

Kira M. Slawson (7081)
BLACKBURN & STOLL, L.C.
Attorneys for Carbon/Emery Telcom, Inc.
257 East 200 South, Suite 800
Salt Lake City, Utah 84111
Telephone: (801) 521-7900

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF
CARBON/EMERY TELCOM, INC.'S
APPLICATION FOR AN INCREASE
IN UTAH UNIVERSAL SERVICE
FUND SUPPORT

CARBON/EMERY TELCOM, INC.'S
MEMORANDUM IN SUPPORT OF
MOTION FOR PARTIAL SUMMARY
JUDGMENT

DOCKET NO. 15-2302-01

Pursuant to the Utah Public Service Commission's (the "Commission") administrative rules R746-100-1.c and R746-100-3.J and Rules 7 and 56 of the Utah Rules of Civil Procedure, Carbon/Emery Telcom, Inc. ("Carbon/Emery") hereby files this Memorandum in Support of its Motion for Partial Summary Judgment filed contemporaneously herewith. In the Testimony of Bion C. Ostrander and David Brevitz filed by the Office of Consumer Services (the "Office") in this docket, the Office has asked the Commission to adjust and allocate fiber/internet related common costs from Carbon/Emery to its non-regulated affiliate for the affiliate's use of Carbon/Emery's plant to provide internet service to the affiliate's retail customers. (See Testimony of Ostrander, lines 264-267). As a matter of law, as demonstrated herein, the Commission is preempted from making this allocation adjustment.

STATEMENT OF MATERIAL UNDISPUTED FACTS

1. Carbon/Emery is deploying fiber to the home (“FTTH”) facilities within its service territory. (Testimony of Brevitz, OCS-3D, lines 317-319).
2. FTTH local distribution facilities (connections to end-user customers) support multiple services. (Testimony of Brevitz, OCS-3D, lines 343-344; Rebuttal Testimony of D Meredith, lines 463-467).
3. Carbon/Emery’s FTTH facilities support basic voice (including long distance), video services, and broadband internet. (Testimony of Brevitz, OCS-3D, lines 351-359).
4. The Carbon/Emery FTTH network is jointly used for regulated and nonregulated retail services, and by regulated and nonregulated entities. The non-regulated entities and third parties “use” the Carbon/Emery FTTH network by purchasing Wireline Broadband Internet Access Service (“WBIAS”), a regulated interstate service, from Carbon/Emery which the non-regulated affiliates or third parties then use to provide their non-regulated service to their end users. (Testimony of Brevitz, OCS-3D, lines 359-361; Rebuttal Testimony of Douglas Meredith, Lines 501-507).
5. The Federal Communications Commission has determined that when an end-user adds broadband service to an existing local exchange service (such as a bundle of regulated voice service and an affiliate’s unregulated broadband service), the regulated entity such as Carbon/Emery shall assign 25 percent of the FTTH loop cost to the interstate jurisdiction and receives cost recovery for this interstate service through various interstate mechanisms. If an end-user only wants broadband service with no voice component, then 100 percent of the FTTH

loop cost is assigned to the interstate jurisdiction where Carbon/Emery recovers the cost through special access service prices. (Rebuttal Testimony of D Meredith, Lines 521-527).

6. The Office seeks to allocate 50 percent of Carbon/Emery's "intrastate" fiber/internet-related common plant costs and related expenses to its nonregulated affiliate. (Testimony of Ostrander, OCS-1D, lines 411-414).

7. Carbon/Emery offers to the public access to its FTTH infrastructure under Title II of the Communications Act of 1934, as amended, under a common carriage obligation. Any provider may purchase WBIAS as a wholesale component of its Internet/Video/VoIP offering to the public. (Rebuttal Testimony of D Meredith, Lines 480-498).

ARGUMENT

Pursuant to Rule 56(c) of the Utah Rules of Civil Procedure, summary judgment shall be granted if "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *Utah R. Civ. P. 56(c)*.

