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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

2019 Utah Universal Service Fund Preliminary Recommendation for Central Utah Telephone, Inc.	DOCKET NO. 18-040-01
2019 Utah Universal Service Fund Recommendation for Citizens Telecommunications Company of Utah dba Frontier Communications of Utah	DOCKET NO. 18-041-02
2019 Utah Universal Service Fund Recommendation for Emery Telephone	DOCKET NO. 18-042-01
2019 Utah Universal Service Fund Preliminary Recommendation for Gunnison Telephone Company	DOCKET NO. 18-043-01
2019 Utah Universal Service Fund Recommendation for Manti Telephone Company	DOCKET NO. 18-046-01
2019 Utah Universal Service Fund Recommendation for Navajo Communications Company, Inc. dba Frontier Navajo Communications Company	DOCKET NO. 18-050-02
2019 Utah Universal Service Fund Preliminary Recommendation for Beehive Telephone Company, Inc.	DOCKET NO. 18-051-01
2019 Utah Universal Service Fund Recommendation for South Central Utah Telephone Association, Inc.	DOCKET NO. 18-052-01
2019 Utah Universal Service Fund Recommendation for UBTA-UBET Communications, Inc. dba Strata Networks	DOCKET NO. 18-053-02

2019 Utah Universal Service Fund Recommendation for Union Telephone Company, Inc.	DOCKET NO. 18-054-01
2019 Utah Universal Service Fund Preliminary Recommendation for Skyline Telecom	DOCKET NO. 18-576-01
2019 Utah Universal Service Fund Recommendation for All West Communications, Inc.	DOCKET NO. 18-2180-01
2019 Utah Universal Service Fund Preliminary Recommendation for Bear Lake Communications, Inc.	DOCKET NO. 18-2201-01
2019 Utah Universal Service Fund Recommendation for Carbon/Emery Telcom, Inc.	DOCKET NO. 18-2302-02
2019 Utah Universal Service Fund Recommendation for Hanksville Telcom, Inc.	DOCKET NO. 18-2303-01
2019 Utah Universal Service Fund Preliminary Recommendation for Direct Communications Cedar Valley, LLC	DOCKET NO. 18-2419-01
	INITIAL COMMENTS OF THE UTAH DIVISION OF PUBLIC UTILITIES

Pursuant to Utah Code Ann. §54-4a-1 and Utah Admin. Code r.746-1, the Division of Public Utilities (“Division”) submits these Initial Comments. The Division recommends that the Public Service Commission of Utah (“Commission”) continue the Utah Public Telecommunications Service Support Fund (“UUSF”) on a prospective basis, continue to apply the tax interest synchronization adjustment, and seek Commission guidance on the treatment of EDIT where it cannot be offset against UUSF payments.

INTRODUCTION

Pursuant to Utah Admin Code r.746-8-401 the Division filed preliminary recommendations regarding UUSF adjustments in the above captioned 16 dockets on October 4, 2018. On October 5, 2018 the Division filed related Comments in Docket No. 18-999-09 addressing the cumulative impacts on the UUSF of those recommendations. The Comments filed in Docket No. 18-999-09 also raised a number of concerns that had come to the attention of the Division during its preparation of the preliminary recommendations and recommended that they be resolved on a broad basis.

On October 11, 2018 the Commission held a scheduling conference in the above captioned dockets. The Commission set the date of October 30, 2018 for Responses to the Division of Public Utilities' Recommendations. The scheduling agreement of the parties contemplated that the Division would also file some initial comments regarding the issues that it identified in Docket No 18-999-09. While not directly responsive to the Scheduling Order in this docket the Division is filing these brief initial comments to help parties understand the Division's position on the issues.

DISCUSSION

On October 4, 2018 the Division filed a preliminary recommendation regarding UUSF payment adjustments in 16 dockets. Those preliminary recommendations are based on the Division's application of Utah Code Ann. §54-8b-15 and Utah Admin Code r.746-8. In the process of developing these recommendations the Division has been in frequent contact with many of the utilities that are affected by the recommendations. The Division is uncertain as to

which parties will file Responses and what issues will be addressed and the Division may reply in more depth as necessary in the next round.

Three primary issues identified by the Division that will require some guidance from the Commission and will be addressed in these comments.¹ The first issue is whether the UUSF is a prospective subsidy that is intended to provide the utility the opportunity to earn its rate of return if it operates efficiently or in the alternative whether the UUSF has been changed to a balancing mechanism that trues up past operations. The Division does not find support in the language of the statute to convert the UUSF from a prospective to retroactive. The second issue is the treatment of income taxes when using a hypothetical capital structure. The Division has followed past Commission practice by applying an interest synchronization adjustment to the calculation of the preliminary recommendations where applicable. The third issue is how to treat excess deferred income tax (“EDIT”) when a company is not entitled to UUSF funds. The Division is uncertain how to properly treat the repayment.

