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**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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<b>In the Matter of the Emery Telephone's</b>	:	<b>Docket No. 15-042-01</b>
<b>Application for an Increase in Utah</b>	:	<b>DPU Exhibit 1.0 R</b>
<b>Universal Service Fund Support</b>	:	
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**REBUTTAL TESTIMONY**

**OF**

**William Duncan**  
**STATE OF UTAH**  
**DIVISION OF PUBLIC UTILITIES**

**August 28, 2015**

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**I. INTRODUCTION**

- Q: Please state your name for the record.**
- A:** My name is William Duncan.
- Q: Are you the same William Duncan that filed direct testimony in this docket?**
- A:** Yes.

**II. PURPOSE AND SCOPE OF TESTIMONY**

- Q: What is the purpose of your rebuttal testimony in this proceeding?**
- A:** My testimony will respond to certain issues raised by Mr. Ostrander and Mr. Brevitz in their direct testimony filed on behalf of the Office of Consumer Services (OCS).
- Q: Please summarize the issues that the Division wishes to address.**
- A:** The DPU has two issues it would like to address. First, the use of a hypothetical capital structure of 65% equity and 35% debt, and second, the use of the NECA DSL tariff as an adequate revenue reimbursement from the unregulated company to the regulated company for the use of regulated infrastructure.
- Q. Please address the use of a hypothetical capital structure and why the DPU is comfortable with this method.**
- A.** Mr. Brevitz addresses this issue on lines 147-154 of his direct testimony. I do not disagree with his statement that the Utah PSC rejected this proposed rule. However, I believe that some context is needed to help the Commission understand why the DPU

23 utilizes this proposed rule as policy. From my perspective, in 2008 when the Utah Rural  
24 Telephone Association (URTA) approached the Commission seeking a rulemaking in this  
25 matter, it really wanted one thing – regulatory consistency. Prior to 2008, the DPU had  
26 used various policies about capital structure. These policies may have started from PSC  
27 rule R746-344-5A which calls for the use of “an average rate base and capital structure.”  
28 While this rule is not a part of R746-360, which defines how USF support is determined,  
29 average (50/50) capital structures were apparently used for several years by the DPU.  
30 Rural ILEC’s came to rely on the 50/50 hypothetical capital structure in making  
31 investment decisions. As time passed, different management in the DPU utilized different  
32 hypothetical and/or a mixture of hypothetical and actual capital structures to determine  
33 USF support. Rural ILEC’s faced a confusing situation, never knowing what the “rules”  
34 would be from case to case.

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36 The DPU saw this a reasonable request – to establish a rule that would provide certainty  
37 and consistency from case to case in the regulatory process. The task force that was  
38 formed to study this question consisted of a broad cross-section of interested parties,  
39 including OCS. That task force met several times during 2008 to develop a rule that all  
40 parties could support.

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42 Although the Commission rejected the proposed rule, in its reply to the DPU the  
43 Commission stated “The general parameter of the rule accompanied by the variability  
44 attempted to be included in the rule proposed may be applied by the Division itself in its

45 interaction with companies”.<sup>1</sup> Consequently, the DPU adopted the proposed rule as  
46 policy, and has been consistent in the application of that proposed rule since that time.

47

48 While the DPU understands the OCS concerns with the 65/35 hypothetical capital  
49 structure, the DPU believes that this proceeding is not the place to make major policy  
50 changes. Adoption of Mr. Brevitz’s 50/50 hypothetical would once again introduce the  
51 regulatory uncertainty the task force was trying to eliminate with the proposed rule. For  
52 example, would the 50/50 hypothetical apply in all cases? This inconsistency in  
53 regulatory practice makes investment decisions difficult in capital intensive industries.

54

55 The DPU would support a much broader proceeding to examine this question that could  
56 ultimately result in consistent practices that could be applied globally. Adoption and  
57 application of a rule for capital structure would give predictability while also allowing  
58 deviation if sufficient evidence shows the rule’s general provision is not in the public  
59 interest in a specific case.

60 Q. Please respond to Mr. Ostrander’s comments concerning Emery’s revenue reimbursement  
61 rate for DSL/Broadband.

62 A. On lines 566 – 585 of his direct testimony, Mr. Ostrander questions the use of Emery’s  
63 reimbursement rate for DSL/Broadband. On line 584, Mr. Ostrander states that “it is  
64 clearly inappropriate for Emery to rely on this prior method in these proceedings after it  
65 has exited the NECA pool.” This is used as support for BCO-1, which allocates 50% of

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<sup>1</sup> See letter to Phil Powlick, PSC Docket No. 07-999-09

66 costs to the unregulated affiliate.

