

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into the
Review of the California High Cost
Fund-A Program.

Rulemaking 11-11-007

**REPLY BRIEF OF THE PUBLIC ADVOCATES OFFICE
ON THE ASSIGNED COMMISSIONER'S FOURTH AMENDED
SCOPING MEMO AND RULING**

CANDACE CHOE

Attorney for the

Public Advocates Office
California Public Utilities Commission
505 Van Ness Ave.

San Francisco, CA 94102

Telephone: (415) 703-5651

Email: Candace.Choe@cpuc.ca.gov

May 9, 2020

TABLE OF CONTENTS

	<u>Page</u>
TABLE OF AUTHORITIES.....	iii
I. INTRODUCTION.....	1
III. BROADBAND DEPLOYMENT AND SUBSCRIPTION IN INDEPENDENT SMALL LEC TERRITORIES [SCOPING MEMO, ISSUES (1)(A), (1)(E), 1(F), (9); HEARING ISSUES (1), (3), (4), (5)].....	3
A. The Small ILECs Misrepresent the Record Regarding Broadband Deployment and Subscription Data.....	3
B. The Commission Should Continue to Collect and Use Broadband Data Provided to The FCC And the Communications Division.....	4
C. The Commission Should Incent CHCF-A Providers to Increase Broadband Subscribership.....	5
D. The Commission Should Require Small ILECs Or Their ISP Affiliates to Provide an Affordable Broadband Option for Low- Income Customers.....	6
IV. BROADBAND IMPUTATION [SCOPING MEMO, ISSUES (1)(C), (1)(D), HEARING ISSUE (2)].....	7
A. Retail Imputation.....	7
1. The Commission Determined in Phase 1 That It Has the Legal Authority To Impute Broadband Revenues And That Authority Has Not Changed.....	7
2. Imputation of Broadband Revenues Is Equitable.....	9
3. The Small ILECs s Already Produce Consolidated Audited Financial Statements	11
B. Wholesale Imputation	11
1. Wholesale Imputation Is Not Illegal	11
V. RATEMAKING TREATMENT OF EXPENSES.....	12
A. Corporate Expense Cap. [Scoping Memo, Issues (2)(B)(I), (2)(B)(Ii), (2)(B)(IV)].....	12
1. Small ILECs Do Not Raise Any New or Persuasive Arguments for Changing The Corporate Expense Cap	12
2. The Commission May Lawfully Remove the Rebuttable Presumption of Reasonableness	13

VI.	RATE CASE EXPENSES. [SCOPING MEMO, ISSUES (2)(B)(I), (2)(B)(II), (2)(B)(IV)].....	15
	A. Recovery of Rate Case Expenses as Part of The Corporate Operations Expense Account Cap Is Consistent With Commission Precedent	15
	B. Operating Expenses [Scoping Memo, Issue (2)(B)(III)].....	16
	1. It Is Reasonable to Limit the Amount Of Operating Expenses That Can Be Recovered Through CHCF-A Subsidies	16
	2. Applying GDP CPI in Conjunction with The National Exchange Carrier Association (NECA) Inflation Figures Will Align the Operating Expense Cap With A Future Test Year	17
VII.	RATEMAKING TREATMENT OF INVESTMENTS	19
	A. Small ILECs Historical Investments Show That The Public Advocates Office’s Methodology Would Be Reasonable And Efficient.....	19
VIII.	MODIFICATIONS TO THE RATE CASE PROCESS. [SCOPING MEMO, ISSUES (2)(B)(I), (2)(B)(IV), (8)]	19
	A. The Small ILECs Recommended Procedural Changes To GRCS Will Violate Due Process And Exacerbate Inefficiencies.....	19
IX.	BASIC SERVICE RATES AND OTHER END USER RATE PROPOSALS [SCOPING MEMO, ISSUE (4)]	21
	A. The Commission Should Gradually Make Small ILECs’ Rates Comparable to Urban Rates	21
X.	RATEMAKING TREATMENT OF MISCELLANEOUS REVENUES [SCOPING MEMO, ISSUE (5)]	22
XI.	CHCF-A ANNUAL FILING PROCESS [SCOPING MEMO, ISSUE (7)]	22
XII.	CONCLUSION	22

TABLE OF AUTHORITIES

	<u>Pages</u>
<u>Court Cases</u>	
<i>Donorovich-Odonnell v. Harris</i> (2015) 241 Cal.App.4th 1118	8
<i>Mozilla Corporation v. Federal Communications Commission</i> (D.C. Cir. 2019) 940 F.3d 1	9
<i>Smith v. County of Los Angeles</i> (1989) 214 Cal.App.3d 266	8
 <u>California Public Utilities Code</u>	
§275	10
§275.6	passim
§275.6(a)	6
§275.6(b)(3)	passim
§275.6 (c)(2)	8
§275.6(c)(5)	5
§275.6(e)	10
§701	8
§1705	7
 <u>CPUC Decisions</u>	
D.10-10-019	9
D.14-08-006	9
D.14-12-084	7,9,12,15,16
D.15-06-048	21
D.16-12-025	4
D.19-04-017	3,18
D.19-12-011	14,16

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into the
Review of the California High Cost
Fund-A Program.

Rulemaking 11-11-007

**REPLY BRIEF OF THE PUBLIC ADVOCATES OFFICE
ON THE ASSIGNED COMMISSIONER’S FOURTH AMENDED
SCOPING MEMO AND RULING**

I. INTRODUCTION

Pursuant to Rule 13.11 of the California Public Utilities Commission’s (Commission) Rules of Practice and Procedure (Rules) and the direction of the Administrative Law Judges McKenzie and Fortune in evidentiary hearings,¹ the Public Advocates Office at the California Public Utilities Commission (Public Advocates Office) submits this reply brief in response to Commissioner Guzman Aceves’ March 22, 2019 Fourth Amended Scoping Memo and Ruling (Fourth Amended Scoping Memo) and the issues raised in the September 12, 2019 Administrative Law Judges’ Ruling Setting Hearing Dates and Issues for Hearing (September 12 Ruling).