The material facts to this discussion are set forth above, and are not in dispute. The question is whether the cost allocation adjustment requested by the Office is preempted by federal law; and this is a question of law. As discussed below, as a matter of law, this Commission is preempted from adopting the Office's FTTH loop cost allocation adjustment because it would be a *de facto* jurisdictional separation performed by the state for the purpose of assigning additional costs to an interstate service regulated by the FCC. This is inconsistent with the jurisdictional separation process established exclusively by the FCC.

A. Jurisdictional Separations Process.

According to the Federal Communications Commission, “jurisdictional separations is the process of apportioning regulated costs between the interstate and intrastate jurisdictions.”

(<https://www.fcc.gov/encyclopedia/jurisdictional-separations>). The FCC states:

The primary purpose of separations is to determine whether a local exchange carrier (LEC)'s cost of providing regulated services are to be recovered through its rates for intrastate services or through its rates for interstate services. The first step in the current separations process requires carriers to apportion regulated costs among categories of plant and expenses. In the second step of the current separations process, the costs in each category are apportioned between the intrastate and interstate jurisdictions. Once costs are separated between the jurisdictions, carriers can then apportion their interstate regulated costs among their interexchange services and their intrastate costs among intrastate services. (*Id.*)

As a practical matter, incumbent local exchange carriers (LECs), like Carbon/Emery record their costs pursuant to Part 32 of the FCC’s regulations. *47 C.F.R. §32*. These costs are then divided between regulated and unregulated costs pursuant to Part 64 of the FCC’s regulations. *47 C.F.R. §64*. Because a LEC’s assets may be used for interstate and intrastate purposes, the FCC endorsed a cost-based methodology “designed to attribute with some precision the costs utilities incur to their appropriate interstate or intrastate source.” (*Crockett at 1566*). This cost-based methodology was codified by the FCC in *47 C.F.R. Part 36*.

Under Part 36, incumbent LECs perform a two-part jurisdictional separations process. First, incumbent LECs assign regulated costs to various categories of plant and expenses¹. Second, the costs in each category are apportioned between the intrastate and interstate

¹ Costs may be further disaggregated among service categories. *See 47 C.F.R. §36.123*.

jurisdictions based upon either a relative use factor, a fixed allocator, or by direct assignment, when specifically allowed in the Part 36 rules.

In 1980, the FCC limited the interstate share of common non-traffic sensitive loop costs to 25 percent. Under separations rules, the “gross allocator” assigns 25 percent of each carrier’s loop costs to the interstate jurisdiction. *47 C.F.R. §36.2*. Additionally, under *47 U.S.C. §410(c)*, the FCC is required to refer any proceeding regarding the jurisdictional separations of common carrier property and expenses between interstate and intrastate operations which the FCC may seek to institute pursuant to a notice of proposed rulemaking to a Federal-State Joint Board.

In 1997, the FCC initiated a proceeding seeking comment on the extent to which legislative, technological, and market changes warranted comprehensive reform of the separations process. In the context of that proceeding, the Federal-State Joint Board recommended that, until comprehensive reform could be achieved, the FCC should freeze Part 36 allocation factors for incumbent LECs subject to rate-of-return regulation. The FCC adopted this freeze and has renewed the freeze several times since 2001. Most recently in 2014, the FCC extended the freeze of Part 36 allocation factors for incumbent LECs subject to rate-of-return regulation through June 30, 2017.

B. Jurisdictional Separations in Carbon/Emery.

In this Docket, the Office seeks an adjustment to Carbon/Emery’s allocation of its FTTH facilities costs based on the argument that Carbon/Emery’s FTTH facilities are used for both interstate and intrastate services, and that Carbon/Emery has not properly allocated fiber and/or internet related common costs to its non-regulated affiliate who provides broadband/internet operations over the FTTH facilities. The Office seeks the allocation adjustment “to properly

allocate costs” between the regulated and non-regulated entities for regulatory purposes. The Office expert contends that he is allocating and removing 50 percent of the “intrastate” only portion of the common fiber costs from Carbon/Emery’s regulated operations, and that this is reasonable since he is not allocating “any additional interstate fiber common costs” to the nonregulated affiliate. (Emphasis added)(Testimony of Ostrander, OCS-1D, lines 602-608). However, this position is not supported by law.

