after the test year?

20 A. Are you saying that Carbon/Emery's depreciation
21 will remain exactly the same for 2014 and 2015?

22 Q. I'm asking if that's your testimony. Do you
23 think it will remain the same for 2014 and 2015?

24 A. No.

25 Q. Do you think that the depreciation expense will

1 remain constant at the number adjusted in the test year in
2 2016?

3 A. No.

4 Q. 2017?

5 A. Of course not.

6 Q. And what about Carbon's rate base over the next
7 few years, is it your testimony that that will remain
8 constant?

9 A. No.

10 Q. Do you know what the calculated -- have you
11 calculated the anticipated depreciation expense for
12 Carbon/Emery going forward beyond the test year?

13 A. We've run projections, but it hasn't ever been
14 entered into testimony.

15 Q. Do you know what happens with that depreciation
16 expense?

17 A. From the projections that we have run the
18 depreciation -- well, are you referring to Carbon/Emery's
19 group depreciation method, what happens to the depreciation
20 expense?

21 Q. Well, actually I'm wondering if you've done the
22 calculation on what Carbon's depreciation expense will be
23 going forward under either method.

24 A. Well, for the single asset straight line the
25 expense will increase proportionately with what is being

1 added to the rate with what is being capitalized. But
2 under Carbon/Emery's group depreciation the expense is
3 significantly more than it is with the single asset
4 straight line method.

5 Q. But does it remain constant?

6 A. Do you mean is there a constant increase?

7 Q. No. I'm wondering if the test year is
8 representative of the depreciation expense going forward?

9 A. Well, the -- no, it would not be. Carbon/Emery
10 has provided known and measurable adjustments saying that
11 they anticipate having additional assets capitalized that
12 would increase the depreciation expense accordingly.

13 Q. I know theoretically it would increase the
14 depreciation expense. But I'm wondering if you have done
15 the calculation to know what the depreciation expense going
16 forward will actually be so that we can identify whether
17 the test year as proposed by Carbon/Emery or as proposed by
18 the Division with its adjustment is representative of the
19 depreciation expense in the future?

20 A. No. Carbon/Emery chose the test year. So we
21 did calculations based upon the test year that Carbon/Emery
22 has chosen.

23 Q. And you did not do any calculation to see what
24 that depreciation expense would do after the test year?

25 A. Not that's been entered into testimony, no.

1 Q. So whether or not it's been entered into
2 testimony do you know what the depreciation expense does
3 after the test year? If you've performed the calculation
4 do you know what that is?

5 A. I'm sorry. Say that one more time.

6 Q. You said you haven't entered that in testimony,
7 but that you have performed the calculation. Is that an
8 accurate reflection of your testimony?

9 A. Yes, that would be accurate.

10 Q. Even though it wasn't in previous testimony,
11 I'm asking you what the depreciation expense for
12 Carbon/Emery will be going forward?

13 A. I don't know the exact number.

14 Q. Do you have a range?

15 A. No.

16 Q. With regard to the depreciation expense you
17 don't have a range and you don't know what the calculation
18 is, can you say whether it's increasing or decreasing?

19 A. Our calculation show that depreciation expense
20 will continue to increase.

21 Q. Okay.

22 A. Under both methods.

23 Q. It is your testimony that the -- on line 54 of
24 your sur-surrebuttal testimony you indicate that the
25 depreciation method chosen by the company has lasting

1 effects and must be chosen correctly, correct?

2 A. Yes.

3 Q. By way of example you testify that if the
4 depreciation method chosen by the company accelerates
5 depreciation expense it will also accelerate the rate at
6 which accumulated depreciation accrues, thereby
7 accelerating rate base reduction as well, correct?

8 A. Yes.

9 Q. You indicate that in prior accounting periods
10 Carbon has reaped the reward of accelerated depreciation,
11 but with that comes the burden of an accelerated
12 accumulated depreciation count. What you see as the
13 consequence or the burden of Carbon/Emery choosing the
14 group method of depreciation is that the group method also
15 accelerates reduction to Carbon/Emery's rate base; is that
16 correct?

17 A. Yes.

18 Q. Your testimony is that the Division is
19 permitted to make an adjustment to the depreciation expense
20 going forward, but is not permitted to make an adjustment
21 to the rate base. And I believe you testified that this
22 would conflict with the basic tenant that the utility
23 regulation is prospective, correct?

24 A. That is not accurate.

25 Q. Let's look at your testimony there. Starting

1 on line 54 of your surrebuttal testimony -- I'm sorry.