Since its inception, the California High Cost Fund – A (CHCF-A) has collected surcharges from all California ratepayers and then apportioned them to the Small Independent Local Exchange Carriers (ILECs) to support universal service of safe, reliable, high-quality communications services in rural areas of the state. In 2012, the Legislature broadened that universal service goal to include broadband, thus expanding the CHCF-A to fund investment in broadband infrastructure. In exchange, the Legislature agreed to permit the Commission to consider the revenues that would be received from

¹ Ruling of ALJs McKenzie and Fortune granting extension, March 17, 2020; initial deadline set in evidentiary hearings, Reporters Transcript (RT) Vol. 13, 2346:6-10 (ALJ McKenzie).

this new infrastructure when allocating CHCF-A subsidies.² Since 2012, ratepayers in California have been funding the Small ILECs broadband infrastructure in furtherance of universal service. In 2014, the Commission determined that it was not yet time to consider the revenues that the Small ILECs Internet Service Provider (ISP) affiliates/division have been receiving through the use of the subsidized broadband infrastructure. Today, the data shows that the Small ILECs' broadband infrastructure has matured, and equity requires that ratepayers share in that success. By considering the revenues received through the Small ILECs' infrastructure in allocating CHCF-A subsidies, the Commission will achieve the balance envisioned by the Legislature in 2012.

However, the fact that the Small ILECs have successfully deployed broadband infrastructure to much of their territory does not mean that we have closed the digital divide in rural areas. Rather, the data show that while broadband infrastructure has been deployed to many residents in rural areas, far fewer actually subscribe to the service available. Deployment of broadband infrastructure capable of delivering increasingly faster speeds will not close the digital divide if consumers are not subscribing to the service. The Commission must ensure that consumers are benefiting from the additional broadband capabilities available in the Small ILECs' service territories. The Commission has the tools available to help Small ILECs achieve greater broadband adoption rates and should use them.

Predictably, the Small ILECs take an alarmist stance in opposition to any suggestion that would disturb the status quo.³ The Commission should rely on the record to determine that their alarmism is unfounded. Even in 2011, when this proceeding was first opened, the Commission understood that technological and policy changes required reform to the CHCF-A program. It should take the opportunity to finally implement them for the benefit of consumers.

² SB 379, Senate Energy, Utilities, and Communications Analysis, Aug. 28, 2012 at 3, https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201120120SB379#.

³ Small ILEC Opening Brief at 3.

III. BROADBAND DEPLOYMENT AND SUBSCRIPTION IN INDEPENDENT SMALL ILEC TERRITORIES [SCOPING MEMO, ISSUES (1)(A), (1)(E), 1(F), (9); HEARING ISSUES (1), (3), (4), (5)]

A. The Small ILECs Misrepresent the Record Regarding Broadband Deployment and Subscription Data

Small ILECs claim that the Public Advocates Office's documentation of discrepancies in the Small ILECs' deployment data are unsubstantiated.⁴ Their claim is unsupported by the record. The Public Advocates Office provided several examples where it was required to pursue further discovery in response to obvious, incorrect broadband availability data that the Small ILECs previously reported to the Commission. After the Public Advocates Office's inquiry, one Small ILEC revised broadband deployment data to show an increase of 51%.⁵ Accurate broadband deployment and subscribership data is necessary to determine the level of broadband investment that is reasonable in the Small ILEC territories.⁶ Therefore, the Commission should ensure that the Small ILECs provide accurate broadband data. By adopting the Public Advocates Office's recommendation that investment in broadband should not be approved until Small ILECs reach 87% subscribership, the Small ILECs would have a greater incentive to provide accurate reporting of broadband data and increase broadband subscriptions in their service area.⁷

The Public Advocates Office reiterates that the Commission should rely on the data produced by the Public Advocates Office on broadband deployment and subscribership. Although both the Public Advocates Office and TURN relied on data produced by the Small ILECs, the data used to produce Table 4 in Dr. Roycroft's

⁴ Small ILEC Opening Brief at 61.

⁵ Cal Adv -4C -at 1-16:16, see also 1-16 – 1-17.

⁶ In Foresthill Telephone Company's (Foresthill) general rate case (GRC), the Commission adopted plant addition costs stating that they were needed to close the digital divide and provide access to telecommunications. Broadband deployment and subscription data can be used to determine whether and to what extent plant additions would assist in closing the digital divide and provide access to communications services. Foresthill GRC Decision (D.19-04-017), May 6, 219 at 52, <http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M288/K040/288040793.PDF>

⁷ Cal Adv – 4 at 1-11:15-16.

(TURN's witness) reply testimony are of varying vintages and some include business locations as well as residential locations.⁸ These are not consistent data and cannot be compared against each other.

B. The Commission Should Continue to Collect and Use Broadband Data Provided to The FCC And the Communications Division

Small ILECs recommend using actual speeds rather than advertised speeds in making policy decisions regarding their infrastructure.⁹ However, the Small ILECs' recommendation is illogical as neither the Federal Communications Commission (FCC) nor the Commission use "actual speeds," due to limitations in collecting that data.¹⁰ The Small ILECs are aware of these limitations; their own witness stated that even if the Commission began to track availability using their "service drop" definition, it would still not account for the actual speed that the customer can receive in all instances.¹¹ The Commission should continue to collect broadband data in the existing format and use this data to make its policy decisions.

Contrary to the Small ILECs' assertions, the Communications Division's validation process is useful.¹² As noted by the Public Advocates Office's witness, Ms. Parker, the Communications Division employs the validation process to limit the overstatement of broadband availability through the exclusion of uninhabited blocks.¹³ Additionally, since

⁸ TURN-1-C, Appendix 3 Confidential, showing, for example, Calaveras' availability is as of Dec. 11, 2019 and Foresthill's availability data is as of Nov. 22, 2019 (DR Response 4.1 at 1); RT Vol. 10, 1846: 13-24 (Choe, Roycroft).

⁹ Small ILEC Opening Brief at 17.

¹⁰ See FCC 19-79 at para 12; fn 24 stating that the FCC declined to require fixed providers to submit data on actual speeds through the Form 477. See also Decision (D.) 16-12-025, stating that in order to obtain actual speed data, measuring devices would need to be placed in a sample of users homes or the public would need to use the CalSPEED application to begin measuring residential broadband in addition to mobile broadband.

