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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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

CARBON/EMERY TELCOM, INC.'S
PETITION FOR REVIEW AND
CLARIFICATION

DOCKET NO. 15-2302-01

PETITION FOR REVIEW AND CLARIFICATION

Pursuant to Utah Code Ann. §§54-7-15 and 63G-4-301 and Utah Administrative Code R746-100-11, Carbon/Emery Telcom, Inc. (“Carbon”) hereby petitions the Utah Public Service Commission (the “Commission”) for review and clarification of the Commission’s Order on Motion for Partial Summary Judgment issued in this docket on October 15, 2015 (“Order”). Carbon respectfully request review and clarification of the following issues on the following grounds:

1. **Carbon’s Process for Removing Fully-Depreciated Assets from its Rate Base.**

In its Order, the Commission found that “*Carbon does not propose, nor does it claim to have, a process by which its fully depreciated assets might be removed from rate base—and its UUSF*

disbursement adjusted accordingly—in years where Carbon does not apply to have its UUSF subsidy increased or otherwise reviewed.”¹ The foregoing statement presumes that Carbon needs a process by which actively removes fully depreciated assets from its rate base, which misconstrues the group depreciation process and its effect on rate base. With group depreciation there is no such thing as a fully depreciated asset within a non-fully depreciated group. Either the group account is fully depreciated or it is not fully depreciated (since the group account is treated as a single asset). Retirement of a portion of assets within a group account does not impact the rate base because the original cost is charged to the depreciation reserve account (and this same amount is taken out of the group asset plant account) whether or not the particular portion of the group asset has attained the average service life. This method provides for “full depreciation” of the disposal preventing regulatory over or under recovery of plant cost in the form of depreciation. As an asset is depreciated on the books of Carbon, the net book value of that asset decreases with a concomitant increase in depreciation expense. As the net book value of the asset decreases, the rate base of the company also automatically decreases.

There are two ways in which Carbon removes assets from its rate base: 1) depreciation; and 2) disposal of assets (removed from rate base but no financial impact on rate base). An asset group can be fully depreciated, but still in use by the company. But in this case, the fully depreciated asset group does not have any impact on rate base because the net book value of a fully depreciated asset group is zero, the company does not earn any return on that asset group. Therefore, because it is undisputed that Carbon depreciates its assets, Carbon submits that the Commission erred when it stated that Carbon does not have a process by which it removes fully

¹ *In the Matter of the Application of Carbon/Emery Telecom, Inc. for an Increase in UUSF*, Docket No. 15-2302-01, Order on Partial Summary Judgment dated October 15, 2015, p.3.

depreciated assets from its rate base. Depreciation of assets is one method by which Carbon systematically removes value from rate base until the asset is fully depreciated and is no longer present in the rate base. Additionally, Carbon disposes of assets. In 2014 Carbon disposed of approximately \$307,000 in assets. Disposals are done in the regular course of business when, for example, plant is no longer in service due to replacement, obsolescence, or abandonment.

Further, Carbon seeks review with regard to the Commission's statement that there is no process by which Carbon's UUSF disbursement can be adjusted in years when the company does not apply for an increase in UUSF. This statement overlooks the duties and rights of the Commission and the Division of Public Utilities ("Division") to periodically review Carbon's books and records to verify eligibility for UUSF support and compliance with applicable state and federal laws. *R746-360-3.G*. Further, there can be no dispute that both the Commission and the Division have the authority to inspect the books and records of the company,² or that Carbon has an obligation to provide the Public Service Commission Annual Report in which, among other things, Carbon identifies its annual depreciation expense, plant additions and plant disposals.³

The Division and the Commission have full authority to review Carbon's Annual Report and its books and records to verify its eligibility for UUSF support whether or not Carbon files

² Under Utah Code Ann. §54-7-7, "the commission, each commissioner and each officer and person employed by the commission shall have the right at all times to inspect the accounts, books, papers and documents of a public utility." Additionally, under *R746-340-2*, each telecommunications corporation shall make its books and records open to inspection by representatives of the Commission, the Division of Public Utilities, and the Office of Consumer Services.