2 Your sur-surrebuttal testimony.

3 A. I'm sorry. The first part was where you quoted
4 the testimony that is accurate, however the second part of
5 the question is not accurate.

6 Q. The second part where I said because it would
7 conflict with the basic tenant that the utility regulation
8 is prospective?

9 A. Right.

10 Q. You're saying that's not accurate?

11 A. Yes. The adjustment that we have proposed is
12 simply an adjustment. We're not proposing that
13 Carbon/Emery change their depreciation method. If the
14 Commission asks Carbon/Emery to change their method then
15 the repercussions of accumulated depreciation would have to
16 be taken into effect on a prospective basis, meaning that
17 we could not go back and change the accumulated
18 depreciation based off the Commission's decision to ask
19 Carbon/Emery to change their depreciation method.

20 Q. And you testified that the Division's
21 depreciation expense adjustment was simply an adjustment of
22 an unreasonably inflated depreciation expense to a
23 reasonable depreciation expense that better matches the
24 actual diminution of value of Carbon's assets during the
25 test year; is that correct?

1 A. Yes.

2 Q. What is the actual diminution of value of
3 Carbon's assets during the test year?

4 A. We feel that because of the acceleration that
5 occurs naturally with the selection of group depreciation
6 method is that the diminution of the assets occur on an
7 accelerated level. So a different method must be chosen to
8 more accurately reflect the assets diminution.

9 Q. Okay. I understand that you don't think that
10 the group method selected by Carbon accurately reflects the
11 actual diminution in value. But what I'm asking you is not
12 about the method, I'm asking you what the actual diminution
13 in value of Carbon/Emery's assets were during the test
14 period?

15 A. Are you asking for the number?

16 Q. Yes, the number.

17 A. I don't have the number in front of me.

18 Q. If you don't know what the actual -- do you
19 have it somewhere?

20 A. I'm going to read off some numbers or I can
21 just tell you where they appear.

22 Q. Tell me where they appear and then we'll decide
23 whether they need it to be in the record.

24 A. Exhibit DPU 1.1D William Duncan.

25 Q. Let me turn there before we move on. Where on

1 **Exhibit 1.1D?**

2 A. It would be column F row 12. That is the
3 proposed depreciation expense by Carbon/Emery. Our
4 adjustment is column G row 12. So the diminution would be
5 column I row 12.

6 Q. Again, I hate to split hairs here, but you're
7 talking about the depreciation expense, the depreciation.
8 What I'm asking is what those assets -- how they actually
9 diminished in value during the test year. Do you know what
10 that is? Did you go and look at the plant?

11 A. We went out and looked at the plant, but I'm
12 not an appraiser so I wouldn't know.

13 Q. Did you go out and look at Carbon/Emery's plant
14 in this case?

15 A. I don't recall. I don't remember.

16 Q. So I guess my question is if you don't know
17 what the actual diminution in value of Carbon's assets were
18 during the test year, how do you know that your method of
19 calculation calculating that depreciation expense better
20 matches the actual diminish in value?

21 A. The acceleration that occurs because of the
22 method chosen on paper, given the test samples that we
23 pulled, there is no way that it could diminish that
24 quickly.

25 Q. But you don't know what the actual diminish

1 value is; is that accurate?

2 A. Correct. Yes, that's accurate.

3 Q. Let's move on. You've noted that in choosing
4 its depreciation method Carbon made a careful and informed
5 decision to use -- well, you've noted that companies use or
6 make a careful and informed decision on which method of
7 depreciation to use; is that accurate?

8 A. Yes.

9 Q. And would it be reasonable to assume that
10 Carbon also made the careful and informed decision to use
11 its methodology for depreciation?

12 A. Yes.

13 Q. Is it reasonable -- Carbon/Emery has elected
14 the group method of depreciation, correct?

15 A. Yes.

16 Q. And I think you testified just a minute ago
17 that the Division is not recommending that Carbon use a
18 different method of depreciation, you're just recommending
19 that the Commission calculate the UUSF using a different
20 method of depreciation; is that correct?

21 A. You're asking whether I -- can you restate the
22 question one more time please?

23 Q. I believe you testified that the Division's
24 position isn't that Carbon/Emery should change its
25 depreciation method; is that correct?

1 A. Yes.

2 Q. Yes, that is correct?

3 A. Yes, that is correct.

4 Q. But you are recommending that for purposes of
5 calculating the Universal Service distribution or
6 disbursement in this case that the Commission should look
7 at or reach the depreciation expense using a different
8 method of depreciation; is that correct?