¹¹ RT 1353: 21-25 (Choe, McNally)

¹² Small ILEC Opening Brief at 17.

¹³ Cal Adv -4 at 1-5: 3-10, stating that, "Without validation, the data collected by the Communications Division would tend to overstate broadband access in rural areas. This is because broadband providers report availability on a census block basis and therefore, if one household has broadband available to it, then all households in that census block are counted as having broadband availability."

the Communications Division applies the validation process to the data received from all broadband providers, the Small ILECs' data can be compared to other providers in the state, including those serving urban areas as required under PU Code §275.6(c)(5).

C. The Commission Should Incent CHCF-A Providers to Increase Broadband Subscribership

The Small ILECs claim that tying CHCF-A recovery to broadband adoption would be unlawful.¹⁴ Specifically, they argue that “rate base calculations must be based on what is ‘reasonably necessary’ to support ‘telephone corporation’ operations.”¹⁵ However, the Public Advocates Office’s recommendation has nothing to do with how rate base would be calculated. Rather, it is recommending that CHCF-A subsidies not be used to fund further investments in broadband deployment until a Small ILEC reaches 87% adoption in territories where it is the sole provider of broadband.¹⁶

The Small ILECs also claim that they already have “every incentive to maximize their subscriber base.”¹⁷ However, there are currently no subscribership incentives tied to CHCF-A subsidies. This means that whether the Small ILECs increase subscribership has no effect on the amount of CHCF-A subsidy they receive. In contrast, when Small ILECs build additional broadband infrastructure, they earn a rate of return on those investments, which is funded by the CHCF-A.¹⁸

The Public Advocates Office gathered data on broadband availability, using both the Commission’s and Small ILECs’ preferred service drop definition, and adoption, as of year-end 2018 and presented that data in its testimony.¹⁹ Broadband adoption measures the percentage of customers who have subscribed to broadband where broadband is already available.²⁰ No matter which definition is used, broadband adoption rates are

¹⁴ Small ILEC Opening Brief at 60.

¹⁵ Small ILEC Opening Brief at 60.

¹⁶ Cal Adv -4 at 1-2:2-5.

¹⁷ Small ILEC Opening Brief at 60.

¹⁸ PU Code §275.6.

¹⁹ Cal Adv -4C at 1-7 – 1-10.

²⁰ Small ILEC Opening Brief at 60, Small ILECs state that broadband adoption cannot occur if broadband

significantly lower than availability rates in the Small ILECs' territories.²¹ TURN agrees that broadband adoption is low in the Small ILECs service territory despite the presence of broadband availability, particularly in comparison to other parts of the state.²² TURN also agrees that there is a "significant difference between broadband speed levels available and those adopted by the Small ILEC customers."²³

The Public Advocates Office supports closing the digital divide. However, California will not succeed in doing so by merely focusing on broadband deployment. Even if broadband is available, the public does not benefit from broadband access if they do not subscribe to the service. Indeed, the Small ILECs fail to mention that broadband does not confer any benefits to those who do not subscribe to the service when discussing the benefits of broadband during the COVID-19 pandemic.²⁴

D. The Commission Should Require Small ILECs Or Their ISP Affiliates to Provide an Affordable Broadband Option for Low-Income Customers

The Public Advocates Office agrees with TURN that an affordable broadband option should be available for customers who want to purchase it on a standalone or bundled basis.²⁵ By accepting CHCF-A subsidies, the Small ILECs have entered into an agreement to be regulated by the Commission.²⁶ Part of the Commission's obligation in regulating the Small ILECs is ensuring the "affordability and widespread availability of safe, reliable, high-quality communications services in rural areas of the state."²⁷ Small

capable facilities do not exist, however, adoption, by definition, only measures the percentage of customers subscribing to existing or available facilities.

²¹ Cal Adv -4C at 1-7 – 1-10.

²² TURN Opening Brief at 6-8.

²³ TURN Opening Brief at 7.

²⁴ Small ILEC Opening Brief at 1, 3, 15, 18, 56, 58.

²⁵ TURN Opening Brief at 34-35.

²⁶ PU Code §275.6.

²⁷ PU Code §275.6(a).

ILECs argue that they cannot afford to lower rates for LifeLine customers.²⁸ However, under the Public Advocates Office’s imputation recommendation, any reduction in revenues due to discounted rates would be accounted for when determining net revenues.²⁹

IV. BROADBAND IMPUTATION [SCOPING MEMO, ISSUES (1)(C), (1)(D), HEARING ISSUE (2)]

A. Retail Imputation

1. The Commission Determined in Phase 1 That It Has the Legal Authority To Impute Broadband Revenues And That Authority Has Not Changed.

The Small ILECs claim that the Commission cannot rely on its previous Phase 1 Decision (D.14-12-084) finding that it has the authority to impute broadband revenues.³⁰ The crux of their argument is that because the Commission decided not to impute revenues, any language regarding its authority to do so is only dicta and cannot be relied on here.³¹ This is incorrect. PU Code §1705 requires that the Commission include findings of fact and conclusions of law on all issues material to the order or decision. D.14-12-084 included several findings of fact and conclusions of law regarding its authority to impute broadband revenues.³² Additionally, based on that authority, the Commission ordered the Communications Division to conduct the Broadband Study so that the Commission could determine when it would be appropriate to impute broadband revenues.³³ Therefore, the Commission’s findings and conclusions cannot be characterized as dicta.

Even if the Commission’s findings, conclusions, and orders were considered dicta (which they are not), case law provides that such dicta may still be relied upon and even

²⁸ Small ILEC Opening Brief at 19-20.

²⁹ RT Vol. 12, 2105: 2-6 (Ahlstedt).

³⁰ Small LECs Opening Brief at 12.

³¹ Small LECs Opening Brief at 12.

³² D.14-12-084 at 89, FOF 15; 93, COL 1-3.

