Docket No. 08-2469-01

Office of Consumer Services

Witness OCS – 1D Michele Beck

Attachment 2

Federal Communication Commission

CC Docket No. 97-249

Transmittal No. 8

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Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 97-249
Beehive Telephone Company, Inc.	)	
Beehive Telephone, Inc. Nevada	)	
	)	Transmittal No. 8
Tariff F.C.C. No. 1	)	

MEMORANDUM OPINION AND ORDER

Adopted: June 1, 1998 Released: June 1, 1998

By the Commission:

I. INTRODUCTION

1. In this Memorandum Opinion and Order, we conclude our investigation of Transmittal
No. 8 filed on December 17, 1997 by Beehive Telephone Company, Inc. and Beehive Telephone, Inc.
of Nevada (collectively "Beehive"). We find that Beehive has failed to meet its burden of proof under
Section 204(a)(1) of the Communications Act (Act), 47 U.S.C. §
204(a)(1), to justify its proposed
interstate traffic sensitive switched access rates that are the subject of this investigation: premium and
non-premium local switching, local transport facility, and local transport termination charges. We
further find for the reasons discussed below that we are unable to rely on supporting information
submitted by Beehive for the purpose of prescribing rates. We, therefore, prescribe rates for these

services using a methodology based on industry averages for comparably sized companies. We direct Beehive to refund to its customers, with interest, the difference between our prescribed rates and the rates filed in December, 1997.

II. BACKGROUND

2. Prior to 1994, Beehive charged interstate local switching and transport rates filed by the National Exchange Carrier Association (NECA) on behalf of incumbent local exchange carriers (LECs) that participate in NECA's traffic-sensitive access tariff. In 1994, Beehive established its own interstate access rates pursuant to Section 61.39 of the Commission's rules, which permits a LEC that qualifies as a small telephone company to file its own tariff for traffic sensitive interstate access charges under more simple rules than those that apply to larger carriers. This methodology generally permits qualifying LECs to base their rates for the next two access tariff years on their actual costs and demand during the previous two calendar years.

3. On July 22, 1997, Beehive filed Transmittal No. 6, which proposed the rates, terms, and conditions under which Beehive would offer interstate access service for the 1997-1999 access years. The Common Carrier Bureau suspended Beehive's tariff filing on August 5, 1997 concluding that it raised significant questions of lawfulness, including whether the proposed rates were unreasonably discriminatory in violation of Section 202(a) of the Act; whether the proposed rates were unjust and unreasonable in violation of Section 201(b) of the Act; and whether Beehive had shown that its proposed traffic sensitive switched access rates were justified under the existing interstate access charge rules.

4. On January 6, 1998, we released the Beehive Tariff Investigation Order, concluding our investigation of the rates filed by Beehive in its 1997 annual access tariff. We found that Beehive had failed to provide an adequate explanation for the sharp increases in its operating costs in 1995 and 1996 and that its premium and nonpremium local switching rates were unjust and unreasonable. In that order, we disallowed Beehive's operating expenses in excess of 25 percent of its total plant in service (TPIS) and prescribed rates for Beehive's premium and non-premium local switching services. We calculated the average ratio of operating expenses to total plant in service among companies with a comparable number of access lines to Beehive in 1995 or 1996 using data

filed with NECA. We found that the average total operating expense to total plant in service ratio among LECs with a comparable number of access lines as Beehive was 21.55 percent. To account for the possibility that Beehive is a high cost carrier, we used an expense to total plant in service ratio of 25 percent. We also directed Beehive to refund the difference between the actual local switching revenues that it obtained between August 6, 1997 and December 31, 1997 and the local switching revenues that it would have obtained during this period based on the rates prescribed by the Commission. Beehive filed a petition for reconsideration of the Beehive Tariff Investigation Order on February 5, 1998 seeking reconsideration of the rate prescriptions and the refund requirements. On May 6, 1998, we released the Beehive Reconsideration Order,which generally denied Beehive's petition in part but found that we should have used Beehive's total 1995/1996 interstate premium and non-premium access minutes.

5. On December 17, 1997, Beehive Telephone Company, Inc. and Beehive Telephone, Inc. of Nevada (collectively "Beehive") filed Transmittal No. 8, which proposed to revise its interstate access service rates in accordance with the Commission's Access Charge Reform Order. Beehive's Transmittal No. 8 proposes per minute switching rates of $0.028252 for premium local switching and $0.01815 for non-premium local switching. Beehive also proposes to reduce its local transport facility rates by approximately 20 percent, and to raise its local transport termination rates by approximately 50 percent.