9 A. Whether the Commission uses group depreciation
10 to arrive at what they believe is a correct expense, single
11 asset straight line, vintage, the FCC method, that's
12 entirely up to them. Our recommendation is that, yes, we
13 adjusted the group depreciation expense down to a level
14 that we felt was representative using a method that we have
15 used for multiple companies across the state.

16 Q. Just so I understand the Division's
17 recommendation, the Division is not suggesting that the
18 single asset depreciation method be applied to assets that
19 are added after the test period, but rather the Division is
20 suggesting that when you looked at the single asset
21 depreciation method you applied it, and I think your
22 language was based upon each capitalized asset having
23 depreciated under a single asset straight line approach
24 since its inception; is that correct?

25 A. Yes.

1 Q. We have established here that Carbon/Emery
2 chose the group asset method of depreciation and used that
3 method to calculate what it believed is an accurate
4 depreciation expense, correct?

5 A. Yes.

6 Q. And the Division is suggesting that that is not
7 an accurate depreciation expense and that the single asset
8 straight line method should be used, or at least was used
9 by the Division to calculate the depreciation expense,
10 correct?

11 A. Yes.

12 Q. So it seems to me that the Division is
13 suggesting or is changing the rules in the middle of the
14 game, effectively eliminating what you call the stable
15 predictable depreciation expense under the group method
16 that Carbon/Emery's management was using for forecasting
17 and planning. Is that not -- are you not doing that?

18 A. Every single company to my knowledge that I
19 have been involved with that has used group depreciation
20 has had an according adjustment on the straight line
21 method. Whether those cases have been settled in the court
22 or out is up to each individual company, but each of those
23 -- we have consistently applied the single asset straight
24 line approach to companies practicing group depreciation,
25 not because we have any fondness or preference over one

1 depreciation method over another, we just feel that the
2 single asset straight line is the most transparent, the
3 most straightforward, the easiest one to duplicate, and the
4 easiest one to communicate back to the companies.

5 Q. Okay. In addition to the single asset straight
6 line method of depreciation that the Division uses to
7 calculate the depreciation expense, in your testimony you
8 identify several other methods of depreciation that you
9 indicate would be Commission approved lives and rates and
10 would be reasonable alternatives for calculating Carbon's
11 revenue requirement; is that correct?

12 A. Yes.

13 Q. And in particular you identify what you call
14 the FCC method as an acceptable method of calculating
15 depreciation expense. So I want to look at that for a
16 minute. On line 223 of your direct testimony you identify
17 a formula that is used by the FCC to recalculate the
18 depreciation rate based on the plant's remaining life,
19 future net salvage, and depreciation reserve ratio. Did
20 you calculate the depreciation expense for Carbon using the
21 FCC method identified on line 223 of your direct testimony?

22 A. No, we did not.

23 Q. As I understand it, the FCC method applies such
24 depreciation rates as will ratably distribute the
25 difference between the net book cost of the plant account

1 and it's estimated net salvage during the known or
2 estimated remaining service life of the plant; is that
3 correct?

4 A. Yes.

5 Q. In other words, the FCC method looks at
6 remaining asset lives to ensure that the depreciation rate
7 is reasonable, correct?

8 A. Yes.

9 Q. And I want you to -- are you familiar with Utah
10 Code 54-7-12.1?

11 A. No.

12 Q. I'll quote that section for you and you can
13 read it together with Mr. Jetter.

14 A. Sure.

15 Q. The Commission shall consider all relevant
16 factors including the alteration of asset lives to better
17 reflect changes in the economic life of plants and
18 equipment used to provide telecommunications services.
19 Does that refresh your recollection as to 54-7-12.1?

20 A. Okay.

21 Q. I believe you referred to this section in your
22 testimony, this section code in your testimony. Do you
23 deny that?

24 A. No, I don't deny.

25 Q. The single asset straight line method that is

1 being recommended or that was used by the Division in
2 calculating the depreciation expense in this case applies
3 the consistent depreciation rate across the expected life
4 of the asset, correct?

5 A. I'm sorry. Say that one more time.

6 Q. So the single asset straight line method
7 applies a consistent depreciation rate across the expected
8 life of an asset, correct?

9 A. Yes.

10 Q. And that depreciation rate is established at
11 the time that the asset is installed, correct?

12 A. Yes.

13 Q. Are there factors that could affect the
14 expected life of an asset?

15 A. Yes.

16 Q. What would those be?

17 A. Any kind of substantial repairs, changes to the
18 asset's nature, any kind of change in the conditions in
19 which it was installed.