³³ D.14-12-084 at 100, Ordering Paragraph 1.

considered precedent.³⁴ For example, in *Smith v. County of Los Angeles*, the court held that dictum should be followed “where it demonstrates a thorough analysis of the issue or reflects compelling logic.”³⁵ Here, all parties provided testimony on the legality of imputation, participated in hearings on that topic, and subsequently briefed the issue. After hearing parties’ analysis of the issue, the Commission correctly concluded that it had the authority to impute broadband revenues.

Since the Commission has already considered the Small ILECs arguments regarding the legality of imputation, it should not waste its time revisiting these arguments. Specifically, the Commission considered the following arguments: (1) whether imputation of either retail or wholesale revenue amounts to broadband regulation;³⁶ (2) whether imputation violates PU Code §§275.6 (c)(2), 275.6 (b)(3), 275.6 (b)(4) because it affects rate of return regulation;³⁷ (3) whether imputation would result in an unlawful taking of property in violation of the constitution;³⁸ (4) whether PU Code §275.6 permits imputation;³⁹ (5) whether the Commission’s powers under PU Code §701 supports its authority to impute;⁴⁰ and (6) whether the Commission’s powers under §706 of the Federal Telecommunications Act supports its authority to impute.⁴¹ The Commission should rely on the existing record to conclude that it continues to have authority to impute both retail and wholesale broadband revenues.

The Commission determined that it had the authority to impute broadband revenues despite the fact that Internet access service was considered an information

³⁴ *Donorovich-Odonnell v. Harris* (2015) 241 Cal.App.4th 1118, 1139, stating, “Additionally, we may give even dicta persuasive weight when “it demonstrates a thorough analysis of the issue or reflects compelling logic.”

³⁵ *Smith v. County of Los Angeles* (1989) 214 Cal.App.3d 266, 297.

³⁶ Small ILEC Phase 1 Opening Brief at 14 -19. Small ILEC Phase 1 Opening Brief at 17-19.

³⁷ Small ILEC Phase 1 Opening Brief at 19- 20.

³⁸ Small ILEC Phase 1 Opening Brief at 20-21.

³⁹ Small ILEC Phase 1 Opening Brief at 26-48.

⁴⁰ Small ILEC Phase 1 Opening Brief at 48-50.

⁴¹ Small ILEC Phase 1 Opening Brief at 50-52.

service at the time of the Phase 1 decision.⁴² This conclusion is correct because imputation of broadband revenues does not equate to regulation of ISPs.⁴³ Imputation is a ratemaking mechanism that would be applied to the regulated utility. Therefore, it does not matter whether Internet access service is categorized as either an information or telecommunications service.⁴⁴ Since the Phase 1 CHCF-A decision, the FCC has vacillated on whether Internet access service is a telecommunications or information service. In the Restoring Internet Freedom Act of 2018 the FCC classified Internet access service as an information service, just as it was in 2014 when the Phase 1 Decision was adopted. However, when the Restoring Internet Freedom Act was upheld by the D.C. circuit court in *Mozilla v. FCC*, the court left the door open for state regulation of broadband by vacating the Restoring Internet Freedom Act’s preemption directive, which had sought to apply a blanket restriction on any state regulation.⁴⁵ In doing so, the court recognized that states have always had a role in broadband regulation.⁴⁶ Thus, its decision has no effect on the Commission’s authority in regard to imputation. Imputation did not then, and still does not today, conflict with federal law.

2. Imputation of Broadband Revenues Is Equitable

Small ILECs suggest that the Public Advocates Office only supports imputation in order to reduce the amount that ratepayers must pay to fund the CHCF-A.⁴⁷ However, the

⁴² D.14-12-084 at 89, Finding of Fact (FOF) 15; 93, Conclusion of Law (COL) 1-3; 100, Ordering Paragraph 1.

⁴³ This is analogous to revenue sharing with ratepayers for sale of non-tariffed products and services in the water industry. See San Jose Water GRC (D.14-08-006) at 103, where parties agreed that revenue from non-tariffed products and services that use utility assets should be allocated to ratepayers pursuant to D. 00-07-018, as modified by D.10-10-019, <https://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M102/K241/102241501.PDF>.

⁴⁴ D.14-12-084 at 93, COL 1, stating that “neither state nor federal law prohibits broadband revenue imputation and the decision of whether to do so is left to the Commission based on the record.” See also Conclusions of Law 3, stating that “broadband revenue imputation is a ratemaking mechanism within the Commission’s regulatory authority to regulate telecommunications companies.”

⁴⁵ *Mozilla Corporation v. Federal Communications Commission* (D.C. Cir. 2019) 940 F.3d 1, 74.

⁴⁶ *Mozilla Corporation v. Federal Communications Commission* (D.C. Cir. 2019) 940 F.3d 1, 81.

⁴⁷ Small ILEC Opening Brief at 40.

Public Advocates Office has been clear; the Commission should impute broadband revenues because it is equitable and consistent with statute. The CHCF-A is funded by a surcharge that is paid by all ratepayers in the state.⁴⁸ Parties agree that the CHCF-A helped fund broadband deployment in the Small ILECs' territories.⁴⁹ Specifically, the Small ILECs are permitted to put investments in broadband into rate base, which means that the Small ILEC receive monies from ratepayers, federal subsidies, and the CHCF-A, and earns a return on the investment.⁵⁰ The Small ILECs' ISP affiliate or division collects broadband revenue from customers but does not contribute to the cost of building the broadband network. The Small ILECs acknowledge this, stating that ISPs are an expense intensive, rather than a capital intensive business.⁵¹ It is only equitable for the Commission to consider the profits earned from the infrastructure funded by the CHCF-A before allocating additional CHCF-A subsidies to the Small ILECs.

The Legislature also believed that imputation was equitable. In 2012 when it decided to permit the CHCF-A to fund investment in broadband infrastructure, it also added PU Code §275.6(e), permitting the Commission to consider broadband revenues in allocating CHCF-A subsidies.⁵² Thus, the Legislature believed that if CHCF-A subsidies were used to construct broadband infrastructure, it would be reasonable for the Commission to consider broadband revenues received from those facilities before the Commission allocated additional CHCF-A subsidies.

Lastly, the Small ILECs claim that imputation would result in an unfair business advantage because other companies are not subject to imputation.⁵³ However, the Small ILECs undermine their own argument. Other companies would not be subject to

⁴⁸ PU Code §275.