67 The DPU has two comments concerning this statement. First, Emery does use the same  
68 methodology as NECA to arrive at the reimbursement rate for DSL/broadband services.  
69 The Division reviewed Emery's calculation for setting this rate and found it to be a  
70 reasonable proxy for the rate Emery Telephone would be reimbursed if it were still in the  
71 NECA pool. Emery has exited the NECA pool for reasons that can be better articulated  
72 by Emery. Second, does Mr. Ostrander's comment indicate that the reimbursement rate  
73 would be appropriate if Emery were still in the NECA pool?

74  
75 While the DPU recognizes the OCS's concerns in this issue, once again the concept of  
76 regulatory consistency arises. Over the last several years, the DPU has consistently used  
77 NECA tariff rates as the standard for review in determining UUSF support. Adoption of  
78 Mr. Ostrander's 50/50 allocation of interstate costs is a major departure from past  
79 practice. Adoption of the 50/50 allocation of costs also seems somewhat arbitrary since in  
80 Mr. Brevitz's testimony, he suggests that there are a number of appropriate methods from  
81 5% regulated (lines 415-417), to 33% regulated (line 441), to 50% regulated (line 448-  
82 449) If one of these results is adopted, should that same standard be applied in the next  
83 case?

84  
85 The DPU recognizes the evolving nature of the telecommunications industry. Only 10-15  
86 years ago, the Commission regulated telephone companies that also sold internet service.  
87 Now it seems we have internet companies that also sell telephone service. The question

88 of proper cost allocation (or proper revenue reimbursement) is another issue that should  
89 be examined in a broader forum where all interested parties can participate.

90

91 To date, the DPU has not seen fit to evaluate companies' broadband reimbursement rates  
92 on an intensive and case by case basis because the NECA tariff reasonably balances the  
93 need for appropriate reimbursement with the ease of determination for widely varying  
94 companies. Should the Commission find the method inadequate, the Commission should  
95 evaluate reimbursement regimes more broadly in a rulemaking proceeding.

96

97 Q. **Conclusion:**

98 A: In recent years the DPU has generally attempted to treat all rural ILEC's in a consistent  
99 manner and apply the same standards in all cases. The DPU's recommendation in this  
100 case follows those same standards. There are other standards that are not unreasonable.  
101 Generally speaking, the methods presented by Mr. Brevitz and Mr. Ostrander are not  
102 unreasonable, although it is not clear that the final adjustments chosen are free from  
103 arbitrary values. They do represent a significant departure from the consistency the DPU  
104 has tried to achieve.

105

106 When the FCC issued its USF/ICC transformation order in November, 2011, it was  
107 apparent that revenue sources traditionally relied upon by rural ILEC's would be reduced.

108 Unfortunately, those changes are not finalized<sup>2</sup>. With no subsequent change in Utah State  
109 law or PSC rules, it was apparent that requests for UUSF support would increase. Nearly  
110 four years later, that scenario is playing out in the form of an increased number of  
111 applications for increased UUSF support. The applications for UUSF support will likely  
112 only continue. In rejecting the Capital Structure Task force recommendation the  
113 Commission noted:

114 The Commission is also concerned of the impact of a rule in setting just and reasonable  
115 rates under Title 54 where the Commission is required to make its determination based  
116 upon the evidence presented in adjudicative proceedings, based upon the circumstances  
117 facing each company and relevant to the time in which rates will be effective.<sup>3</sup>  
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119 With this explanation, the Commission indicated a desire to evaluate each issue on a case  
120 by case basis. This was three years before the FCC transformation order. With the change  
121 in FCC policy, and sixteen rural ILECs to regulate, it may be time to examine methods  
122 that provide a higher level of regulatory efficiency.

123  
124 At an appropriate time, it may be beneficial to consider these recurring issues in a  
125 rulemaking to provide consistency and predictability. For now, the Commission should  
126 reject the OCS's proposed adjustments in favor of the DPU's recommended methods,  
127 which arrive at reasonable values in light of the regulatory burden and other  
128 considerations that make other methods difficult.

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130 Q. Does this conclude your rebuttal testimony?

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2 The FCC has released seven orders on reconsideration since the original USF/ICC transformation order was released in November, 2011.

3 See PSC letter to Phil Powlick PSC Docket No. 07-999-09

131 A. Yes.