

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of Carbon/Emery Telecom)	
Inc.'s Application for an Increase in)	Docket No. 15-2302-01
Utah Universal Service Fund Support)	Rebuttal Testimony
)	of David Brevitz, C.F.A.
)	For the Office of
)	Consumer Services
)	

NONCONFIDENTIAL - REDACTED VERSION

September 4, 2015

1 Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.

2 A. My name is David Brevitz. My business address is Brevitz Consulting Services,
3 3623 SW Woodvalley Terrace, Topeka, KS, 66614.

4 Q. HAVE YOU PREVIOUSLY FILED DIRECT TESTIMONY IN THIS MATTER
5 ON BEHALF OF THE OFFICE OF CONSUMER SERVICES ("OCS")?

6 A. Yes.

7 Q. WHAT IS THE PURPOSE OF THIS REBUTTAL TESTIMONY?

8 A. The purpose of this rebuttal is to respond to positions taken in the testimony of
9 Casey Coleman on behalf of the Division of Public Utilities ("DPU") and suggest
10 that my direct testimony on those issues should be adopted by the Commission.
11 Specifically I am referring to Mr. Coleman's stated basis for adopting a different
12 hypothetical capital structure (65% equity, 35% debt) than I recommend (50%
13 equity, 50% long term debt), his stated basis for determining Carbon/Emery's
14 rate of return for interstate services (9.40%), and his selection of "comparable
15 companies" for purposes of determining return on equity.

16 **RATE OF RETURN FOR INTERSTATE SERVICES**

17 Q. PLEASE ADDRESS MR. COLEMAN'S RECOMMENDATION OF A 9.40%
18 RATE OF RETURN FOR INTERSTATE SERVICES.

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19 A. Mr. Coleman correctly notes that there are different rates of return reflected on
20 the FCC Form 492 and selects the correct rate of return – 9.40% -- for use in this
21 case. This is the rate of return I recommended to the Commission in my Direct
22 Testimony.

23 **Q. WHAT IS MR. COLEMAN’S BASIS FOR SELECTING THIS RATE OF**
24 **RETURN FROM THE FCC FORM 492?**

25 A. At line 119, Mr. Coleman states “the correct interstate rate to use when
26 calculating the allowed rate of return is the 9.40% which blends the Common
27 Line, Switched Traffic Sensitive and Special Access pools.” This is exactly
28 correct, as specified by the Commission’s rules which require the interstate
29 jurisdictional return to be drawn from a specific FCC Form 492. The
30 Commission’s rules determine which rate of return to use.

31 **Q. DID MR. COLEMAN SELECT THIS RATE OF RETURN FOR THE**
32 **CORRECT REASONS?**

33 A. It appears he may not have selected the correct rate of return for the right
34 reasons, as apparently (per lines 113 - 119) he is hinging the decision on whether
35 or not the particular company is a member of the NECA Common Line Pool or
36 not, and based on phone conversation with NECA management.

37 **Q. IS NECA INDEPENDENT OF CARBON/EMERY TELECOM?**

38 A. No, quite the opposite. "NECA" stands for "National Exchange Carriers
39 Association". NECA is "a membership association of U.S. local
40 telecommunications companies".¹ NECA represents the interests of its member
41 local exchange companies like Emery, and is far from independent of its member
42 companies. NECA's board members are selected from its member incumbent
43 local exchange companies (10 directors), with additional "outside" directors (5
44 directors) who worked for companies or entities that worked for or on behalf of
45 various NECA members.² NECA has an advocacy function on behalf of its
46 members,³ which includes rate of return issues. The person Mr. Coleman spoke
47 with is the Western Region Manager, and a person at that management level
48 would no doubt be well acquainted with current advocacy issues and positions.

49 **Q. WHY IS IT CORRECT TO USE AS THE ALLOWED RATE OF RETURN "THE**
50 **9.4 PERCENT WHICH BLENDS COMMON LINE, SWITCHED TRAFFIC**
51 **SENSITIVE AND SPECIAL ACCESS POOLS"⁴ UNDER THE**
52 **COMMISSION'S RULES?**

53 A. The Commission's rules at Utah Admin. Code § R746-360-8 (A) (1) clearly require
54 calculation of "a weighted average rate of return on capital of the intrastate

¹ <https://www.neca.org/Home.aspx>

² https://www.neca.org/NECA_Board.aspx

³ https://www.neca.org/About_Us.aspx

⁴ Coleman Prefiled Direct Testimony, at line 119.