20 Q. Obsolescence of the asset?

21 A. Yes.

22 Q. End of life, if a piece of equipment as
23 Mr. Johansen has testified is no longer supported by the
24 manufacturer that could reduce the life of the asset?

25 A. Yes.

1 **Q. And the single asset straight line method of**
2 **depreciation doesn't account for these potential issues; is**
3 **that correct?**

4 A. In the calculation of the expense, no.
5 However, common depreciation practice as implemented by an
6 accountant accounts for these changes as they occur.

7 **Q. How?**

8 A. So if a company asset is all of a sudden struck
9 by lightning then that asset would obviously need to be
10 retired. Then it's removed from the book, it's removed
11 from the asset base, and its corresponding accumulated
12 depreciation is also removed.

13 **Q. But as long as the asset stays in service --**
14 **you're talking about an adjustment that is made after the**
15 **asset is retired from service, correct?**

16 A. Yes.

17 **Q. So doesn't 54-7-12.1 require the Commission to**
18 **consider the alteration of asset lives to reflect changes**
19 **in the economic life of plant and equipment?**

20 MR. JETTER: I'm going to object to that to the
21 extent that it calls for a legal conclusion.

22 HEARING OFFICER: Let's maybe handle it this
23 way. That's what that section says. Are you asking for
24 the Division to explain what it feels it means?

25 MS. SLAWSON: No. Mr. Hellewell identified

1 this section in his testimony. So I was just asking him to
2 -- Mr. Jetter is right. I've represented what that says so
3 there is no question.

4 HEARING OFFICER: Okay.

5 Q. (By Ms. Slawson) You testified that
6 identification of the remaining lives of the asset group on
7 a periodic basis is critical to a properly configured
8 group, correct?

9 A. Yes.

10 Q. In fact, on line 126 of your sur-surrebuttal
11 testimony you criticize Carbon's group asset methodology
12 because you state when additions are made to a group no
13 adjustment is made to the depreciable life of the group; is
14 that correct?

15 A. I'm sorry. Which line again?

16 Q. Line 126 of your sur-surrebuttal.

17 A. Yes.

18 Q. I want to look at that conclusion that you
19 reach and I want to walk you through a depreciation
20 example. It's very simple because I too -- I am a lawyer
21 and not an accountant. So let's say you have an existing
22 group asset that when you put it in service it costs
23 \$1,000. Its life in years is 10 years. What would the
24 annual depreciation expense for that group be?

25 A. \$100.

1 Q. Let's say in year nine you have accumulated
2 depreciation of \$900, correct?

3 A. Yes, under the straight line method.

4 Q. Under the straight line method, right. And you
5 have a net book value -- well, yes, the group method
6 applying straight line depreciation.

7 A. Okay.

8 Q. In year nine if you have accumulated
9 depreciation of \$900, what is the net book value of that
10 asset?

11 A. \$100.

12 Q. And what is the remaining life in years?

13 A. One year.

14 Q. Let's say that group has a piece of copper
15 cable in it that stops working. You replace that copper
16 cable for \$200. So you add that to the group. At that
17 point the entire value of the group asset when it was
18 placed in service would be \$1200, correct, the \$1000
19 original plus the \$200 that you have added?

20 A. Right, that would be the gross book value.

21 Q. And the life in years would remain the same,
22 the straight line depreciation method would remain a 10
23 year depreciable life, correct?

24 A. It depends on what the addition does.

25 Q. So under group methodology what would the life

1 in years for that group be?

2 A. According to Carbon/Emery from what I
3 understand the remaining life would still be one year in
4 which they would depreciate \$300 in the remaining year.
5 No, no. Without doing the math it would be \$1200 divided
6 by 10. So it would be \$120.

7 Q. Great. In year nine the accumulated
8 depreciation of the group is still \$900, correct?

9 A. Yes.

10 Q. And in year nine the net book value of the
11 group with the \$200 addition is now \$300, correct?

12 A. The net book value is \$300 with the addition,
13 yes. It's a complicated example for being a simple one.

14 Q. How many years will it take to depreciate that
15 remaining net book value using the annual depreciation
16 expense of \$120?

17 A. Roughly two and a half years.

18 Q. So it's not accurate to say that Carbon/Emery's
19 group method doesn't make any adjustment to the depreciable
20 life of the group, is it? We've just shown that it does
21 add a year and a half to the plant life?