It is undisputed that Carbon/Emery’s FTTH facilities in question are used to provide both intrastate and interstate service. Therefore, some system for apportioning costs and investments is necessary to set fair rates for the respective interstate and intrastate services. *See generally, MCI Telecommunications Corp. v. FCC, 750F.2d 135 (D.C. Cir. 1984)*. In fact, as stated by the Ninth Circuit Court in *Hawaiian Telephone Company v. PUC* “when the same plant and equipment is used to provide both interstate and intrastate services and different authorities set rates for these respective services, cost and investment must be apportioned uniformly in order to establish fair rates.” *Hawaiian Telephone Company v. PUC, 827 F.2d 1264, 1275 (9th Cir. 1987)*.

It is also undisputed that the wholesale service used by Carbon/Emery’s non regulated affiliate is an interstate service that Carbon/Emery must offer to all parties. This service is a Title II regulated service with attendant common carriage obligations.

C. The Utah Public Service Commission is preempted by Federal Law from removing reasonable intrastate costs for FTTH facilities from Carbon/Emery’s rate base.

Pursuant to 47 U.S.C. §§151, 152(a), the FCC has exclusive jurisdiction to regulate interstate common carrier services, including the setting of rates. Further, the Communications Act empowers the FCC to prescribe uniform separations procedures, and authorizes the FCC to

determine what portion of the carrier's property shall be apportioned between state and federal jurisdictions. *See 47 U.S.C. §221(c)*.

As indicated above, it is undisputed that Carbon/Emery is a rate-of-return incumbent local exchange carrier that offers WBIAS, including Digital Subscriber Line service (DSL), to its affiliates and other third parties as a wholesale interstate service. Retail providers order WBIAS from Carbon/Emery and then package this wholesale access service with their own services or products to offer to their end-user customers. WBIAS is an interstate service that is regulated by the FCC. Thus, the FCC is responsible for determining the interstate costs that account for the use of FTTH loop plant when providing WBIAS.

The FCC, in Part 36, has determined that when an end-user adds broadband service to an existing local exchange service (such as a bundle of regulated voice service and an unregulated broadband service), the regulated entity such as Carbon/Emery shall assign 25 percent of the FTTH loop cost to the interstate jurisdiction and receives cost recovery through various interstate mechanisms. If an end-user only wants broadband service with no voice component, then 100 percent of the FTTH loop cost is assigned to the interstate jurisdiction where Carbon/Emery recovers the cost through special access service prices.

It is undisputed that Carbon/Emery has allocated the FTTH loop costs in compliance with Part 36 as set forth above (25 percent of the FTTH loop costs to the interstate jurisdiction when the end-user added broadband to an existing local exchange service and 100 percent of the FTTH loop costs to the interstate jurisdiction if the end-user ordered stand-alone broadband service). The Office, however, wants to exclude an additional 50 percent of these FTTH loop costs and expenses from the intrastate costs and assign them to a non-regulated affiliate after the 25

percent allocation of loop costs to the interstate jurisdiction has been made. This “reallocation” or “removal” would effectively eliminate this portion of the intrastate costs of plant and expenses from the rate computations of either the Utah Commission or the FCC. This is not permitted.

As set forth above, there is considerable legal guidance on the separation of costs between interstate and intrastate jurisdictions. The Supreme Court established that this separation is “important not simply as a theoretical allocation of the two branches of the business. It is essential to the appropriate recognition of the competent governmental authority in each field of regulation.” *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133, 148 (1930). The Communications Act of 1934, as amended empowers the FCC to prescribe uniform separations procedures. *Illinois Bell Telephone Company v. Illinois Commerce Commission*, 740 F.2d 566, 567 (7th Cir. 1984). The FCC has prescribed uniform separation procedures in 47 C.F.R. §36.

