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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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| Investigation of Revenue Requirement Impacts of the New Federal Tax Legislation Titled: “An act to provide for reconciliation pursuant to Titles II and V of the concurrent resolution of the budget for fiscal year 2018” | DOCKET NO. 17-2302-02 COMMENTS OF CARBON/EMERY TELCOM, INC. |
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On December 21, 2017, the Utah Public Service Commission (the “Commission”) issued a Notice of Comment Period (“Notice”) to investigate the revenue requirement impacts of the new federal tax legislation (“Tax Reform Act”). The Commission requested that all regulated utilities in Utah file Comments describing in detail, to the extent practical, the impacts of Tax Reform Act on their respective revenue requirement in the corresponding docket on or before Wednesday, January 31, 2018. The Notice listed a separate docket number for each regulated utility. However, when the Notice was served on Carbon/Emery Telcom, Inc. (“Carbon/Emery”), the email sent by the Commission listed the docket numbers of Rocky Mountain Power (17-035-69) and Dominion Energy Utah (17-057-26) first. As a result, Carbon/Emery inadvertently missed the Notice and did not file Comments on or before January 31, 2018. On February 2, 2018, Carbon/Emery, along with every other regulated telephone company, received an Order to Show Cause (“Order to Show Cause”) for its failure to file the requisite Comments. Carbon/Emery hereby files these Comments in response to the Notice and the Order to Show Cause. As a result of Carbon/Emery’s filing of these Comments on or before February 27, 2018, and for the reasons stated herein, Carbon/Emery’s UUSF support should not be suspended or modified at this time.

COMMENTS OF CARBON/EMERY

I. Tax Reform Act

The Tax Reform Act was signed into law on or about December 22, 2017. Most notably, the Tax Reform Act, among other things, reduces the corporate federal income taxes from a maximum of 35% to 21%. The reduction in corporate income tax will also result in a reduction to the accumulated deferred income tax (“ADIT”) liability that is carried on Carbon/Emery’s balance sheet. The ADIT liability represents the difference in tax expense recognized in prior years (based on a tax rate of 34% for Carbon/Emery) which will be paid in future years (at the lower tax rate). Because the ADIT liability for Carbon/Emery was established based on the 34% tax rate, by reducing the corporate tax rate to 21% the ADIT liability will be overstated and will need to be adjusted. A reduction in the ADIT generally results in an increase in rate base.

II. Revenue Requirement Impacts

As the Commission is aware, public utilities ratemaking requires that all income and expenses be evaluated to determine a company’s revenue requirement. Typically, only after the revenue requirement has been determined will rates be adjusted. Changes in expenses, such as a reduction (or increase) in the federal income taxes, would need to be evaluated against a company’s revenue requirement and associated authorized rate of return. While rate of return incumbent local exchange carriers, such as Carbon/Emery, are regulated public utilities like electricity, gas, and water, the regulated telecommunications industry in Utah is different from other public utilities.

First, the rates for basic service are set by the Commission at \$18/per customer per month as a result of the Federal Communications Commission’s (“FCC”) USF/ICC Transformation Order dated November 18, 2011 (“Transformation Order”). The Transformation Order required Carbon/Emery to set its rates at a federally determined benchmark or lose federal high-cost-loop support funding on a dollar

for dollar basis by the amount the local rates fell short of the federal benchmark. As a result, this Commission has set the local rates for basic service to mirror the federal benchmark. Therefore, rates for telecommunication service were not set based on a federal tax gross up, and should not be reduced based on the reduction in federal tax rate. It would be imprudent for the Commission to reduce rates below the federal benchmark.

Second, rate of return regulated carriers of last resort in Utah, unlike other types of utilities in Utah, are eligible for support from the Universal Public Telecommunications Service Support Fund (“UUSF”). As the Commission is aware, the UUSF is available to rate-of-return carriers of last resort whose costs to provide public telecommunications service and wholesale broadband Internet access service exceed the carrier’s revenues. As a result, any discussion of the impacts of the Tax Reform Act on rate of return regulated carriers of last resort in Utah will focus on the carrier’s receipt of support from the UUSF, not on the rates charged to customers.

As the Commission is aware, the UUSF statute was overhauled during the 2017 Legislative Session, resulting in substantial changes to Utah Code Section 54-8b-15. Among the changes to Utah Code Section 54-8b-15 are:

1. The rate of return in Utah is required to mirror the FCC prescribed weighted average cost of capital for rate of return regulated carriers. This rate of return is currently set at 10.75%, with a step down to 10.5% effective July 1, 2018.¹
2. The rate of return carriers of last resort are permitted to use any FCC approved method of depreciation.²

These statutory modifications could have an impact on Carbon/Emery’s revenue requirement and UUSF disbursement. As a result, it would be imprudent to consider the impacts of the Tax Reform Act,

¹ Utah Administrative Rule R746-8-401(3)(a).