22 A. In the example you are correct. However, the
23 groups -- when we see Carbon/Emery add things to a group,
24 we don't know if it's a betterment or a repair that's
25 extending the life. All we see is that a new asset is

1 being added to the group. And oftentimes it's a
2 substantial new asset. So we think that an entire new
3 asset, an entire new \$1000 asset is being added to the
4 group. We don't know if it's a change or a repair or what.
5 All we see is the capital additions.

6 Q. So it seems to me -- is it fair to say that
7 your concern is that you're not sure whether Carbon/Emery
8 is actually adjusting the depreciable life of the asset
9 remaining, the actual remaining life of the asset?

10 A. Right. We see no adjustment on the life of an
11 asset that's being repaired.

12 Q. That's different from what you just said
13 because initially you said you're not sure if they're doing
14 that. So is your testimony now that they're not doing
15 that?

16 A. No. My testimony is not that they're not. We
17 do not know.

18 HEARING OFFICER: The testimony is you see no
19 evidence in the record that Carbon/Emery does adjust the
20 life of an asset that has an addition?

21 THE WITNESS: Correct.

22 Q. (By Ms. Slawson) But you will agree that the
23 example that I said was simple and you said turned out to
24 be a little bit complicated shows that under the group
25 method the depreciable life of the asset is increased by a

1 year and a half under that simple example, correct?

2 A. Yes. It is a simplified explanation, but yes.

3 Q. In Mr. Woolsey -- wouldn't the FCC method which
4 specifically requires consideration of the average
5 remaining life more closely align with Utah Code 54-7-12
6 than the single asset straight line method?

7 A. Each asset method is the business of the
8 company that chooses it. I feel like each one could be --
9 as long as it's properly implemented each depreciation
10 method is proper.

11 Q. But you testified here that one of the kind of
12 sticking points is that the depreciable life should reflect
13 the actual life?

14 A. Yes.

15 Q. And 54-7-12 also states, and I'll read it here,
16 that the Commission shall consider all relevant factors
17 including the alteration of asset lives to better reflect
18 changes in the economic life of plant and equipment used to
19 provide telecommunications services, correct?

20 A. Yes.

21 Q. And the FCC method also uses the calculation
22 that includes adjusting the average remaining service life
23 of the asset, correct?

24 A. Of the asset group, yes.

25 Q. And the single asset straight line method does

1 not make any adjustments of the asset lives?

2 A. The single asset approach is done again on a
3 reactionary basis. So as betterments are made to the asset
4 then the CFO or the accountant in charge would make a
5 judgment call to see if that extended the life of the asset
6 or not. It seems the FCC method is doing this as it goes
7 along.

8 Q. Did the single asset straight line method that
9 the Division used in this case to come up with depreciation
10 expense make adjustments to the remaining asset lives of
11 the asset, the remaining life of the asset? Did you make
12 any adjustments?

13 A. No.

14 Q. In Mr. Woolsey's surrebuttal testimony he
15 calculated the depreciation expense using the FCC method.
16 Did you review that testimony?

17 A. Yes.

18 Q. And his testimony was filed on December 18,
19 2015, correct?

20 A. Yes.

21 Q. And you indicate in your sur-surrebuttal
22 testimony that given Carbon/Emery's use of a new method at
23 such a late date the Division was unable to fully review
24 and investigate Mr. Woolsey's implementation of this
25 method, correct?

1 A. Yes.

2 Q. I'm a little confused by that because in your
3 direct testimony filed on August 21st it was you that
4 identified the FCC method as a reasonable alternative for
5 calculating Carbon's revenue requirement, wasn't it?

6 A. Yes.

7 Q. And didn't you have access to all of the data
8 necessary to do the calculation prior to Mr. Woolsey doing
9 the calculation in sur-surrebuttal testimony?

10 A. Yes.

11 Q. If you have never performed this calculation
12 how do you know that the FCC method would be a reasonable
13 alternative as you testified to in your direct examination?

14 A. Because it's a generally accepted depreciation
15 method.

16 Q. And doesn't is also eliminate issues related to
17 inaccurate depreciation life?

18 A. It could if done correctly.

19 Q. Since you haven't done the actual FCC
20 calculation you can't say whether Mr. Woolsey's calculation
21 using the FCC method was performed correctly or
22 incorrectly, can you?

23 A. I'm not an employee of Carbon/Emery so I didn't
24 do their depreciation for them, no.

25 Q. But you reviewed his calculation, correct?

1 A. His FCC method of calculation?

2 Q. Yes.

3 A. Not in its entirety, which is what my testimony
4 reflects.

5 Q. And your testimony is that you couldn't review
6 it in its entirety because you didn't have enough time, or
7 why couldn't you review that in its entirety?