³ Under Utah Code Ann. §54-3-21, Carbon is required to furnish the Commission with such forms and detail as the Commission may prescribe. Pursuant to *R746-400-4*, the Division is required to promulgate forms and/or reports used in the administration of the State Universal Public Telecommunications Service Support Fund. *R746-360-3* requires Carbon to provide access to the Division as the administrator of the UUSF to the books and records of the company to confirm the level of eligibility for USF support.

an application for an increase in UUSF support.⁴ Carbon seeks clarification of that portion of the Commission's Order which seems to indicate that the Carbon's eligibility for UUSF is only subject to review when and if Carbon files an application for an increase in the UUSF support and that Carbon is responsible for ensuring that the Commission and Division properly review Carbon's annual report.

2. **Single Asset Depreciation versus Group Asset Depreciation.** In its Order the Commission seemed to use "single asset depreciation" interchangeably with "straight-line depreciation." For example, on page 3, the Commission states "*Carbon does argue that accelerating depreciation of its newer assets removes them from the rate base more quickly than would be the case if the newer assets were depreciated under the straight-line method. . .*" This misstates Carbon's argument. Carbon submits that the Commission erred in using "straight-line" interchangeably with "single asset." Otherwise, the above referenced statement demonstrates a fundamental misunderstanding of Carbon's Motion for Partial Summary Judgment. In its Motion, Carbon states that Carbon calculates depreciation expense using a straight-line calculation in conformity with a group plan of accounting as prescribed by Federal Communications Commission (FCC) in the Code of Federal Regulations, Title 47, Chapter I, Subchapter B, Part 32. FCC Part 32.2000 and 32.9000. The Division argues that Carbon should use a single-asset straight-line calculation for depreciation. Thus, the issue is not whether Carbon should be required to use a straight-line calculation. The issue is whether Carbon should be required to use a single asset rather than a group asset method. Both the single asset and the group asset method use straight-line depreciation. The difference is whether the depreciation

⁴ Such review may be further complicated if Carbon is required to maintain separate depreciation methods for interstate and intrastate assets as indicated below.

rate is applied to individual (single) assets, or whether the depreciation rate is applied to the group of assets as a whole.

Under a group asset plan of depreciation, group assets are treated as a single entity for the purpose of depreciation. These assets may reside in different locations, or they may be in different stages of their service lives.⁵ Nevertheless, the group's collective cost is consolidated and depreciated as if it were that of a single asset using a properly weighted average service life. Each group asset is associated with an average service life that is usually set by the local regulatory agency, in this case the Commission. A group plan of depreciation uses the assets' remaining average service life to calculate a group depreciation rate. The group depreciation rate is usually calculated annually and remains fixed for the entire year. This rate is applied to the asset's depreciable basis (the sum of the depreciable bases of its group members) to calculate depreciation expense. Depreciation expense is booked to general ledger by applying the depreciation rate either to an average account balance for the period (using an averaging option) or to actual activity for the period. Average service life calculations provide the basis for calculating average remaining life for a group of assets. Because depreciation rates are calculated by using remaining service life at the group asset level, and depreciation also takes place at the group asset level, it is not possible to over-depreciate group members. The group asset method uses straight-line depreciation applied to the "asset group" rather than each individual asset in the group.

⁵ See Exhibit 1 of Carbon's Reply Memorandum, Summary from Moss-Adams regarding Component, Group and Composite Depreciation (U.S. GAAP); and Exhibit 2, Price Waterhouse Coopers, Accounting for Property, Plant and Equipment, Asset Retirement Obligations and Depreciation, p.1.Moss-Adams.

By interchanging the “single-asset” with “straight-line” the Commission’s Order is confusing and inaccurate. The Commission should modify its Order accordingly.