55 and interstate jurisdiction” (emphasis added). The 11.45% rate of return for the
 56 Common Line pool proposed by Emery comprises only a portion of the interstate
 57 jurisdictional services. It does not include the jurisdictional services of interstate
 58 special access and interstate switched traffic sensitive access, which Mr. Coleman
 59 correctly picks up in his recommendation.

60 **Q. DOES CARBON/EMERY IN FACT HAVE INTERSTATE SWITCHED AND**
 61 **SPECIAL ACCESS SERVICES, AND CAPITAL DEVOTED TO THOSE**
 62 **SERVICES?**

63 A. Yes, Carbon/Emery like all incumbent local exchange companies provides these
 64 services. In fact these other services (unrecognized in the common line rate of
 65 return) are the preponderant part of Carbon/Emery’s interstate jurisdictional
 66 rate base according to Carbon/Emery’s cost separations study, as shown by the
 67 following calculation drawn from Carbon/Emery’s Part 69 distribution of its
 68 interstate rate base in its most recent cost 2014 study (provided in response to
 69 OCS 2.16), which is attached as OCS Exhibit 2R-1 (Confidential).

70 [BEGIN CONFIDENTIAL]

	Source
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]

71

72 [END CONFIDENTIAL]

73 Carbon/Emery's proposed 11.45% drawn from the rate of return for only the
74 common line pool is applicable to only [BEGIN CONFIDENTIAL] [REDACTED] [END
75 CONFIDENTIAL] of Carbon/Emery's interstate jurisdictional rate base, and
76 thus does not meet the Commission's rule, which requires "weighted average
77 rate of return on capital of the intrastate and interstate jurisdiction". Fully
78 [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL] of capital (or rate
79 base) for interstate jurisdictional services is unaccounted for by use of the 11.45%
80 rate of return for only the common line portion of the interstate business. It is for
81 this reason, to be consistent with the Commission's rules, that I recommended
82 use of the full interstate jurisdictional rate of return as shown on the Form 492 -
83 9.40%.

84 **Q. IS THE USE OF THE COMMON LINE ONLY RATE OF RETURN**
85 **INCONSISTENT WITH THE COMPANY'S PROPOSED**
86 **STATE/INTERSTATE SEPARATION FACTOR CONTAINED IN MR.**
87 **WOOLSEY'S EXHIBIT 3?**

88 A. Yes, use of the common line-only rate of return is inconsistent with the
89 state/interstate separations factor proposed by Carbon/Emery. The company's
90 proposed state/interstate separations factors total to 100% as they should, yet the
91 11.45% common line rate of return is applicable to only a relatively small fraction

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92 of that interstate rate base as shown above, leaving the difference identified
93 above unaccounted for under the Commission's rules.

94 **Q. ONE COULD NOTE ON OCS EXHIBIT 3R-1 (CONFIDENTIAL) THAT THE**
95 **"RATE OF RETURN" LINE SHOWS AN INPUT OF 11.25%. SHOULD THIS**
96 **RATE OF RETURN BE USED?**

97 A. No. This return is an assumption used for cost study purposes, based on an FCC
98 rate of return from 1984. It is also contrary to the Commission's rules to use this
99 return, since the Commission's rules explicitly call for earned rate of return as
100 reported on the FCC's Form 492. The earned rate of return for the interstate
101 jurisdiction on that report is the 9.40% which I recommend that the Commission
102 use in this case.

103 **HYPOTHETICAL CAPITAL STRUCTURE**

104 **Q. TURNING TO HYPOTHETICAL CAPITAL STRUCTURE, MR. COLEMAN**
105 **PROPOSES THE USE OF A HYPOTHETICAL CAPITAL STRUCTURE OF**
106 **65% EQUITY AND 35% DEBT, BASED ON A 2008 TASK FORCE REPORT**
107 **FILED WITH THE COMMISSION IN 2008. SHOULD THE COMMISSION**
108 **ACCEPT THIS RECOMMENDATION?**

109 A. No. DPU recommends the 65/35 hypothetical capital structure, indicating at line
110 64 of the Coleman testimony that "the Commission never formally adopted the

111 rule as proposed by the Task Force". This statement does not acknowledge the
112 fact that the Commission explicitly rejected that proposed rule on capital
113 structure in favor of individual company determinations, and appropriate fact-
114 based ratemaking determinations. "The Commission questions the need for the
115 proposed rule, and its potential impact in ratemaking settings." "The
116 Commission is also concerned of the impact of the rule in setting just and
117 reasonable rates under Title 54 where the Commission is required to make its
118 determination based upon the evidence presented in adjudicative proceedings,
119 based on the circumstances facing each company and relevant to the time in
120 which rates will be effective." The complete PSC letter is attached as OCS 2R-2.
121 The Commission should accept the recommendation of a 50/50 hypothetical
122 capital structure as contained in my direct testimony, based on analysis of
123 comparable companies.