8 A. Time was definitely a substantial factor.

9 Q. But you testified that you had all the
10 information you needed, you identified the method in August
11 and you had a month before your sur-surrebuttal testimony
12 was due; is that correct?

13 A. Yes.

14 Q. You did state on line 161 of your
15 sur-surrebuttal testimony that Mr. Woolsey failed to
16 include several asset groups, which are not included in the
17 most recent depreciation expense calculation. Do you
18 recall that in your testimony?

19 A. Yes.

20 Q. And you identified seven asset groups which you
21 state contain assets and depreciation expense; is that
22 correct?

23 A. Yes.

24 Q. And isn't it true, however, that none of those
25 asset groups which you have identified have any remaining

1 **book value to be depreciated?**

2 A. Under the group depreciation method they do
3 not. However, using single asset straight line they do.

4 Q. Right. But we're talking about the FCC method
5 and adjusting, which is a group method, and adjusting for
6 the average remaining life of the asset group, correct?

7 A. I did not fully review Mr. Woolsey's FCC
8 calculation, so I do not know.

9 Q. So you don't know if it was correct or
10 incorrect?

11 A. A cursory glance shows that they're missing.

12 Q. But those asset groups have no remaining book
13 value, correct?

14 A. I didn't go through every asset group and
15 determine if they have book value or not.

16 Q. Would you agree that if the asset groups have
17 no remaining book value then they're not relevant to the
18 FCC method calculation?

19 A. That would be correct, except for the fact if a
20 company is trying to persuade somebody to adopt their
21 methodology then it would stand to reason that they would
22 at least show that they themselves looked at the groups.

23 Q. But you don't know if he looked at the group or
24 he didn't look at the group, right?

25 A. Yes, that's correct.

1 Q. You testified that the estimated service life
2 is critical to these calculations, correct?

3 A. Sorry?

4 Q. Estimated remaining service life is critical to
5 these calculations?

6 A. To the FCC method, yes.

7 Q. And you haven't offered any testimony that the
8 service life as determined by Mr. Woolsey in his
9 calculation do not properly represent the remaining service
10 life of Carbon's assets; is that correct?

11 A. Yes.

12 Q. I just have a couple more issues here. I want
13 to talk a little bit about the interstate affect that's
14 been identified in the testimony. You haven't performed
15 the depreciation calculation using the FCC method, but you
16 have provided a calculation of the depreciation expense
17 using what you call the single asset straight line method,
18 correct?

19 A. Yes.

20 Q. And I believe you provided a calculation using
21 what you call the vintage method of depreciation, correct?

22 A. Yes.

23 Q. Upon calculating the depreciation expense
24 adjustments using either of those methods, did you make any
25 adjustment for the interstate revenue associated with that

1 adjustment?

2 A. No.

3 Q. Would you agree that if you change a general
4 expense item on the books of Carbon/Emery there is an
5 interstate impact where the jurisdiction separations of the
6 company -- I don't want to use confidential numbers here --
7 are divided between interstate and intrastate
8 jurisdictions?

9 A. Yes.

10 Q. If you don't consider the interstate revenue
11 impact of the depreciation expense adjustment, then next
12 year if Carbon/Emery takes the lower depreciation expense
13 that you're suggesting and applies the jurisdictional
14 percentage to that adjusted lower number, Carbon/Emery will
15 recover less on the federal interstate side for that
16 adjusted depreciation expense; is that correct?

17 A. Sure.

18 Q. And if that happens, then under the total
19 company approach adopted by the Commission Carbon/Emery
20 would be entitled to seek recovery of the revenue shortfall
21 on the interstate side from the state; is that correct?

22 A. Yes.

23 Q. One final issue. You identified in your
24 summary testimony that you carefully examined the books and
25 records of Carbon/Emery, correct?

1 A. Yes.

2 Q. And I've been through your testimony at length
3 and you allude in several places that the UUSF should not
4 be used as an incentive for increase infrastructure
5 investment, but I couldn't find any example where you
6 testified that Carbon/Emery actually did this. Is there
7 anything like that in your testimony?