3. **Rule R746-340-2.D adopts the FCC’s Part 32 expressly for the purpose of evaluating service standards.** In its order, the Commission states that the Commission Rule R746-340-2.D adopts the FCC’s Part 32 expressly for the purpose of evaluating service standards. The only evidence to support this statement is the title of Section R746-340 which is “Service Quality for Telecommunications Corporations” and R746-340-1 which states that “the purpose of these rules is to establish reasonable service standards to the end that adequate and satisfactory service will be rendered to the public.” However, Under R746-100-1, the Commission has determined that “headings are for convenience only, and they shall not be used in construing any meaning.” Utah Admin. Code R746-100-1.D. While certain portions of R746-340 deal with service quality, Subsection 340-2.D has nothing to do with service quality. Rather, a detailed review of the more than 60 pages of 47 CFR Part 32 demonstrate that the Uniform System of Accounts contained therein establish accounting procedures and have nothing to do with the service provided to end users.

In fact, the preface of Part 32 provides:

“The revised Uniform System of Accounts (USOA) is a historical financial accounting system which reports the results of operational and financial events in a manner which enables both management and regulators to assess these results within specified accounting period. The USOA also provides the financial community and others with financial performance results. In order for an accounting system to fulfill these purposes, it must exhibit consistency and stability in financial reporting (including the results published for regulatory purposes). Accordingly, the USOA has been designed to reflect stable, recurring financial data based to the extent regulatory considerations permit upon the consistency of the well-established body of accounting theories and principles commonly referred to as generally accepted accounting principles.”

The Commission should modify the Order to reflect that the Commission adopted the Uniform System of Accounts contained in 47 CFR Part 32 “to record the results of Utah intrastate operations.” Part 32 has nothing to do with service quality standards and inclusion of this language in the Order is confusing. Furthermore, if the Commission relied on this errant view to conclude that it did not adopt FCC’s Part 32 to record the results of Utah intrastate operations, Carbon requests that the Commission review its decision and clarify the purpose of R746-340-2.D.

4. **Group Assets with Different Service Lives.** In its Order, the Commission cites Subpart 32.2000(g)(1)(i) of the FCC’s Part 32 which provides:

(g) Depreciation accounting—(1) Computation of depreciation rates. (i) Unless otherwise provided by the Commission, either through prior approval or upon prescription by the Commission, depreciation percentage rates shall be computed in conformity with a group plan of depreciation and shall be such that the loss in service value of the property, except for losses excluded under the definition of depreciation, may be distributed under the straight-line method during the service life of the property.

Referring to this “rule” (47 CFR 32.2000(g)(1)(i)), the Commission states “*the FCC rule does not allow a regulated utility to place assets with differing service values into the same asset group so as to fully depreciate newer assets at an accelerated rate. The FCC rule also prohibits an asset group from including fully depreciated assets, as the expenses associated with such an asset do not fall under the definition of depreciation.*”⁶ While the citation referring to 47 CFR 32.2000(g)(1)(i) is accurate, the Commission’s interpretation of that rule contained in the statements identified above are in error. The group method of depreciation described by the Commission where assets of the same vintage (service life) are placed into a group is a “vintage”

⁶ Order, p. 5.

method of depreciation with the depreciation rate applied to that group. In a vintage method, the average service life of the group equals the service life of each asset in the group because the assets in the group are placed into service in the same year. While the Commission is correct that the vintage method is a form of group depreciation, it is not the method of group depreciation prescribed by the FCC for Carbon.

On the contrary, the FCC permits telecommunications corporations to group assets by year of acquisition (vintage), by type (all drill presses), by classification (all machinery), by location, or by a combination of these ways. Depreciation based on groups that include items with varying lives is known as group/composite depreciation and is explicitly defined by the FCC as its group method in 32.9000.⁷ (For a properly weighted average service life to have any meaning there needs to be assets with varying service lives in the group—otherwise all assets have the same service life and there is no need to average nor weight properly the service life of the group. The “vintage” approach renders the terms “properly weighted” and “average service life” a nullity which signals an incorrect interpretation of the rule.) Assets are aggregated and depreciated by applying a depreciation rate based on the average expected useful life of the group of assets. This does not mean that the average service life of the group is exactly equal to the service life of each asset in the group. Rather, when group methods are applied, periodic studies should be undertaken to ensure that the average life being used is appropriate for the group of assets. As the Commission reviews Carbon’s asset groups, if it finds that the average service life being used is not appropriate for the group of assets, it can adjust the average