The State of Utah cannot abrogate the FCC’s uniform separation procedures in its state ratemaking process. Rather, as recognized in *Louisiana Public Service*, 106 S. Ct. 1890, 1902 (1986), it is only after a uniform separations of costs has been applied that a state’s independent rules for intrastate ratemaking can be protected from federal preemption. Additionally, as indicated by the D.C. Circuit Court in the Crockett case:

The Part 36 cost-based separations rules do affect state ratemaking authority to the extent such rules apply to the telephone companies within their jurisdictions. Although each state has great freedom to regulate intrastate rates, once the FCC has applied its jurisdictional separation, that part of the cost base deemed to be interstate is outside the jurisdictional reach of the state regulatory agency.” *Crockett at 1567, citing Hawaiian Telephone Company v. Public Utilities Commission of Hawaii*, 827 F.2d 1264, 1275 (9th Cir. 1987). *Crockett at 1567, citing Smith v. Illinois Bell*, 282 U.S. 133, 150 (1930).

Thus, as demonstrated herein, once a jurisdictional separation of costs has been made by the FCC for interstate services offered under common carriage, this Commission, or any state

Commission for that matter, is preempted from assigning more costs to the interstate jurisdiction or to interstate services. This is more particularly explained by the *Hawaiian Telephone*

Company Court as follows:

If the sum of the intrastate and interstate portions for rate-base allocation purposes were not 100 percent, some costs of plant and expenses would not be included in the rate computations of either [the PUC or the FCC] and the carrier may be deprived of a fair rate of return when interstate and intrastate jurisdictions are both taken into account.”

Hawaiian Telephone Company at 1275, citing Application of Hawaiian Tel. Co, 689 P.2d at 751-52, quoting New England Tel. & Tel. Co. v. Public Utilities Comm’n, 448 A.2d 272, 298 (ME 1982). As stated by the Ninth Circuit court in the *Hawaiian Telephone Company* case, the question is not whether federal separation procedures preempt state ratemaking, but rather “whether federal separations procedures preempt any inconsistent separations adopted, openly or otherwise, by the state for the purposes of establishing the intrastate ratebase.” *Hawaiian Telephone Company at 1275.*

The position of the Office in this case is very similar to the position of the Public Utilities Commission and the Consumer Advocate in the *Hawaiian Telephone Company* case. In *Hawaiian Telephone Company*, the Hawaiian Public Utilities Commission (PUC) and the Consumer Advocate sought review of the judgment of the United States District Court (Hawaii) which issued an injunction requiring the PUC to obey an FCC order that mandated the use of a particular set of jurisdictional separations procedures for the allocations of costs and investment between intrastate and interstate telephone operations. By way of background, in 1972 the FCC determined that Hawaii’s interstate rates should be integrated into the mainland domestic rate pattern. The FCC did not prescribe any separations procedures for Hawaii at that time, rather the Hawaii PUC apportioned costs between interstate and intrastate jurisdictions according to its

own “plan”. Subsequent to 1972, the FCC decided that Hawaii’s integration into the mainland domestic rate pattern should be accomplished by establishing new procedures for interstate and intrastate cost apportionment. The FCC exercised its authority under 47 U.S.C. §410 and established a Federal-State Joint Board to advise it on fair jurisdictional separation procedures for Hawaii. In 1981 the Joint Board recommended use of the separations procedure which was developed through the cooperative efforts of the FCC and utility regulators nationwide, and which had been used in the 48 states for some time. The “Ozark Plan”, as it was called, was codified in 47 C.F.R. §67.1-67.701. The FCC ordered Hawaii to use the Ozark Plan for determination of its interstate and intrastate jurisdictional separations. However, when Hawaiian Telephone Company applied for a rate increase, the Hawaiian PUC initially used the Ozark Plan to calculate rates, but then adjusted the rates downward by 1.1 percent. The District Court found that this “adjustment” was “a fairly transparent and improper attempt to circumvent the FCC mandate” regarding appropriate jurisdictional separations. As stated by the *Hawaiian Telephone Company* court, “The Supremacy Clause does not countenance state policies—in this case a state ratemaking ruling—that may produce results inconsistent with the objectives of a federal statute.” *Hawaiian Telephone Company at 1277, citing Maryland v. Louisiana, 451 U.S. 725 (1981)*.