I. Under Utah Law Utah Universal Public Telecommunications Service Support Fund Subsidy Payments are Prospective

Unless otherwise specified by statute UUSF funds should be provided on a prospective basis. The Division is aware that some of the companies that have received the preliminary recommendations disagree with the Division continuing to apply the UUSF on a forward-looking basis. The Division understands the position of those companies to be that the UUSF is now a

¹ The Division would not normally participate in the first round of briefing or comments following the Division’s own initial recommendations. The Division is in the position at this stage of addressing concerns that have been expressed by some, but not all, of the utilities that are subject to the UUSF recommendations made by the Division. Each of the decisions that will need to be made by the Commission in this docket are likely to benefit some portion of the rural ILECs who receive UUSF while reducing the UUSF funds to others. The Division position on the issues addressed is not necessarily supported or opposed by each company.

backward-looking mechanism where the Companies' actual eligible costs and expenses during a prior period are recovered through the UUSF. The Division understands the argument in favor of this interpretation relies on the language of Utah Code § 54-8b-15(5)(a) that states in relevant part "is entitled to a rate of return equal to ..." The emphasis being on the entitlement. In order to ensure that the companies receive the entire subsidy they are entitled to, it must be a retroactive mechanism.

The language in the current law does not support that conclusion. Unless the Legislature explicitly reverses the prospective nature of the UUSF, the Division recommends that the UUSF remain prospective in nature. Utah law has long followed the standard method of utility regulation where revenue recovery, whether through rates or other revenue sources, is prospective in nature.²

The Division is directed by §54-4a-6(1) to "promote the ... efficient ... operation of all public utilities." The prospective nature of ratemaking or rate recovery serves a critical public interest by providing incentives for utilities to operate efficiently. "The prohibition against retroactive rate making is designed to provide utilities with an incentive to operate efficiently."³ Prospective regulation with periodic resets serves to drive efficiency through the iterative process that benefits utilities in the short run and rate payers in the long run. This is widely recognized throughout the United States.⁴

² *MCI Telecommunications Corp. v. Public Service Com'n of Utah*, 840 P.2d 765, 770 (Utah 1992) ("As a general proposition, a utility's recoupment of costs that were greater than projected or revenues that were less than projected from future rates constitutes retroactive rate making").

³ *Id.*

⁴ See Ex.73B C.J.S. Public Utilities § 141 ("Unless otherwise provided by statute, rates prescribed by a public utility regulatory commission are prospective, and cannot ordinarily be

As explained in *Div. of Public Utilities v. Public Service Com'n*,

In determining an appropriate rate, the PSC considers the utility's historical income and cost data, as well as predictions of future costs and revenues, and arrives at a rate which is projected as being adequate to cover costs and give the utility's shareholders a fair return on equity. To provide utilities with some incentive to operate efficiently, they are generally not permitted to adjust their rates retroactively to compensate for unanticipated costs or unrealized revenues. See U.C.A., 1953, § 54-4-4 (Repl.Vol. 6A, 1974, Supp.1985); see also *Southern California Edison Co. v. Public Utilities Commission*, 20 Cal.3d 813, 144 Cal.Rptr. 905, 905-06, 576 P.2d 945, 945-46 (1978). This process places both the utility and the consumers at risk that the rate-making procedures have not accurately predicted costs and revenues. If the utility underestimates its costs or overestimates revenues, the utility makes less money. By the same token, if a utility's revenues exceed expectations or if costs are below predictions, the utility keeps the excess.⁵

The UUSF has historically been a prospective program where payments are set based on the projected operations during the effective period. If the utility operates efficiently it has the opportunity to earn its authorized rate of return. 2017 Senate Bill 130 ("SB 130") did not reverse the long-standing principle that utility rate making and revenue subsidy programs are prospective. For example, §54-8b-15(2)(b) states in relevant part that "the fund shall provide a mechanism for a qualifying carrier of last resort to obtain specific, predictable, and sufficient funds..." The language describing the funds as specific, predictable, and sufficient all suggest prospective application.

If the language intended such funds to be retroactive in nature, there would be no reason to require any of those elements. The funds would simply be calculated retroactively and paid

made to operate retroactively, whether it favors the utility or the ratepayers." Internal citations omitted).

⁵ *Utah Dept. of Business Regulation, Div. of Public Utilities v. Public Service Com'n of Utah*, 720 P.2d 420, 420 (Utah 1986).

out. As a point of comparison, §54-8b-15(4)(a) describes the carriers of last resort as “eligible for payment from the [UUSF] if...” whereas it addresses retroactive payments for one-time projects as a “reimbursement of reasonable costs.” The UUSF payments to carriers of last resort have not previously been a reimbursements of reasonable costs, but rather additional revenue from the UUSF to meet projected revenue requirement shortfalls.