⁷ Contrary to the Commission’s reading of 32.9000, see *infra*, the principal clause of this rule explains the FCC’s group method.

remaining life for the group.⁸ Such adjustments are clearly within the scope of the Commission's review of Carbon's application and it is undisputed that such a review may be undertaken by the Division. Whether the Division appropriately examined the average service life of Carbon's groups and adjusted said service lives accordingly is a material fact that will be the subject of the hearing. This is not part of the Carbon Petition for summary judgment that focused solely on the use of a group asset method.

The Commission's Order as quoted above seems to imply that the only group method of depreciation that would be appropriate is a vintage method whereby all of the assets in the group have the exact same service life. While the Commission is free to adopt this method of group depreciation through a rulemaking, the FCC Rule 47 CFR 32.2000 does not require vintage depreciation.

Further, in its Order, on page 5, Footnote 5, the Commission states that Part 32.9000 *"does not allow a utility to mingle older assets and newer assets so as to artificially shorten the service life of the newer assets. Nor does it allow a utility to continue to claim depreciation expense as to a fully depreciated asset."* This is not, however, what Part 32.9000 states. Rather, 47 CFR 32.9000 provides (Emphasis Supplied):

Group plan, as applied to depreciation accounting, means **the plan under which depreciation charges are accrued upon the basis of the original cost of all property including in each depreciable plant account, using the average service life thereof properly weighted**, and upon the retirement of any depreciable property its cost is charged to the depreciation reserve whether or not the particular item has attained the average life.

⁸This adjustment would approximate the FCC Method that Joseph Hellewell testified to on lines 223-234 of his direct testimony.

In this rule, the key concept is that the group plan uses an “average service life” that is “properly weighted.” As discussed above, the FCC does not require all assets in the group to have the same age. This reading would ignore the plain language of the rule that discusses the “average service life” of the group that is “properly weighted.” If the FCC required all assets in the group to be of the same vintage there would be no need to “properly weight” the average service life of the group. Carbon requests that the Commission review its Order accordingly.

5. **No FCC rule prohibits an asset group from including fully depreciated assets.** In its Order, the Commission states that *“the FCC rule also prohibits an asset group from including fully-depreciated assets, as the expenses associated with such an asset do not fall under the definition of depreciation. FN 4 Part 32 refers to such expenses as “losses,” clearly distinguishing them from depreciation expenses.”* Carbon requests that the Commission clarify where this “rule” is found in Part 32. As indicated above either a group is fully depreciated or not fully depreciated--there are no individual assets to consider or exclude. Carbon has reviewed Part 32. Neither the sentence in the Order referring to prohibition of fully-depreciated assets, nor the associated footnote, seem to be supported by FCC rule. Carbon is not aware of any such expense associated with fully-depreciated assets (group or otherwise) which could be recorded or which would require the exclusion of portions of a group asset, nor has it recorded any such expense. A complete search of 47 CFR Part 32 shows 41 occurrences of the words “loss” or “losses.” Most of such references have nothing to do with plant accounting (e.g. extraordinary losses, investment losses) and have no relevance to Carbon’s motion and the resulting Commission Order. On the contrary, Part 32 does not prohibit an asset group from including fully depreciated assets. Fully depreciated assets remain in the plant account until the asset has

been disposed of, and the depreciation expense account fully accounts for the “fully depreciated” nature of the asset. In other words, as discussed above, a fully depreciated asset that is still in service remains in the plant account, but it has no effect on the rate base because it has been fully depreciated and has a net book value of zero. In the case of groups that are not fully depreciated, Part 32 does not preclude older group components being mixed with newer group additions. The Commission’s Order seems to state that a fully depreciated asset should be removed from a plant account because it is fully depreciated. However, basic accounting procedures and Part 32 provide that an asset is removed from a plant account when it is actually disposed of, not when it is fully depreciated. Carbon, therefore believes that the Commission should clarify and/or correct its statements in the Order regarding when assets should be removed from plant accounts to properly reflect generally accepted accounting procedures and the requirements of Part 32.