⁴⁹ RT Vol. 7, 1082: 10-15 (Fortune, Duval); see also RT Vol. 7, 902-904:27-1 (Choe, Duval); RT Vol. 9, 1407: 4-24 (Boos, Choe); TURN Opening Brief at 11, Small ILECs Opening Brief at 15.

⁵⁰ PU Code § 275.6(c)(6).

⁵¹ RT Vol. 11, 1897: 8-26 (Votaw); RT Vol. 10, 1716: 2-3 (Aron).

⁵² SB 379, Senate Energy, Utilities, and Communications Analysis, Aug. 28, 2012 at 3, https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201120120SB379#.

⁵³ Small ILEC Opening Brief at 32. See Cal Adv-4 at 1-10:2, showing competitors of CHCF-A recipients.

imputation because they do not participate in the CHCF-A program and therefore do not receive subsidies. In fact, the Small ILECs already have an advantage over their competitors, where they exist, because they receive CHCF-A subsidies whereas their competitors do not.⁵⁴

3. The Small ILECs s Already Produce Consolidated Audited Financial Statements

The Public Advocates Office clarifies that under its imputation proposal, the Small ILEC and its ISP affiliate would produce consolidated audited financial statements identical to those the Small ILECs already create. The audit would be conducted by a financial auditor to determine whether the financials are fairly stated. Since the Small ILECs already produce these documents on a consolidated company basis, it would not add an additional expense or burden to provide the documents in general rate cases (GRCs).

B. Wholesale Imputation

1. Wholesale Imputation Is Not Illegal

Small ILECs and TURN claim that imputation of wholesale revenues would be illegal.⁵⁵ However, Small ILECs also seem to imply that if wholesale revenue imputation were to operate as a reduction to CHCF-A without any impact to the federal regulatory apparatus it would not be “illegal.”⁵⁶ This reduction is exactly what the Public Advocates Office proposes. Thus, there would be no revenue shortfall or a reduction in the rate of return.⁵⁷ Rather, the Commission would consider broadband revenues in addition to other streams of revenue (such as the CHCF-A and federal subsidies). Furthermore, as stated previously, the Commission considered imputation of both retail and wholesale revenues in Phase 1 and found that it had the authority to impute broadband revenues without

⁵⁴ Cal Adv-4 at 1-10:2.

⁵⁵ Small ILEC Opening Brief at 44-55; TURN Opening Brief at 32-34.

⁵⁶ Small ILEC Opening Brief at 45.

⁵⁷ Small ILEC Opening Brief at 43.

making a distinction between the two types of revenues.⁵⁸ Similar to imputation of retail revenues, imputation of wholesale revenues does not violate federal or state laws because it does not require changing the categorization of any funds. TURN supports its proposal for imputing retail broadband stating that imputation is “possible and necessary even though retail broadband services are not tariffed or directly regulated by the Commission.”⁵⁹ Similarly, although wholesale revenues are not directly regulated by the Commission, those revenues can be considered when determining the amount of CHCF-A subsidies. Contrary to TURN’s assertions, this does not require any changes to the federal cost allocation rules or separations rules.⁶⁰

V. RATEMAKING TREATMENT OF EXPENSES

A. Corporate Expense Cap. [Scoping Memo, Issues (2)(B)(I), (2)(B)(ii), (2)(B)(IV)]

1. Small ILECs Do Not Raise Any New or Persuasive Arguments for Changing The Corporate Expense Cap

In Phase 1, the Commission found that the Corporate Operations Expense Cap is a rational mechanism for calculating and determining a reasonable level of corporate expenses for those carriers drawing from the CHCF-A.⁶¹ The Small ILECs do not raise any new arguments that should cause the Commission to revise its finding. For example, the Small ILECs argue again that California has higher costs than other states and therefore, the Commission should modify the FCC’s Corporate Operations Expense Account cap formula to account for that.⁶² In Phase 1, the Small ILECs made the same argument.⁶³ And in fact, on this point, the Small ILECs have been rearguing their

⁵⁸ D.14-12-084 at 89, FOF 15; 93, COL 1-3.

⁵⁹ TURN Opening Brief at 12.

⁶⁰ TURN Opening Brief at 32.

⁶¹ D.14-12-084 at 90, FOF 23.

⁶² Small ILEC Opening Brief at 52; see also Small ILEC Phase 1 Opening Brief at 96.

⁶³ Small ILEC Phase 1 Opening Brief at 96-97.

position in every GRC subsequent to 2014, to no avail.⁶⁴ Based on this claim, the Small ILECs ask that the Commission include a “regional adjustment” with the Corporate Operations Expense Account cap.⁶⁵ However, the FCC’s Corporate Operations Expense Account cap was calculated using a formula that took into account data submitted by all companies and then setting a range of reasonableness for each study area where the upper limit of that range is 115% of the projected level of corporate expenses for each expense line. Thus, the FCC’s formula already accounts for variability in costs and sets an upper limit on expenses that can be 115% greater than projected.⁶⁶ The Small ILECs did not provide any evidence that could be used to calculate or justify an additional adjustment.

Inexplicably, Mr. Duval, the Small ILECs’ witness, cited to one website as evidence that average costs in California are higher than in Mississippi and Alaska, but then used a different website to compare average costs in rural areas of California with rural areas of all other states.⁶⁷ Based on his analysis he states that the Regional Price Parity (RPP) in nonmetropolitan California is 97.2% whereas the average RPP in nonmetropolitan areas nationwide is 89.68%. However, Mr. Duval failed to consider that the FCC’s Corporate Operations Expense Account cap formula already accounts for different costs among study areas. Finally, if the Small ILECs believe that the FCC is calculating the Corporate Operations Expense Account cap incorrectly and have evidence to support that contention, they should petition the FCC rather than attempting to collect increased CHCF-A subsidies.

2. The Commission May Lawfully Remove the Rebuttable Presumption of Reasonableness

The Small ILECs claim that removing the ability to rebut the presumption of reasonableness would be unlawful “as it would necessarily foreclose recovery of

⁶⁴ Cal Adv -13 at 1-7:11-16.

⁶⁵ Small ILEC Opening Brief at 52.