8 A. Your conclusions are your own.

9 Q. But you --

10 A. My testimony it my testimony.

11 Q. But there is nothing in your testimony about
12 them doing that?

13 A. No, absolutely not. There is no implication
14 that Carbon/Emery is misusing any of the state USF funds.

15 MS. SLAWSON: I have no other questions.

16 HEARING OFFICER: Mr. Moore, you have a very
17 big decision to make. We do need to close today at 5:00.
18 So you can elect to conduct your cross examination of
19 Mr. Hellewell if you have any right now or --

20 MR. MOORE: I have no questions.

21 HEARING OFFICER: All right. Mr. Jetter, you
22 have a very big decision to make. You can elect to do
23 redirect now, or depending on how much time you feel like
24 you need and how much energy you have left, I will let you
25 choose to begin with that tomorrow morning.

1 MR. JETTER: I actually have a fairly brief
2 redirect, so it may be actually easier to press to do it
3 now.

4 HEARING OFFICER: That's fine. Let's go to it.

5 REDIRECT EXAMINATION

6 BY MR. JETTER:

7 Q. I would like to just walk through a few
8 questions with you on redirect.

9 A. Sure.

10 Q. Is it accurate to say that the depreciation
11 number proposed by Carbon/Emery compared to their proposed
12 rate base or the current book value of the assets in
13 service would fully depreciate the entire company's
14 remaining book value in about five years?

15 A. Yes.

16 Q. Is that even plausible, that could be the case?
17 Based on --

18 A. Not unless everything was a computer.

19 MS. SLAWSON: I'm sorry. I didn't hear what
20 you said.

21 THE WITNESS: I said not unless everything was
22 a computer and has that asset life.

23 Q. (By Mr. Jetter) I would like to ask you
24 quickly about the same hypothetical used by Ms. Slawson.
25 In this hypothetical you have a gross book value of initial

1 asset on year one with a 10 year depreciation rate. Using
2 Carbon/Emery's group method year 10 with no additions that
3 would sum set to a zero annual depreciation; is that
4 correct?

5 A. Yes.

6 Q. And let's say hypothetically in year 11 you add
7 another thousand dollar investment that you capitalize in
8 that same group, while the original thousand dollar capital
9 investment remains in service, what would the depreciation
10 be in year 12?

11 A. \$200.

12 Q. So in fact that second asset now would be
13 depreciating at twice the rate of the first asset even
14 though theoretically they should have the same depreciation
15 rate?

16 A. That's correct.

17 Q. And that's because leaving an asset in the
18 group that has lived in that group beyond its service life
19 begins to affect the depreciation of all other assets added
20 later; is that correct?

21 A. Yes.

22 Q. And when you looked at the asset groups that
23 Carbon has used, they include significant amounts in dollar
24 value of assets that are beyond the calculated depreciation
25 life?

1 A. Yes.

2 Q. And those are driving what we would consider
3 significantly increased rates of depreciation?

4 A. Yes.

5 Q. Let me take my hypothetical one step further
6 and let's say we get out to year 20. And now you have
7 \$2000 in gross value that is entirely depreciated based on
8 the group method, but they both remain in service. Now
9 let's say in year 21 you add another asset that would be a
10 10 year depreciable life and let's say its value is \$220 to
11 make the math easy. How quickly would that asset, which
12 presumably under the Commission's 10 year depreciation rate
13 or the company's 10 year depreciation rate, how fast would
14 that asset actually be depreciated under the group method?

15 A. It would be depreciated in one year.

16 Q. And let's take that hypothetical and use it
17 with straight line depreciation. You add your \$1000 asset
18 in year one. Year 10 that would depreciate \$100 per year
19 and that would reach zero in year 10; is that correct?

20 A. Yes.

21 Q. And now at year 11 add \$1000, how would that
22 depreciate over the next 10 years?

23 A. It would depreciate at \$100 for the next 10
24 years.

25 Q. Would that be something you would consider

1 ratably distributing the \$1000 capitalization over the 10
2 year depreciable life?

3 A. Absolutely.

4 Q. In the alternative, if you were depreciating
5 that at \$200 a year, you're depreciating that entirely over
6 five years. Is it also ratably distributing the value over
7 10 years?

8 A. No.

9 Q. And finally with my hypothetical third
10 investment at year 21, would depreciating the entire asset
11 in one year ratably distribute it over a 10 year service
12 life?

13 A. No.

14 MR. JETTER: That is all the redirect I have.
15 Thank you.

16 HEARING OFFICER: Any recross, Ms. Slawson?

17 MS. SLAWSON: Yes, I have just a couple.

18 RE CROSS EXAMINATION

19 BY MS. SLAWSON:

20 Q. You testified that Carbon's assets will -- if
21 the depreciation expense provided by Carbon in its
22 application is accurate, then Carbon's assets will fully
23 depreciate in five years; is that correct?