6. **Abandonment of Group Method.** Carbon’s Motion for Partial Summary Judgment sought only a finding that Part 32, which has been adopted by the Commission for intrastate record keeping, permits a utility to use of the FCC’s version of group depreciation as an acceptable method of depreciation, and that the Division and the Commission cannot require Carbon to utilize a single asset method of depreciation without a modification of R746-340-2.D. R746-340-2.D provides that the Uniform System of Accounts, as prescribed by the FCC at 47 CFR Part 32, is the prescribed system of accounts to record the results of Utah intrastate operations. Carbon argues that Part 32.2000(g)(1)(i) requires companies to use a group plan of accounting for depreciation unless another method of depreciation is prescribed by or approved by the FCC. The Commission acknowledges in footnote 3 of the Order that “*there is no*

evidence in the record to demonstrate that the FCC has approved or required Carbon to use a method other than group depreciation in relation to its intrastate operations.” Further, the Commission states that *“it is undisputed that a utility is permitted to use a group depreciation system in a UUSF calculation, provided the utility does so correctly.”*⁹ Carbon believes that this means that the Commission, pursuant to its rule adopting Part 32, cannot require a separate alternative method for depreciation without express FCC approval or prescription under Part 32, unless and until the Commission changes R746-340-2.D by way of rulemaking. This does not mean that the Commission is required as a matter of law to accept and credit Carbon’s asset groups without question or evaluation. On the contrary, under Part 32, the Commission can question and evaluate Carbon’s asset groups or its calculations of depreciation, and as indicated above, if the Commission finds credible evidence that Carbon has not used the FCC’s group depreciation method correctly, it is free to make corrections or adjustments to Carbon’s group depreciation calculation including, but not limited to, corrections or adjustments to the average remaining life of the group or elimination of assets that are no longer in service from a group account

However, in its Order, the Commission states that *“should the FCC consider that an asset group has been improperly configured, Part 32 is structured to allow the FCC to issue an order requiring a regulated utility to calculate depreciation using a method other than group depreciation; for example straight-line depreciation”*¹⁰ First, as previously indicated, Carbon’s group plan of depreciation uses a straight-line method of depreciation as applied to the group.

⁹ Order, p. 4.

¹⁰ Order, p.5.

Therefore, if the Commission, in fact meant “single asset straight-line” it should clarify this in the Order.

Second, because utilities are permitted, in fact required,¹¹ to use a group plan of depreciation under Part 32, the Commission should, as indicated in the Commission’s Order, review and evaluate whether such asset group has been properly configured and if not, make appropriate adjustments to the asset group and/or the composite percentage rate. The Commission should not throw out the group method in favor of a single asset method of depreciation--particularly where the company has been using a group method for years and the switch to single asset is made in the middle of a UUSF application and on a retroactive basis. The transition to a single asset method of depreciation on a retroactive basis results in an abnormal test year. Rather, although it is somewhat outside the scope of this motion, the method for making adjustments to a group plan of depreciation is identified in the Direct Testimony of Joseph Hellewell as the FCC Method. “The FCC has developed a formula that has been used to recalculate the depreciation rate based on the plants average remaining life, future net salvage, and depreciation reserve ratio. . . The depreciation rate is calculated using the following formula:

$$\text{Depreciation Rate} = \frac{100\% - \text{Accumulated Depreciation}\% - \text{Future Net Salvage}\%}{\text{Average Remaining Life}}^{12}$$

Additionally, 47 CFR Part 32.2000(g)(1) provides:

(ii) In the event any composite percentage rate becomes no longer applicable, revised composite percentage rates shall be computed in accordance with paragraph (g)(1)(i) of this section.”