⁶⁶ See also FCC 97-157 para 283, “...recognizing that small study areas, based on the number of lines, may experience greater amounts of corporate operations expense per line than larger study areas.”

⁶⁷ LEC - 1 at 39-40: 17-24; 41:1-15.

reasonable expenses just because they are deemed to exceed the cap.”⁶⁸ This misrepresents how the Corporate Operations Expense Account cap functions. As the Small ILECs are aware, the cap does not prevent recovery of expenses, rather, it ensures that the CHCF-A does not subsidize expenses that exceed the cap.⁶⁹ In the most recent GRC cycle, the Small ILECs abused the opportunity to rebut the presumption of reasonableness by inappropriately relitigating the legitimacy of the Corporate Operations Expense Account cap and did not raise any arguments that supported raising the cap.⁷⁰ Thus, the Commission should eliminate the ability to rebut the presumption of reasonableness of the Corporate Operations Expense Account cap.

TURN appears to support the rebuttable presumption,⁷¹ citing variability among the size and efficiency of each small ILEC.⁷² However, as noted previously, the Corporate Operations Expense Account cap formula already accounts for these differences. The cap is a limit that was established after the FCC conducted a cost study of rural telephone companies throughout the country. Based on that cost study, the FCC determined a range of reasonable costs. Additionally, in order to account for variability among study areas, the FCC multiplied the costs determined in the cost study by 115%.⁷³ Furthermore, TURN has not participated in the review of individual Small ILECs’ GRCs unlike the Public Advocates Office.⁷⁴ The Public Advocates Office’s detailed review of

⁶⁸ Small ILEC Opening Brief at 52.

⁶⁹ Decision Approving Pinnacles GRC TY 2019 (D.19-12-011) December 5, 2019 at 29, <http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M321/K514/321514031.PDF>, stating, “Adopting and applying the FCC Corporate Expense Caps will cap the amount of corporate expenditures *that can be recovered* from the CHCF-A program, and create incentives to align expenditures with the cap to reduce rate case litigation costs.” Emphasis added.

⁷⁰ Small ILECs argue that the Commission did not consider any of the Small ILECs’ evidence to rebut the application of the cap (Small ILEC Opening Brief at 51), however, this is false and in fact, the Small ILECs spend millions in legal fees and special witness fees to do so. Cal Adv – 11 at 1-2:3, 1-5:6. Even Mr. Duval notes that the Small ILECs were given the opportunity to present evidence in support of rebutting the cap. Small ILEC Opening Brief at 51, fn 320.

⁷¹ TURN Opening Brief at 36-37, this argument is included in section regarding operating expenses, but appears to relate to the Corporate Operations Expense Account cap.

⁷² TURN Opening Brief at 36.

⁷³ Cal Adv – 10 at 1-4:14-17; FCC 11-161A1 at Appendix C, para. 6.

⁷⁴ See also RT Vol. 10, 1803: 5-7, Dr. Roycroft, TURN’s witness, stating that he is “not familiar enough

Corporate Operations Expense Account across multiple GRCs supports that the Corporate Operations Expense Account cap already accounts for the size of each Small ILEC and that expenses should be managed within that cap.

VI. RATE CASE EXPENSES. [SCOPING MEMO, ISSUES (2)(B)(I), (2)(B)(II), (2)(B)(IV)]

A. Recovery of Rate Case Expenses as Part of The Corporate Operations Expense Account Cap Is Consistent With Commission Precedent

Contrary to Small ILECs' claim, the Public Advocates Office's proposal does not preclude recovery of rate case expenses.⁷⁵ The Public Advocates Office only argues that rate case expenses be recovered as part of the Corporate Operations Expense Account, in accordance with Commission and federal rules. The Commission specifically included rate case expenses in the Corporate Operations Expense Account cap to reduce litigation costs.⁷⁶ Small ILECs also claim that including rate case expenses would force Small ILECs to "endure a burdensome and expensive rate case without cost recovery..."⁷⁷ This misrepresents the facts. First, Small ILECs choose to be regulated under rate of return regulation in exchange for receiving CHCF-A subsidies. They have the option to forego a rate case and not receive CHCF-A subsidies. Second, the expense of rate cases is not something that is outside of the Small ILECs' control. They have consistently chosen to hire witnesses to make arguments barred by res judicata and cause unnecessary delay to GRCs.⁷⁸

The Small ILECs erroneously cite to recent GRCs for Cal-Ore Telephone Co. (Cal-Ore), Calaveras Telephone Company (Calaveras), and Pinnacles Telephone Co. (Pinnacles) as evidence that the Commission has authorized recovery of rate case

with the details of how the rate case procedures unfold."

⁷⁵ Small ILEC Opening Brief at 39, 53.

⁷⁶ D.14-12-084 at 24 stating, "Adopting and applying the FCC Corporate Expense Caps will not limit the amount of a company's corporate expenditures, but will limit the amount of corporate expenditures that can be recovered from the CHCF-A program."

⁷⁷ Small ILEC Opening Brief at 3, 54.

⁷⁸ Small ILEC Opening Brief at 39. Cal Adv – 12 at 1-3:14.

expenses outside of the Corporate Operations Expense Account cap.⁷⁹ This is false. Cal-Ore and Calaveras' GRCs were resolved through settlement and any authorized amounts do not negate the Commission's specific intent in the 2014 Phase 1 Decision to apply the Corporate Operations Expense Account cap to reduce rate case litigation costs.⁸⁰ Furthermore, pursuant to Rule 12.5 of the Commission Rules of Practice and Procedure, adoption of a settlement agreement does not constitute precedent regarding any principle or issue in the proceeding or in any future proceeding. Additionally, in the Pinnacles GRC, the Commission explicitly stated its intent that the company should not recover its rate case expenses outside of the Corporate Operations Expense Account cap.⁸¹ The Commission should also disregard the Small ILECs' reference to decisions before the 2014 Phase 1 Decision⁸² regarding rate case expenses, as those conclusions were superseded by the 2014 Phase 1 Decision.