In the Carbon/Emery Docket, it is undisputed that the federally mandated interstate allocation for FTTH loop costs is 25 percent, and that Carbon/Emery has complied with this Part 36 requirement. With its proposed allocation adjustment, the Office is not suggesting that the FTTH costs and expenses incurred by Carbon/Emery are not reasonable, or are too high. Rather, the Office presumably concedes that the FTTH costs and expenses are reasonable, but

nevertheless excludes an additional 50 percent of those costs from Carbon/Emery's intrastate rate base. The Office claims that this allocation adjustment only allocates a portion of Carbon/Emery's intrastate fiber/internet related common costs to a non-regulated affiliate, and does not allocate any interstate costs, but this is not accurate. Rather this allocation adjustment, like the PUC's adjustment in *Hawaiian Telephone Company*, is a thinly veiled attempt to depart from the required separation of plant and expenses between interstate and intrastate use. In fact, the Office's proposed adjustment/allocation is made precisely because Office thinks that the interstate proportion of the costs set by the FCC at 25 percent is too low. This is not permissible under federal law. The FCC separations procedures authorized by 47 U.S.C. §410(c) and set forth in 47 U.S.C. §36 bind the states. *Hawaiian Telephone Company at 1276, referring to Louisiana Public Service Comm'n v. FCC, 106 S.Ct. 1890 (1986)*. Therefore, this Commission is precluded from accepting the "intrastate fiber/internet-related common cost" adjustment proposed by the Office because it directly conflicts with federal jurisdictional separations law, and as such, is preempted by federal law.

CONCLUSION

In the Testimony of Bion C. Ostrander and David Brevitz filed by the Office of Consumer Services (the "Office") in this docket, the Office has asked the Commission to adjust and allocate fiber/internet related common costs from Carbon/Emery to its non-regulated affiliate for the affiliate's use of Carbon/Emery's plant to provide internet service to the affiliate's retail customers. This proposed allocation conflicts with Part 36 of the FCC regulations and, thus is preempted under federal law. Carbon/Emery is entitled to partial summary judgment on this legal question.

Dated this 11th day of September, 2015.

BLACKBURN & STOLL, LC

Kira M. Slawson
Attorneys for Carbon/Emery Telcom, Inc.

CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the Carbon/Emery Telcom, Inc.'s Motion for Partial Summary Judgment, Docket No. 15-2302-01 was sent to the following individuals by email and/or mailing a copy thereof via first-class mail, postage prepaid (as indicated), this 11th day of September, 2015:

Justin Jetter
Assistant Attorney General
Division of Public Utilities
jjetter@utah.gov

Chris Parker
William Duncan
Dennis Miller
Joseph Hellewell
Paul Hicken
Division of Public Utilities
chrisparker@utah.gov
wduncan@utah.gov
dennismiller@utah.gov
jhellewell@utah.gov
phicken@utah.gov

Robert Moore
Assistant Attorney General
Office of Consumer Services
rmoore@utah.gov

Michele Beck
Danny Martinez
Office Of Consumer Services
mbeck@utah.gov
dannymartinez@utah.gov

Bion C. Ostrander
Ostrander Consulting
bionostrander@cox.net

David Brevitz
Ostrander Consulting
davidbrevitz@att.net

Kira M. Slawson