6. On December 23, 1997, AT&T filed a petition requesting that the Commission suspend and investigate Beehive's Transmittal No. 8, alleging that Beehive had failed to provide supporting documentation with its filing and failed to justify the rates proposed. Beehive submitted additional cost support with its reply to AT&T's opposition and urged the Commission to deny AT&T's request, alleging that Beehive had been prejudiced by AT&T's failure to serve Beehive with AT&T's opposition in a timely manner. On December 30, 1997, the Competitive Pricing Division of the Common Carrier Bureau (Bureau) suspended Beehive's Transmittal No. 8 for one day, initiated an investigation into the lawfulness of this tariff filing, and imposed an accounting order.

7. On March 13, 1998, the Bureau released the Beehive Designation Order, designating for investigation whether Beehive's premium and non-premium local transport facility, local transport

termination, and local switching rates filed in Transmittal No. 8 are just and reasonable. The Bureau directed Beehive to file additional supporting documentation for its actual demand and costs during recent years and designated many of the same issues that were the subject of the investigation of Beehive's 1997 annual access tariff. In particular, the Bureau directed Beehive to explain in detail why its ratio of operating expenses to TPIS, reflected in Transmittal No. 8, is significantly higher than its ratio in 1994 and 1995 and to explain in detail why its operating expenses to TPIS ratio in Transmittal No. 8 is significantly higher than the ratio among LECs with a similar number of access lines. The Bureau also directed Beehive to provide detailed cost data for calendar years 1994, 1995, and 1996 in Table 1 of FCC ARMIS Report 43-01 format; provide all investment, expense, and revenue account balances that it is required to keep as a Class B company under Part 32 of the Commission's rules; show the amounts in the access charge categories in Part 69 of the rules; provide its general ledgers for calendar years 1994, 1995, and 1996; provide a detailed list of all its expenses for corporate operations, plant specific operations, plant nonspecific operations, and customer operations; provide all subsidiary record information for each summary account for corporate operations, plant specific, plant nonspecific, and customer operations expenses required to be kept in accordance with Section 32.12 of our rules; provide information regarding its lease agreements for switching equipment that constitute capital leases or some other type of lease agreement; list all legal expenses included in the general and administrative expenses account, and describe the administrative proceedings or court actions for which Beehive incurred legal costs; and identify the specific costs incurred for each administrative proceeding or court action.

8. The Bureau further directed Beehive to identify all of its nonregulated services, including, but not limited to, any cable, cellular and other wireless services it may offer. Further, the Bureau directed Beehive to show the development of its January 1, 1998 revenue requirement based on its 1995 and 1996 actual costs as adjusted to reflect the Universal Service Order and the Access Reform Order, and to show the development of all traffic sensitive rates, including transport and local switching rates, filed in Transmittal No. 8. Because the cost information filed by Beehive in Transmittal No. 8 reflects several additional changes that Beehive made since it filed cost data in support of Transmittal No. 6, the Bureau further directed Beehive to provide an explanation of each

change made to the cost data filed for Transmittal No. 6 that is reflected in the cost information filed with Transmittal No. 8 and to state the specific reason for each change.

III. PLEADINGS

9. In its Direct Case, Beehive states that its accountant did not record its transactions in accordance with Part 32 of the Commission's rules for the years 1994 through 1996. Beehive explains that its ratio of operating expenses to TPIS was significantly higher in 1995 than its ratio in 1994 because of significant increases in its plant specific and corporate operations expenses, specifically attributable to Beehive's efforts to stimulate usage of its system and to its involvement in extraordinary litigation. Beehive provides cost data for 1994, 1995, and 1996 in Table 1 of FCC ARMIS Report 43-01 format and its general ledgers for calendar years 1994, 1995, and 1996. Beehive also submits its subsidiary record information, and provides information regarding its lease agreements, and copies of the lease agreement covering switching equipment.

10. Beehive also includes a list of legal expenses and an explanation of the proceedings for which Beehive incurred legal costs. Beehive's information regarding nonregulated activities includes information about its provision of customer premises wiring and Internet service, but no information regarding any provision of cable, cellular, or other wireless service. Beehive also provides cost support information that shows the development of its revenue requirement and local switching rates. Beehive explains that its 1995-1996 data differs from the data filed in support of Transmittal No. 6 for the following reasons: (1) Transmittal No. 6 was erroneously based on cost data for only calendar year 1996 instead of for calendar years 1995 and 1996, the total period since Beehive's last annual filing, as required by Section 61.39(b)(ii) of our rules; and (2) Transmittal No. 6 was based on interstate cost data determined using a weighted DEM jurisdictional separations factor.