In addition to the statutory history and public policy reasons for retaining the forward-looking operation of the UUSF, there are other practical considerations. Prior UUSF funds have always been forward-looking. Meaning that the monthly UUSF payments each company has been receiving subsidized the service during the then current period. As a result, each company will have received the full amount that it is entitled to through the end of 2018 as of the final 2018 payment. Under prior precedent, those payments would not be subject to true-up whether up or down outside of an extraordinary and unforeseen event. In short, the 2018 revenue shortfall was provided to UUSF recipients during 2018.

This leaves an open question as to how to handle 2019. Hypothetically, 2019 would be the first effective period under the new method. While not an exhaustive set of concerns, the following are some that will need to be addressed regarding the transition. Assuming 2017 and 2018 payments were prospective, should companies receive payments from the UUSF during the 2019 to pay for costs incurred during the 2017 or 2018 year again? If payments are continued through 2019 based on 2017 historical year operations and they are not intended to for projected costs of the 2019 operations; should the amount be set to address the true-up for 2017 plus projections for 2019 that would then be trued up at a later date? For the portion that is a true-up for a past period; how long should the true up period last? How would overearning be addressed

in the event that it exceeds the amount that can be offset against UUSF? Would a refund be due to the UUSF or would rates be reduced through a rate decrease or credit to customers?

Procedurally, the Division would anticipate that a retroactive UUSF would require a process much like other balancing accounts. Current Rule 746-8 does not support such a process. The recently promulgated Rule 746-8 language is prospective. If the Commission does determine that the UUSF is transitioning from a prospective process to a retroactive one, the Division's preliminary recommendations will need to be significantly revised based on guidance from the Commission.

II. Tax Interest Synchronization is Consistent with Commission Precedent

Tax interest synchronization has historically been part of Utah's ratemaking for utilities. In a recent UUSF case the Commission explained why interest synchronization is a type of prudence adjustment that applies to UUSF calculation.

A public utility must operate in an efficient, low-cost manner. We found in our Order that funding 100% of operations through equity is both inefficient and costly. In imputing debt to Carbon/Emery, we imputed the prudence that a public utility is required to exercise, and we attributed to Carbon/Emery all calculable effects of that prudence. We do not see an error of law in that attribution.⁶

Some companies have suggested to the Division that because SB130 fixes the rate of return calculation at the same rate used by the FCC, such an adjustment will effectively lower the realized rate of return. Such a conclusion would exclude prudence review by the Commission. The Division finds little in Utah law supporting for this assertion. Section 54-8b-11 directs the Commission to "to make available high-quality, universal telecommunications services at just

⁶ May 19, 2016 Order on Petition for Review, Rehearing, or Reconsideration of the Commission's March 31, 2016 Order at p. 17, *In the Matter of the Application of Carbon/Emery Telcom, Inc. for an Increase in Utah Universal Service Fund Support*, Docket No. 15-2302-01.

and reasonable rates for all classes of customers throughout this state.” Similarly, eligibility for receipt of UUSF funds under Section 54-8b-15(5) refers to “reasonable costs, as determined by the commission.” In order to carry out the legislative guidance it is necessary for the Commission to make adjustments if companies are not acting in the least cost manner. Tax interest synchronization is a type of prudence adjustment that ensures customers are paying just and reasonable rates based on reasonable costs.

III. Excess Deferred Income Tax (EDIT)

The change in tax law has required companies to calculate EDIT. EDIT money should be refunded to the UUSF for past over-payments that were made based on a higher tax rate that no longer applies. There are instances where EDIT repayments calculated by the Division will exceed the UUSF the company may otherwise be entitled to. Therefore, the Division cannot deduct the amount from UUSF payments. This is a similar problem to an overearning scenario if the UUSF is considered a retroactive mechanism. The alternative is to refund the payment through a reduction in rates during the effective period. However, this option may reduce rates below the affordable base rate and may have other impacts on federal programs. The Division is uncertain regarding the treatment of the repayment.

CONCLUSION

The UUSF funds are prospective in nature. SB 130 did not convert the UUSF from a prospective fund into a retroactive one. Utah law and public policy considerations support the continuation as a prospective fund where the utilities are funded for current costs during the current period. The Commission retains authority under SB 130 to make prudence adjustments and tax interest synchronization is an applied prudence adjustment. The Commission should

continue to apply tax interest synchronization. Finally, the Division seeks guidance on the treatment of EDIT when it cannot be deducted from UUSF payments.

Submitted this 30th day of October 2018.

/s/ Justin C. Jetter

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing comments filed by the Utah Division of Public Utilities was emailed on 30 October 2018 to the following in Utah Dockets 18-040-01, 18-041-02, 18-042-01, 18-043-01, 18-046-01, 18-050-02, 18-051-01, 18-052-01, 18-053-02, 18-054-01, 18-576-01, 18-2180-01, 18-2201-01, 18-2302-02, 18-2303-01, and 18-2419-01.

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