124 **COMPARABLE COMPANIES IN RATE OF RETURN ANALYSIS**

125 **Q. BOTH YOUR TESTIMONY AND MR. COLEMAN'S TESTIMONY RELY ON**
126 **"COMPARABLE COMPANIES" THAT DO NOT INCLUDE ANY**
127 **TELECOMMUNICATIONS COMPANIES THAT ARE LOCATED IN UTAH.**
128 **WHY IS THAT NECESSARY AND APPROPRIATE?**

129 **A.** Both Mr. Coleman and I must rely on public information associated with
130 publicly traded companies in order to perform calculations necessary to

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131 determine the cost of capital elements of capital structure and return on equity.
132 There is no public market data for Utah telecommunications companies since
133 these companies are not publicly held with stocks and bonds that trade in public
134 financial markets. If there were publicly traded telecommunications companies
135 in Utah, those companies could be considered for reasonableness for inclusion as
136 “comparable companies” for rate of return analysis purposes. Since there are no
137 such companies, other telecommunications companies which are publicly traded
138 must be reviewed for inclusion in the pool of “comparable companies” for this
139 analysis – recognizing that it is not possible to assemble a pool of companies that
140 are direct analogs to Carbon/Emery. As adjusted below, I believe the pool of
141 “comparable companies” presented in our testimonies is the closest possible pool
142 of “comparable companies” that can be assembled for this analysis – I am aware
143 of no other companies that can or should be included.

144 **Q. MR. COLEMAN’S TESTIMONY IS BASED ON “COMPARABLE**
145 **COMPANIES” AS IS YOUR ANALYSIS OF LEVERAGE RATIOS IN YOUR**
146 **DIRECT TESTIMONY. DO YOU USE THE SAME “COMPARABLE**
147 **COMPANIES” AS MR. COLEMAN?**

148 **A.** There is significant overlap in the companies we each consider comparable, but
149 there are some differences as well. I include CenturyLink (CTL) where Mr.
150 Coleman does not. Mr. Coleman includes additional comparable companies of

151 Atlantic Tele-Network (ATNI); IDT Corporation (IDT); Hickory Tech
152 Corporation (HTCO); Cincinnati Bell (CBB); Otelco (OTEL); Alteva Inc. (ALTV);
153 Earthlink Holdings (ELNK); and FairPoint Communications (FRP).

154 **Q. DO YOU HAVE ANY CONCERNS WITH CONSIDERING THESE**
155 **ADDITIONAL COMPANIES TO BE “COMPARABLE” FOR PURPOSES OF**
156 **RATE OF RETURN ANALYSES?**

157 A. Yes. While I am not opposed to inclusion of additional “comparable companies”
158 on a well-founded basis, most of these companies clearly should not be
159 considered “comparable” or included as follows:

160 1. Hickory Tech Corporation (HTCO) should not be included in any analysis
161 because it no longer exists, and obviously therefore there would not be any
162 public data associated with its operations. Searching for this ticker symbol
163 will yield a screen, but with no financial or operating data, but evidently
164 including an historic “beta” factor which Mr. Coleman included in his
165 analysis. The reason there is no current financial data for “HTCO” is because
166 first Hickory Tech changed its name to Enventis, and then Enventis later
167 merged with Consolidated Communications (CNSL).⁵ Both Mr. Coleman
168 and I include Consolidated Communications as a “comparable company”.