11. In its opposition, AT&T contends that Beehive's cost support shows that its expenses are excessive in relation to its investment as a result of a revenue sharing agreement between Beehive and Joy Enterprises, Inc. (JEI), a chat line provider operating in Beehive's service area. AT&T also contends that Beehive has failed to justify nearly all of the legal expenses Beehive claims contribute to its high corporate operations expenses. AT&T states that Beehive's cost support contains numerous

entries for which it has provided no explanation and for which it has not met its burden of proof.
AT&T argues that the debits and credits in Beehive's general ledgers are an accounting fiction set up
to mask the fact that Beehive is the owner of JEI, which generates 95 percent of the traffic that
terminates in Beehive's territory. AT&T also alleges that Beehive erred in its local switching
calculations by using exchange minutes of use rather than total company minutes of use.

12. In its rebuttal, Beehive maintains that its relationship with JEI has allowed Beehive to
decrease its access rates. Beehive also disagrees with AT&T's statements regarding its relationship
with JEI and with AT&T's claims that Beehive's legal expenses are unjustified. Beehive also
provides an explanation for the ledger entries that AT&T found objectionable.

VI. DISCUSSION

13. As noted, Beehive states that its accountant has not maintained its cost accounts and
records in accordance with Part 32 of the Commission's rules. Beehive has not explained what
accounting procedures were employed, sought to identify specific departures from Part 32, or the
extent to which its accounting system may have complied in certain respects with Part 32.

14. Moreover, Beehive's cost data supporting its operating expenses show many
inconsistent, questionable, and unexplained entries. For example, Account 6728, Other General and
Administrative Expenses, which under normal Part 32 accounting would include only expenses
incurred to perform general administrative activities not directly charged to the user and not provided
for in other accounts, includes payments to dentists, florists, toy stores, the Immigration and
Naturalization Service, and the Internal Revenue Service. Beehive has not explained these entries.

15. Beehive's cost information also shows numerous unexplained or inadequately
explained entries relating to JEI that raise serious questions regarding whether Beehive's proposed
rates are based on costs legitimately related to the provision of interstate access service. For example,
the record shows substantial, inadequately explained payments to JEI. Prior to 1995 Beehive
compensated JEI for stimulation of traffic at a rate of four cents per minute of traffic originating from
JEI or about $1.2 million per year. Subsequently, this payment terminated, but in 1996 a new charge

arose of $84,000 per month, or approximately $1 million annually for the leasing of switches from JEI. Beehive has submitted a copy of a lease agreement, but this agreement has few of the normal terms and conditions of an operating lease, such as term and descriptions of the switches or capabilities that will be provided. As another example, Beehive's general ledgers for its Utah company in 1995 includes $1,194,110.24 in expense paid to JEI posted to Account 7990 (Nonregulated Net Income), an income account. Subsequently, at the end of 1995, Beehive divided this amount and transferred it to three expense accounts, and then consolidated it and transferred it to yet another account, Account 6540 (Access Expense). Under Part 32, Account 6540 is used for "amounts paid by interexchange carriers or other exchange carriers to another exchange carrier for the provision of access service." Beehive has failed to provide any explanation for this accounting treatment or how any expense associated with JEI could legitimately be for payment by Beehive for provision of access by JEI.

16. Beehive also recorded other payments to JEI in Account 5082 (Access Revenue). Beehive's general ledger for its Utah company reflect debits attributable to JEI which are subsequently nullified by credits in various amounts. Beehive explains these entries as corrections, but it is not clear why these entries for JEI should appear in Beehive's regulated accounts at all or why they were posted as debits when entries to a revenue account are normally posted as credits. As a whole, these entries raise substantial questions of whether Beehive's apparent lack of a regular accounting system leaves ratepayers unprotected from paying imprudent expenses or expenses unrelated to regulated interstate access service. Beehive has not provided any explanation for its relationship with JEI that would rebut concerns raised by its accounting treatment of JEI-related costs.

17. Beehive has additionally failed to show that its litigation expenses should be recovered from ratepayers. It claims that its corporate operating expenses rose in 1995 partly because of its involvement in extraordinary litigation. It states that its legal expenses rose from $274,872 in 1994, to $672,992 in 1995, and then dropped to $272,459 for 1996. These expenses constitute 35.43% of the increase in Beehive's operating costs from 1994 and approximately 20.26% of Beehive's total operating costs for 1995.

18. Under the Other Litigation Costs Order Beehive is entitled to a rebuttable presumption

that all litigation costs "arise out of events occurring in the normal course of providing service to ratepayers, and that ratepayers benefit from provision of service." The presumption may be overcome by evidence that the proceeding was illegal, duplicative, or unnecessary. We find that this presumption is rebutted in several instances by Beehive's own explanation of the nature of the litigation expense. Nor has Beehive otherwise shown that these expenses benefited ratepayers.