B. Operating Expenses [Scoping Memo, Issue (2)(B)(III)]

1. It Is Reasonable to Limit the Amount Of Operating Expenses That Can Be Recovered Through CHCF-A Subsidies

The Small ILECs misrepresent the Public Advocates Office's recommendation when they state that "the goal of the CHCFA program is not to force rural telecommunications providers to arbitrarily reduce their operating costs..."⁸³ The Public Advocates Office seeks to set a reasonable cap on operating expenses above which the Small ILECs could not collect CHCF-A subsidies. Thus, the Commission would never "reject reasonable expenses."⁸⁴ Additionally, if a Small ILEC chose to reduce its operating costs so that all of its operating expenses would continue to be subsidized by

⁷⁹ Small ILEC Opening Brief at 53.

⁸⁰ D.14-12-084 at 29.

⁸¹ D.19-12-011 at 33, COL 14, stating, "The rate case costs of Pinnacles should be included within the corporate expense cap."

⁸² Small ILEC Opening Brief at 53.

⁸³ Small ILEC Opening Brief at 55.

⁸⁴ Small ILEC Opening Brief at 56.

the CHCF-A, presumably, it would act rationally and find efficiencies rather than “arbitrarily” reducing their costs. The Small ILECs’ arguments reveal another benefit of a cap.

The Small ILECs cite to various outside factors that they believe make it unreasonable to apply the FCC’s operating expense cap to intrastate operating expenses.⁸⁵ None of these arguments are persuasive. First, the Commission should not be persuaded by the Small ILECs’ opportunistic injection of the COVID-19 pandemic into the proceeding. None of the costs related to this pandemic, if any, can be definitively calculated as of today and are not part of the record. Furthermore, it is unclear at this time whether the Commission might provide for other relief in response to this unprecedented event. Second, the Small ILECs cite to their obligations to implement STIR/ SHAKEN.⁸⁶ However, the FCC found that implementing STIR/ SHAKEN would reduce network costs and reduce customer service costs related to illegal calls for voice service providers.⁸⁷ Third, the Small ILECs argue that because the data used to calculate the operating expense limitation is historical, it cannot be used in a GRC. However, the Public Advocates Office proposes that these historical figures be grown using the most recent available indices from the Bureau of Economic Analysis.⁸⁸ Lastly, there has been a continuous decline in customers using traditional telephone service, which means that operating expenses will only decline in the future.⁸⁹

2. Applying GDP CPI in Conjunction with The National Exchange Carrier Association (NECA)

⁸⁵ Small ILEC Opening Brief at 54-57.

⁸⁶ Small ILEC Opening Brief at 56, fn. 354.

⁸⁷ FCC 20-42, para 51. STIR/ SHAKEN is a technology that allows voice service providers to verify that the caller ID information transmitted with a particular call matches the caller’s number.

⁸⁸ RT Vol. 12, 2215: 3-9.

⁸⁹ Cal Adv – 1 at 4-6 to 4-8.

Inflation Figures Will Align the Operating Expense Cap With A Future Test Year

The Small ILECs argue that using the Public Advocates Office’s proposed method would not align the operating expense cap with a future test year.⁹⁰ The Small ILECs misrepresent how the Public Advocates Office proposes to apply the NECA inflation factors to obtain an operating expense cap for a future test year. In hearings, counsel for the Small ILECs questioned Ms. Montero, the Public Advocates Office’s witness, on Calaveras’ response to data request PHH-001 B(4)(A).⁹¹ In that response Calaveras provided the computation of the operating expense limit for 2017, using the formula and method determined by the FCC.⁹² This method took historical data from 2016 and applied NECA’s gross domestic product-chain-type price index (GDP-CPI) Adjustment Factor to obtain the 2017 operations expense cap. NECA regularly publishes its projected GDP-CPI Adjustment Factor and it had projected that it would be 1.0273 for 2017.⁹³ Using the method used for 2017 as an example, Ms. Montero proposed that an operating expense cap for a hypothetical future test year could be derived by applying the GDP-CPI Adjustment Factor to historical data.⁹⁴ For example, NECA’s projected GDP-CPI Adjustment Factor for 2020 could be applied to historical data from 2019 to determine a 2020 operating expense cap. It is true that the cap would be based on historical data to project the future test year, but using the GDP-CPI Adjustment Factor to grow the historical data would be an efficient method to approximate future expenses. Furthermore, the Commission has already used the GDP-CPI Adjustment Factor in Small ILEC GRCs to inflate the Corporate Operations Expense Account cap, stating that the “NECA GDP-CPI factor...is the appropriate factor to use.”⁹⁵

⁹⁰ Small ILEC Opening Brief at 57.

⁹¹ RT Vol. 12, 2204:3-17.

⁹² Cal Adv – 7C, Attachment D-9.

⁹³ Cal Adv – 7 at 1-5, Table 2.

⁹⁴ Cal Adv – 7 at 1-5.

⁹⁵ D.19-04-017 at 32-33.

VII. RATEMAKING TREATMENT OF INVESTMENTS

A. Small ILECs Historical Investments Show That The Public Advocates Office’s Methodology Would Be Reasonable And Efficient

Contrary to the Small ILECs’ claim, the Public Advocates Office did not misrepresent the Small ILECs’ historical level of investment.⁹⁶ The Public Advocates Office’s testimony states that on average from 2011-2018 rate base for the Small ILECs was nearly flat and year to year variances were, for the most part, +/-10%.⁹⁷ The result is that, on average, rate base changed little during that period. Additionally, any investments that the Small ILECs make will be included in their cost study and reflected in the next rate case. Thus, there may even be some GRCs where more investment is forecasted than is needed by the company.⁹⁸ Lastly, as stated previously, investments in response to COVID-19 are not part of the record and it is unclear what infrastructure investments, if any, are directly attributed to COVID-19 response. However, if the Small ILECs make investments during 2020 in response to the COVID-19 pandemic, those investments would be reflected in the next year’s NECA cost studies and would be captured in subsequent GRCs.

VIII. MODIFICATIONS TO THE RATE CASE PROCESS. [SCOPING MEMO, ISSUES (2)(B)(I), (2)(B)(IV), (8)]

A. The Small ILECs Recommended Procedural Changes To GRCs Will Violate Due Process And Exacerbate Inefficiencies

The Public Advocates Office opposed the Small ILECs’ recommended procedural changes to GRCs in its Opening Brief and will not reiterate every point here. However, the Public Advocates Office replies to some portions of the Small ILECs’ statements in Opening Briefs that require clarification.

