State of Utah
Department of Commerce
Division of Public Utilities

FRANCINE GIANI
Executive Director

CHRIS PARKER
Director, Division of Public Utilities

GARY HERBERT
Governor

SPENCER J. COX
Lieutenant Governor

Recommendation

To: Utah Public Service Commission

From: Utah Division of Public Utilities

Chris Parker, Director

Artie Powell, Manager
Shauna Benvegnu-Springer, Utility Technical Consultant
Gary Smith, Utility Analyst

Date: October 1, 2019

Re: **2020 UUSF Recommendation - Direct Communications Cedar Valley, Docket No. 19-2419-01**

Recommendation (Approve)

The Division of Public Utilities (Division) recommends that the Public Service Commission of Utah (PSC) adjust the annual Utah Universal Service Fund (UUSF) payable to Direct Communications Cedar Valley (Direct CCV) to $3,287,222. Direct CCV's current annual UUSF distribution is $1,853,611 (This 2019 annual distribution amount includes a reduction for the normalization, and repayment of EDIT).

The Division also recommends the PSC order the Company to refund $93,120 from Direct CCV's 2020 UUSF to comply with the 2017 IRS tax law change and its normalization of Excess Deferred Income Tax (EDIT). This refund would reduce Direct CCV's proposed 2020 UUSF amount to $3,194,102, or $266,175 monthly.

Issue

The Division of Public Utilities (Division) has reviewed the annual report of Direct CCV submitted on April 15, 2019. Pursuant to PSC rule R746-8-401(a) and (b), the Division has calculated the annual UUSF eligibility based on this annual report, and the Division's adjustments deemed prudent during its review.

Background

PSC rule R746-8-401 requires the Division to recommend to the PSC adjustments to the monthly UUSF distribution for each provider based on 1) the FCC rate of return set forth in R746-401-(3)(a) and the provider's financial information from its last annual report filed with the Commission. This memo and exhibits present the Division recommendation for adjustment to the UUSF distribution of Direct CCV.

Discussion

In calculating the UUSF eligibility for Direct CCV, the Division utilized the following:

1) Rate of Return – Because the FCC prescribed rate of return (ROR) changes on July 1, 2020, the Division used an average of the 10.25% ROR that would be applicable from January to June, 2020, and the 10.00% applicable from July to December 2020. The average rate is 10.125%.

2) State and Federal Income Tax – The Division used a federal tax rate of 21% and a Utah tax rate of 4.95% to estimate future income taxes included in the 2020 UUSF calculation.

3) Depreciation – Direct CCV utilizes group depreciation rather than single asset depreciation. Depreciation expense is expected to be affected by current rule changes for companies using group asset depreciation. Changes in depreciation expense would impact the calculated UUSF distribution eligibility.

4) Direct CCV's Federal 2018 USF support decreased approximately $232,979 from 2017.

5) Excluded Costs – Direct CCV's annual report included costs that should be excluded, the Division adjusted for these expenses.

6) Direct CCV has utilized accelerated depreciation and has Accumulated Deferred Income Taxes (ADIT). Due to the decrease in the federal tax rate, Direct CCV has Excess Deferred Income Taxes (EDIT). EDIT is a Deferred Regulatory Liability which should be returned to UUSF. The Tax Act which reduced federal taxes requires that a normalization method of accounting must be used to amortize EDIT over the original life of the underlying assets for public utility property. The primary normalization method provided in the Tax Act is the Average Rate Assumption Method (ARAM). The Tax Act advises that if EDIT is returned sooner than calculated utilizing ARAM, federal penalties would be assessed. Any penalties assessed in association with Direct CCV's treatment of EDIT would be an excluded expense that could not be recaptured through UUSF. The

Division recommends refunding Direct CCV's amortized EDIT amount of $93,120 by reducing Direct CCV's 2020 UUSF.

Conclusion

The Division recommends adjusting the 2020 UUSF distribution for Direct CCV to $3,194,102, or $266,175 monthly. This amount includes a reduction for the normalization of EDIT.

Cc: Kip Wilson, Direct Communications Cedar Valley (kip@directcom.com)
R. Michael Parish, Direct Communications Cedar Valley (michael@directcom.com)
Michele Beck, Director – Office of Consumer Services
Justin Jetter, Assistant Attorney General