19. For example, Beehive seeks to recover in its proposed interstate access charges $562,946 in legal expenses for "shareholder" litigation that its description reveals primarily to be a defense to a property claim that arose from a divorce action filed against Beehive's president, Art Brothers, by Frances Gaines Brothers. Beehive also seeks to recover $51,601 for a breach of contract case brought against Beehive by James E. Ball concerning benefits from an educational trust. These cases do not show any relationship to Beehive's provision of interstate access service to its ratepayers and, thus, the associated legal expenses should not be recovered in Beehive's rates. Beehive also seeks to recover approximately $12,615 in legal expenses for its lawsuit against the City of Wendover and the Federal Aviation Administration in which Beehive sought to lease space at the airport so that Beehive could construct a heated airport hanger for its aircraft. Although Beehive may require aircraft to respond to service outages and customer complaints, as it contends in its direct case and rebuttal, we find that litigation regarding the construction of a heated hanger does not necessarily arise in the ordinary course of providing telecommunications service. Beehive also seeks to recover $204,775 for its lawsuit against US West regarding the Hanksville exchange. In this litigation, Beehive contested the decision of US West to sell the Hanksville exchange to the South Central Utah Telephone Cooperative Association. We do not believe that this litigation was necessary to Beehive's provision of service to its existing ratepayers.

20. Beehive has additionally not adequately explained its net investment costs. It has not explained why its net investment is approximately 55% higher than the net investment of companies with a comparable number of access lines as Beehive. Further, it has not sought to reconcile its net investment claimed in this investigation with net investment claimed in previous proceedings, or explained why it has changed.

21. Under Section 201(a)(1), carriers bear the burden of demonstrating in a tariff

investigation that the proposed rates are reasonable. As part of meeting this burden, carriers developing rates based on costs will ordinarily do so based on books and accounts maintained in accordance with Part 32 of the Commission's rules. Under Part 32, local exchange carriers will maintain investments, revenues, and expenses associated with tariffed telecommunications products and services in specific accounts. Recording costs in specified accounts then serves as the basis for regulatory treatment of those costs as specified in other sections of the Commission rules, including identification of nonregulated costs under Part 64, separation of costs between interstate and state jurisdictions under Part 36, and development of interstate access charges under Part 69. Beehive has chosen not to justify its rates using Part 32 in this way, nor has it provided any other explanation of its accounting treatment of costs that could provide assurance that its costs are presented and identified in a way that would permit development of lawful interstate access charges. This circumstance, combined with the inconsistencies in its costs presented, the questionable entries, its unexplained treatment of costs associated with JEI, and its unjustified legal expenses persuade us that Beehive has failed to meet the burden of justifying its rates in this investigation. We note that these concerns affect all its proposed rates because its unexplained accounting system and its claimed operating costs and net investment are used to support all its proposed traffic sensitive rates. Accordingly, we will prescribe rates for these services.

22. We find additionally that we are not able to base a prescription on any of the operating expense or net investment figures submitted by Beehive. Without an explanation of its system of accounting, if it has employed one, and in light of the other concerns discussed above, we are not persuaded that we could, with any degree of certainty, determine that any rates based on Beehive's expenses and investments, as reported here, are just and reasonable. We will therefore disregard the cost and investment information that Beehive has filed in support of its 1998 access tariff filing and base our prescription on costs of comparable companies as described immediately below.

23. We prescribe Beehive's rates by computing a total interstate revenue requirement based on the average total plant in service and net investment of similar companies using the same sample of comparable telephone companies in NECA that we used in our 1997 access tariff investigation. We then compute the ratio of this revenue requirement to the total interstate revenue

requirement reported in Beehive's Direct Case. The prescribed rates are then computed by multiplying each of Beehive's filed rates by this ratio. Under this approach we preserve the manner in which Beehive has allocated its costs between interstate and intrastate services and among the various traffic sensitive services. We additionally use Beehive's reported interstate minutes of use.