¹¹ 47 CFR 32.2000(g)(1)(i) states “unless otherwise provided by the Commission [FCC], either through prior approval or upon prescription by the Commission, depreciation percentage rates shall be computed in conformity with a group plan of accounting for depreciation.”

¹² Direct Testimony of Joseph Hellewell, lines 223-234.

If the FCC finds that the depreciation rate applied to a group account does not accurately reflect the average remaining life of the group, it does not abandon the group method. Rather, it makes the necessary adjustments to ensure that the group account is properly configured and the average remaining life of the group is properly reflected. For purposes of Carbon's Motion, the question put to the Commission is whether a group plan of depreciation is an acceptable method under 47 CFR Part 32, as adopted by the Commission in R746-340-2.D. The Commission has determined that it is. The Commission should clarify that the issue to be decided at hearing is whether Carbon has used group depreciation correctly, and if not, what adjustments need to be made to Carbon's group depreciation calculation.

If, on the other hand, the Commission is stating that when R746-340-2.D is applied in a Utah Universal Service Fund ("UUSF") case, the Commission can abandon a group plan of depreciation and require a company, such as Carbon, to use a method other than a group method for depreciation, the Commission must clarify whether a Company would be required to use such alternative method (*i.e.*, single asset) for its depreciation calculation for interstate operations and intrastate operations.

Carbon submits that it is critical that companies be entitled to apply the same method of depreciation for both interstate and intrastate operations. First, requiring companies to have two separate depreciation methods for interstate and intrastate operations would be administratively burdensome. As this Commission is aware, the regulated telephone companies are required to do jurisdictional separations under 47 CFR Part 36 so that assets are properly allocated to the interstate jurisdiction or the intrastate jurisdiction. These separations are done on an annual basis and change to a certain extent from year to year. For example, in 2014 the interstate/intrastate

separations might be 46%/54% respectively, and the following year that percentage could change to 52%/48%. If a company is required, on the federal interstate side, to use a group plan of depreciation, but is required by Utah to use a single asset plan of depreciation for intrastate assets, the ongoing depreciation calculation becomes burdensome, opaque, and difficult to administer. For example, if an asset's (asset group) jurisdictional separation changes from year to year, how will the depreciation be calculated using group method and single asset? How will that calculation be accurate as the jurisdictional nature (and thus method/rate of depreciation changes each year). Assets will be flip-flopping between jurisdictions and between depreciation methods, making reporting and tracking difficult. Additionally, the current Public Service Commission Annual Report in its current form would not accurately reflect the depreciation going forward.

Second, if Commission is stating that it can set the method of depreciation for both interstate and intrastate operations, Carbon encourages the Commission to think through what may be the unintended consequences of such a decision. As the Commission is aware, several rate of return regulated telecommunications companies in the State of Utah utilize a group plan of depreciation under Part 32. This can result in accelerated depreciation of assets (but not over depreciation). If a company utilizing group depreciation is a recipient of high cost federal support, and is now required to move to a single asset method of depreciation for total company operations, this could have a significant impact on such company's federal universal service support. This loss of federal support could have a significant impact on the Utah Universal Service Fund.

As a result of the administrative burden associated with maintaining two separate methods of depreciation, and the potential impact associated with requiring companies to change from a group plan for interstate operations, Carbon submits that the more prudent course of action for the Commission is to permit companies to use the depreciation method prescribed by the FCC for interstate operations (group in this case) for their intrastate operations. This approach is consistent with R746-340-2.D; is administratively transparent; is not burdensome; and still permits the Commission to review each company's group plan and make adjustments as needed. Carbon hereby requests that the Commission review and clarify this portion of its Order accordingly.

CONCLUSION

Carbon respectfully requests review and clarification on the issues identified herein. Carbon further submits that these matters should be resolved prior to the hearing on this matter for the reasons set forth in Carbon's Motion to Vacate Hearing filed contemporaneously herewith.

Dated this 27th day of October, 2015.

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CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the Carbon/Emery Telcom, Inc.'s Petition for Review and, 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 27th day of October, 2015:

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