² Utah Code Section 54-8b-15(5)(b); UAR R746-8-401(3)(b).

without also considering the impacts of the UUSF statutory changes, and the administrative rule changes on Carbon/Emery's revenue requirement/UUSF disbursement. Utah Administrative Rule R746-8 was made effective February 21, 2018, so some issues, such as rate of return, have been resolved. However, other issues, such as depreciation expense, remain subject to further rulemaking, and may impact Carbon/Emery's revenue requirement. Additionally, the Tax Reform Act is effective January 1, 2018. Therefore, any impact should be applied against 2018 operations.

Carbon/Emery agrees that the impact of these issues on Carbon/Emery's revenue requirement and UUSF disbursement should be considered, but Carbon/Emery believes that the Commission should consider all of the relevant potential impacts to revenue requirement including, but not limited to:

- The reduction in the corporate tax rate;
- The impact of the reduction in ADIT and the corresponding increase in rate base;
- The new state rate-of-return;
- The depreciation expense rules.

It would be premature and imprudent to calculate the revenue requirement impacts based solely on the Tax Reform Act at this time. Additionally, Carbon/Emery's UUSF disbursement was set by Commission Order and included a Commission established rate base, rate of return, and tax gross up of 34%.

However, since the time of the Commission Order, all three of those factors have changed. Therefore, it would be inequitable to merely reduce the UUSF disbursement by the percentage change in the mixed tax rate as a result of the reduction in federal corporate tax rate. Rather, the Commission should undertake a process to examine all of the issues affecting Carbon/Emery as a rate of return regulated carrier of last resort. Fortunately, R746-8-401(4), recently implemented by the Commission provides a procedure for consideration of these issues. R746-8-401(4) provides that:

(4) Yearly following a change in the FCC rate-of-return, unless the provider files with the Commission a petition for review of its UUSF disbursement, the Division shall make a recommendation of whether each provider's monthly distribution should be adjusted according to:

- (a) the current FCC rate-of-return as set forth in R746-8-401(3)(a); and
- (b) the provider's financial information from its last Annual Report filed with the Commission.³

While this process may be subject to further clarification by rule, the framework contained in R746-8-401(4) can be utilized by the Division and the company to evaluate the effects of the state statutory and administrative rule changes on Carbon/Emery's revenue requirement once Carbon/Emery has filed its 2017 Annual Report with the Commission and received its 2017 audited financial statements; and once the Commission has finalized the administrative rules related to Utah Code 54-8b-15. The impacts of the federal Tax Reform Act will apply to 2018 operations and cannot be fully determined at this time.

Carbon/Emery has examined its preliminary 2017 year end trial balances in conjunction with the preparation of these Comments. This preliminary examination considered the newly established state rate of return; the reasonableness of its current depreciation methodology; increases to rate base from a combination of capital additions with projected reductions in ADIT and actual reductions in post-retirement obligations; and the effect of a revised tax gross up using a 21% Federal tax rate. This preliminary examination evidences the need for additional UUSF for Carbon/Emery pending final audited financial statements and proposed rulemaking.

CONCLUSION

Carbon/Emery appreciates the opportunity to provide these Comments and believes that evaluation of Carbon/Emery's revenue requirement should be made taking into consideration all of the relevant changes: the changes associated with the Tax Reform Act, the changes to Utah Code 54-8b-15, and the newly enacted and proposed administrative rule changes. To consider any one of these impacts in a vacuum would be inappropriate. Because the administrative rule changes are not yet complete, and because Carbon/Emery has not yet filed its 2017 annual report, or received its 2017 audited financial statements, the evaluation of these impacts cannot be determined at this time. Carbon/Emery requests that

³ UAR R746-8-401(4).

these issues be reviewed after the finalization of the administrative rulemaking and the filing of 2017 annual report. For these reason, Carbon/Emery's UUSF support should not be suspended or modified at this time.

DATED this 26th day of February, 2018.

BLACKBURN & STOLL, LC



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CERTIFICATE OF SERVICE

I hereby certify that on the 26th day of February, 2018, I served a true and correct copy of Carbon/Emery Telcom, Inc.'s Comments on Investigation of Revenue Requirement Impacts of the New Federal Tax Legislation Titled: "An act to provide for reconciliation pursuant to Titles II and V of the concurrent resolution of the budget for fiscal year 2018," Docket No. 17-2302-02 via e-mail transmission to following persons at the e-mail addresses listed below:

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