⁵ <http://ir.consolidated.com/releasedetail.cfm?ReleaseID=918875> and
<http://www.dividendchannel.com/symbol/htco/>

- 169 Since Hickory Tech no longer exists, and its operations are included within
170 Consolidated Communications operations, Hickory Tech's data should be
171 stricken from Mr. Coleman's analysis.
- 172 2. Atlantic Tele-Network (ATNI) should not be included in any analysis due to
173 lack of comparability to the U.S. wireline telephony business. According to
174 Atlantic's most recent SEC Form 10-K filing⁶, its business segments are
175 wireless services in US markets under the trade names Commnet and Choice;
176 Island Wireless services in the Caribbean under various tradenames;
177 International telephony in Guyana; Competitive Local Exchange Carrier
178 services under Sovernet, ION, and Essexel tradenames; and renewable
179 energy under the trade name Ahana Renewables. These lines of business lack
180 comparability, and Atlantic should not be included as a comparable company
181 in rate of return analysis in this case.
- 182 3. Cincinnati Bell (CBB) should not be included as a comparable company since
183 it serves a single large and compact metropolitan area and also operates very
184 significant IT services, hardware and data center business, including
185 "managed infrastructure services, IT and telephony equipment sales, and
186 provisional IT staffing services."⁷

⁶ <http://biz.yahoo.com/e/150316/atni10-k.html>

⁷ Cincinnati Bell 2014 SEC Form 10-K at page 8.

- 187 4. IDT Corporation should not be included in any analysis for purposes of
188 determining rate of return in this case due to lack of comparability to the U.S.
189 wireline telephony business. According to its website,
190 through its IDT Telecom division, [IDT] provides retail
191 telecommunications and payment services to help immigrants and the
192 under-banked to conveniently and inexpensively communicate and share
193 resources around the world. IDT Telecom's wholesale business is a
194 leading global carrier of international long distance voice calls. IDT also
195 holds a majority interest in Zedge (www.zedge.net), a mobile content
196 discovery and acquisition platform that includes one of the most popular
197 Apps for Android and iOS.⁸
- 198 5. Alteva Inc. (ALTV) has a small ILEC operation in New York and New Jersey
199 (the former Warwick Valley Telephone Company area) that is a primarily
200 rural service area with approximately 50,000 population, and a larger Unified
201 Communications/Hosted VoIP business.⁹ The company's operations and
202 management appear to me to be very problematic¹⁰, and I would not include
203 this company as a "comparable" company.
- 204 6. EarthLink Holdings (ELNK) should not be included in any analysis for
205 purposes of determining rate of return in this case due to lack of
206 comparability to the U.S. wireline telephony business. According to its
207 website, EarthLink
208 provides managed network, security and cloud solutions for multi-
209 location businesses. We help thousands of specialty retailers, restaurants,

⁸ <http://ir.idt.net/>

⁹ Alteva Inc. SEC Form 10-K, dated March 17, 2015, at page 3.

¹⁰ See for example, GMI Ratings Accounting and Governance Risk Overview", attached as OCS 2R-3.

210 financial institutions, healthcare providers, professional service firms and
211 local governments deliver a reliable and engaging customer experience in
212 their stores and branch offices. We do so by building and managing MPLS
213 WAN networks, by providing virtualized infrastructure, security, hosted
214 voice, secure WiFi and compliance solutions, and by offering exceptional
215 customer care. We operate a nationwide network spanning more than
216 28,000 fiber route miles, with 90 metro fiber rings and secure data centers
217 that provide ubiquitous data and voice IP service coverage. Our EarthLink
218 Carrier™ division sells facilities-based wholesale telecommunications to
219 other providers and our award-winning Internet services connect
220 hundreds of thousands of residential customers across the U.S.¹¹

221 7. I am very familiar with FairPoint Communications (FRP) from many years of
222 working in other states on various FairPoint cases and dockets, including the
223 acquisition case in which FairPoint acquired Verizon's Northern New
224 England operations, and the subsequent bankruptcy case less than two years
225 later. FairPoint does not pay a dividend and is owned by a variety of entities
226 that acquired ownership as a result of the bankruptcy proceeding, and
227 subsequent "distressed capital" (or "vulture fund") investors. FairPoint has
228 yet to earn a profit, and it is unclear if and when it may do so. For these
229 reasons I would not include FairPoint as a comparable company.

230 I am familiar with Otelco from work in other jurisdictions, and it is not
231 unreasonable to include Otelco as a comparable company.

¹¹ <http://ir.earthlink.net/>

232 Q. **WHAT IMPACT WOULD CORRECTION OF THE COMPARABLE**
233 **COMPANIES AND INCLUSION OF CENTURYLINK HAVE ON MR.**
234 **COLEMAN'S COMPUTED 10.75% ROE?**

235 A. These corrections would bring the computed ROE much closer to my
236 recommended 10% ROE.

237 Q. **DOES THIS COMPLETE YOUR PREFILED REBUTTAL TESTIMONY?**

238 A. Yes.