24 A. That's assuming no additions and no increase to
25 depreciation expense.

1 **Q. And in fact Carbon is adding an additional**
2 **plant, correct?**

3 A. Yes. So a depreciation expense, therefore,
4 should also unreasonably inflate.

5 **Q. Are Carbon's -- one second please. If the**
6 **company is adding an additional plant, but also making**
7 **disposals, the statement that you just made would not be**
8 **accurate; is that correct?**

9 A. Yes. However, Carbon/Emery's disposals do not
10 match in any way their additions. Their additions far
11 exceed the amount at which they're disposing.

12 **Q. Do you believe that Carbon's assets are going**
13 **to fully depreciate in five years even with the additions?**

14 A. Like I said, the situation was holding that
15 everything stands still. I don't know the calculation,
16 however I do feel very strongly that a depreciation cliff
17 will happen somewhere in the future at which no matter what
18 Carbon/Emery adds it will be depreciated in an unreasonably
19 quick manner.

20 **Q. So I have two issues on that. How far in the**
21 **future do you think this depreciation cliff will happen?**

22 A. I don't know.

23 **Q. More than three years?**

24 A. Possibly.

25 **Q. More than five years?**

1 A. Again, I don't know.

2 Q. Do you think it will happen in less than three
3 years?

4 A. I don't know.

5 Q. That was my first question. My second question
6 on this -- my second question is this. It seems that the
7 overarching concern about Carbon's group method of
8 depreciation that the Division has is that it does not
9 accurately reflect the average remaining life of the assets
10 in the group; is that correct?

11 A. Yes.

12 Q. And isn't it true that the FCC method would
13 address this concern that the Division has?

14 A. If properly configured, yes.

15 Q. And by being properly configured you mean if
16 the asset remaining lives are accurately reflected; is that
17 correct?

18 A. Well, all of the components which go into the
19 calculation using the FCC must be properly configured.

20 Q. So average remaining life?

21 A. That's the main sticking point. Because is it
22 average remaining depreciable life, is it average remaining
23 life as it exists in the field. That's the question that
24 needs to be answered.

25 Q. What does the FCC formula say?

1 A. Average remaining life.

2 Q. Wouldn't it make most sense if you're actually
3 trying to figure out when you should retire assets and what
4 the depreciation rate should be, wouldn't it actually make
5 the most sense to figure out what the average remaining
6 life of the asset in the field is?

7 A. Yes.

8 Q. Mr. Jetter asked you about a lot of
9 hypothetical examples. If the average remaining life --
10 wouldn't the FCC method address the concerns that the
11 Division has with those hypotheticals?

12 A. Yes, in part.

13 MS. SLAWSON: I have no other questions.

14 HEARING OFFICER: We are going to adjourn for
15 today. Mr. Jetter, do you have any other witnesses?

16 MR. JETTER: No, that would be the end of the
17 Division's presentation.

18 HEARING OFFICER: So Mr. Moore, tomorrow --

19 MR. MOORE: We have two witnesses.

20 HEARING OFFICER: -- is all yours.

21 MR. MOORE: Fine.

22 HEARING OFFICER: Ms. Slawson, do you need the
23 screen tomorrow?

24 MS. SLAWSON: I need the screen tomorrow. I
25 didn't need it today.

1 HEARING OFFICER: Thank you. This room, I
2 believe, will be locked and secured. I'm going to leave
3 all of my things right where they are. So with that I
4 think we can close.

5 (The hearing adjourned at 5:10 p.m.)

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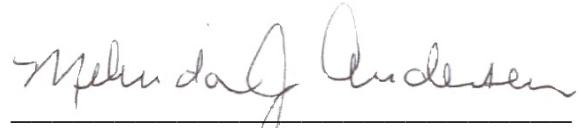
STATE OF UTAH)
:
COUNTY OF SALT LAKE)

I, Melinda J. Andersen, Certified Shorthand Reporter and Notary Public in and for the County of Salt Lake and State of Utah, do hereby certify:

That the foregoing proceedings were taken before me at the time and place herein set forth, and were taken down by me in shorthand and thereafter transcribed into typewritten under my direction and supervision:

That the foregoing 244 pages contain a true and correct transcription of my shorthand notes so taken.

WITNESS MY HAND and official seal at Salt Lake City, Utah this 5th day of February, 2016.



My Commission Expires:
February 10, 2018

Melinda J. Andersen, C.S.R.

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