⁹⁶ Small ILECs Opening Brief at 34, 58-60.

⁹⁷ Cal Adv – 9C at 1-5 – 1-6: 11-3.

⁹⁸ Cal Adv – 9C at 1-7:14-16.

The Small ILECs purport to show the benefits of holding public participation hearings (PPH) after the Public Advocates Office's testimony by citing to the anecdotal testimony of Mr. Boos, the Small ILECs' witness, in regard to Ponderosa's 2018 GRC.⁹⁹ However, Mr. Boos was only able to state that unnamed and an unspecified number of customers appreciated the opportunity to provide input on all proposals.¹⁰⁰ Furthermore, he did not state that more customers attended the PPH held after the Public Advocates Office provided its testimony nor did he state that customers provided more input. In contrast, the Commission has already determined that holding PPHs before the Public Advocates Office's testimony is beneficial because it allows the Public Advocates Office to incorporate information it receives at the PPH in its testimony.¹⁰¹ The Commission should not change its established policy based on the anecdotal statements of one witness representing one company.

The Small ILECs claim that because the Public Advocates Office participates as a party in GRCs, it is somehow no longer entitled to its statutory discovery rights.¹⁰² The Small ILECs fail to support this statement with any case law or other statutes, as none exist.

Finally, the Commission should not shorten the time that the Public Advocates Office is afforded to serve its rebuttal testimony.¹⁰³ The Public Advocates Office is already at a disadvantage because the Small ILECs have all the information about their business. Thus, the Public Advocates Office must use the discovery process to obtain the information that supports its rebuttal testimony. The last GRC cycle has shown that the

⁹⁹ Small ILEC Opening Brief at 63.

¹⁰⁰ LEC -4 at 40:8-11.

¹⁰¹ Public Advocates Office Reply Comments to Fourth Amended Scoping Memo at 18; A.17-10-003, Scoping Memo and Ruling, March 13, 2018 at 9, <http://docs.cpuc.ca.gov/SearchRes.aspx?DocFormat=ALL&DocID=212071656>; See also ALJ's ruling that the PPH should be held before testimony because ratepayers' concerns inform what the Commission, including decisionmakers and the Public Advocates Office, should focus on. A.17-10-003, prehearing conference transcript 33:4-8.

¹⁰² Small ILEC Opening Brief at 66

¹⁰³ Small ILEC Opening Brief at 66.

Small ILECs often impede that process, which requires additional time to obtain the necessary information.¹⁰⁴ Furthermore, the Public Advocates Office must also complete site visits and attend public participation hearings before it can begin to draft its rebuttal testimony. Lastly, in D.15-06-048 the Small ILECs previously proposed shortening time for the Public Advocates Office and the Commission rejected that proposal.¹⁰⁵

Based on the above considerations, the Small ILECs' recommended procedural changes to GRCs should be rejected.

IX. BASIC SERVICE RATES AND OTHER END USER RATE PROPOSALS [SCOPING MEMO, ISSUE (4)]

A. The Commission Should Gradually Make Small ILECs' Rates Comparable to Urban Rates

TURN argues that because GDP-CPI is not used by NECA to set rates and has little relation to telephone companies it should not be used to increase local rates.¹⁰⁶ However, the Public Advocates Office does not argue that GDP-CPI is used to set rates and that is not the basis of its argument. Rather, the Public Advocates Office suggested the using GDP-CPI to gradually increase local rates because it is already in use by NECA in a separate filing and it is updated annually.¹⁰⁷ The Public Advocates Office would be amenable to using another inflation index provided that parties agree to it beforehand and that it is publicly available and updated annually. Additionally, the Public Advocates Office notes that the Small ILECs' rates are already not tied to the cost of service because the CHCF-A program subsidizes cost. In fact, without CHCF-A, the Small ILECs' rates would increase to over \$100 per month for basic service.¹⁰⁸

¹⁰⁴ Cal Adv – 12 at 1-3:14.

¹⁰⁵ Decision Adopting Rate Case Plan (D.15-06-048) June 26, 2015 at Appendix A, p. 3; Small ILECs' Opening Comments to Proposed Decision Adopting a Rate Case Plan, June 15, 2015 at 12-13.

¹⁰⁶ TURN Opening Brief at 38.

¹⁰⁷ Ahlstedt Opening Testimony at

¹⁰⁸ Small ILECs Opening Brief at 2.

The Small ILECs also argue that increasing rates at regular intervals outside of a GRC would not provide customers with notice.¹⁰⁹ However, there is nothing that prohibits the Commission from providing notice of such rate increases before they are implemented.

The Commission should increase the Small ILECs' local rates at the same rate as inflation to gradually make rates comparable to urban rates, as required by Public Utilities (PU) Code §275.6(c)(3).

X. RATEMAKING TREATMENT OF MISCELLANEOUS REVENUES [SCOPING MEMO, ISSUE (5)]

The Public Advocates Office does not comment on this topic.

XI. CHCF-A ANNUAL FILING PROCESS [SCOPING MEMO, ISSUE (7)]

The Public Advocates Office clarifies that broadband service quality rules¹¹⁰ should be addressed at workshops.¹¹¹

XII. CONCLUSION

The Commission should disregard the Small ILECs' repetitive arguments regarding the legality and appropriateness of broadband imputation. Instead, the Commission should take this opportunity to incorporate broadband availability and subscribership data as well as the experience of the last round of GRCs to reform the CHCF-A program.

Respectfully submitted,

/s/ CANDACE CHOE

Candace Choe
Attorney for the

Public Advocates Office
California Public Utilities Commission

¹⁰⁹ Small ILECs Opening Brief at 69.

¹¹⁰ Small ILECs Opening Brief at 31.

¹¹¹ RT Vol. 6, 402:11-19.

May 19, 2020

505 Van Ness Avenue
San Francisco, CA 94102
Telephone: (415) 703-5651
Email: Candace.Choec@cpuc.ca.gov