24. Accordingly, as set forth in Table I attached hereto, we prescribe Beehive's interstate revenue requirement by first multiplying 25 percent ratio of total expense to total plant in service, by the sample's average unseparated total plant in service of $3,773,709. We derived the 25 percent factor by first calculating the average total operating expense to total plant in service ratio among LECs with a comparable number of access lines as Beehive. That ratio was 21.55 percent. To account for the possibility that Beehive is a high cost carrier, we used an expense to total plant in service ratio of 25%. This is the same approach we used in our investigation of Beehives 1997 access rates to calculate its expenses for purposes of our prescription, except that we now rely on the sample's average total plant in service, instead of Beehive's data, because we have found the Beehive data unreliable. The resulting operating expenses of $943,427 are multiplied by the interstate allocation factor of 0.6234, which is based on Beehive's reported ratio of interstate to total company plant in service (for 1995 and 1996). This results in the allowable interstate operating expenses of $588,130. The total company return on investment is calculated by multiplying the maximum authorized rate of return of 11.25% by the average interstate net investment for the companies in the NECA sample of $2,244,584. We multiply the resulting total allowed return of $252,516 by 0.4678, the ratio of Beehive's reported interstate net plant to total net plant, to compute allowed interstate return of $118,128. The allowed interstate return is allocated between the two states for income tax purposes by the percent of net plant in each state. This produces taxable income of $96,624 in Utah and $21,504 in Nevada. Beehive reports average interstate fixed charges of $10,499 in Utah, and these are subtracted from $118,128 to calculate the interstate return subject to taxes, $107,629, of which $86,125 is allocated to Utah. Allowance for federal and Utah income taxes are computed, and Beehive's average interstate customer operations expenses are added to form the total allowed interstate revenue requirement of $824,965. The ratio of allowed to reported interstate revenue requirement is 0.3401, which we multiply by Beehive's filed rates to calculate the prescribed rates.

25. Based on these calculations, we prescribe for Beehive a premium local switching rate of $0.009607 per minute of use and a non-premium local switching rate of $0.004323 per minute of use. We prescribe a premium local transport facility rate of $0.000181 per mile per minute of use and a non-premium local transport facility rate of $0.000082 per mile per minute of use. For Beehive's local transport termination, we prescribe a premium local transport termination rate of $0.009179 and a non premium local transport termination rate of $0.004116. We will require Beehive to refund with interest the difference between these prescribed rates and the actual rates charged during the course of this investigation.

26. We find that prescribing rates that are based on the average cost and investment of companies with a comparable number of access lines as Beehive is consistent with our authority under Section 205(a) of the Act. Section 205(a) provides in pertinent part that, whenever "after full opportunity for hearing . . . the Commission shall be of opinion that any charge . . . of any carrier or carriers is or will be in violation of any of the provisions of this Act, the Commission is authorized and empowered to determine and prescribe what will be the just and reasonable charge." As noted in our previous orders where a similar methodology has been successfully implemented, courts have consistently found in the Act a Congressional intent to grant us broad discretion in "selecting methods . . . to make and oversee rates." Courts, and federal agencies with authority to prescribe and oversee rates similar to our own, evaluate whether an established regulatory scheme produces rates that fall within a "zone of reasonableness" rather than insisting upon a single method of determining whether rates are just and reasonable.

V. CONCLUSION AND ORDERING CLAUSES

27. For the reasons stated herein, WE FIND that the rates subject to this investigation and identified in this Order, of Beehive Telephone Company, Inc. and Beehive Telephone, Inc. Nevada are unlawful.

28. IT IS ORDERED that Beehive Telephone Company shall file tariffs within five business days of the release date of this Memorandum Opinion and Order, establishing the premium and non-premium local switching, local transport facility, and local transport termination rates prescribed herein.

29. Accordingly, IT IS FURTHER ORDERED that, pursuant to Sections 4(i), 201(b), 203, 204(a), and 205(a) of the Communications Act, 47 U.S.C. § 4(i), 201(b), 203, 204(a), 205(a), Beehive Telephone Company, Inc. and Beehive Telephone, Inc. Nevada SHALL REFUND to its access customers with compounded daily interest, the difference between the actual local switching, local transport facility, and local transport termination revenues they obtained between January 1, 1998 and the effective date of tariffs filed in response to this order for each rate element and the local switching, local transport facility, and local transport termination revenues that they would have obtained during this period based on rates prescribed in this Memorandum Opinion and Order. Interest shall be computed on the basis of interest specified by the United States Internal Revenue Service.

30. IT IS FURTHER ORDERED that Beehive Telephone Company must submit its plans for issuing refunds to the Common Carrier Bureau for review and approval pursuant to our delegation of authority under Section 0.291 of the Commission's rules, 47 C.F.R. § 0.291, within 30 calendar days of the release date of this Memorandum Opinion and Order.

31. IT IS FURTHER ORDERED that pursuant to Section 204(a) of the Communications Act, 47 U.S.C. § 204(a), the investigation instituted by the Common Carrier Bureau in CC Docket No. 97-249 for Beehive Telephone Company, Inc. and Beehive Telephone, Inc. Nevada, Transmittal No. 8 IS TERMINATED.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary