

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Calaveras Telephone Company (U 1004 C), Cal-Ore Telephone Co. (U 1006 C), Ducor Telephone Company (U 1007 C), Foresthill Telephone Co. (U 1009 C), Kerman Telephone Co. (U 1012 C), Pinnacles Telephone Co. (U 1013 C), The Ponderosa Telephone Co. (U 1014 C), Sierra Telephone Company, Inc. (U 1016 C), The Siskiyou Telephone Company (U 1017 C), and Volcano Telephone Company (U 1019 C) For Rehearing of Resolution T-17616

Application 18-12-010

ORDER DENYING REHEARING OF RESOLUTION T-17616

In this Order, we dispose of the Application for Rehearing of Resolution T-17616 (Resolution) by Calaveras Telephone Company (U 1004 C), Cal-Ore Telephone Co. (U 1006 C), Ducor Telephone Company (U 1007 C), Foresthill Telephone Co. (U 1009 C), Kerman Telephone Co. (U 1012 C), Pinnacles Telephone Co. (U 1013 C), The Ponderosa Telephone Co. (U 1014 C), Sierra Telephone Company, Inc. (U 1016 C), The Siskiyou Telephone Company (U 1017 C), and Volcano Telephone Company (U 1019 C), filed on December 14, 2018. We deny rehearing, but order modifications to Resolution T-17616, as discussed below.

BACKGROUND

The Commission administers the California High Cost Fund A (CHCF-A) program pursuant to Public Utilities Code section 275.6 as part of the state’s universal service commitment to the continued affordability and widespread availability of safe, reliable, high quality communications services in rural areas of the state.¹ The CHCF-A funds support the ten Independent Small Local Exchange Carriers (Small LECs) subject

¹ All subsequent section references are to the Public Utilities Code unless otherwise stated.

to rate-of-return regulation in amounts sufficient to meet their Commission authorized revenue requirements.² The Commission adopts the revenue requirement as well as the CHCF-A support in the carriers' respective General Rate Cases (GRCs). These amounts may be updated by post-GRC Cost of Capital proceedings. The Commission verifies a carrier's eligibility for continued funding through an annual advice letter process outlined in the CHCF-A rules in Decision (D.) 91-09-042.³

On December 22, 2017, Congress enacted the Tax Cut and Jobs Act of 2017 (TCJA), which substantively reduced the top corporate income tax rate from 35 percent to 21 percent.⁴ The new law became effective on January 1, 2018.

In general, the Commission treats income tax expense as a revenue requirement component during the Test Year of a GRC. Noting that the impact of the TCJA could be lost without regulatory action, the CPUC's Communications Division Director sent a letter to the ten Small LECs on March 16, 2018.⁵ The letter acknowledged that Calaveras, Cal-Ore, Ponderosa, and Sierra had a GRC for Test Year 2018 and had already filed Tier 2 advice letters to account for the TCJA tax changes.⁶ The letter directed the remaining six Small LECs—Ducor, Foresthill, Kerman, Pinnacles, Siskiyou, and Volcano—to file separate Tier 1 Advice Letters to establish a Tax Accounting Memorandum Account, effective April 1, 2018, to track the realized tax

² Calaveras Telephone Company (U 1004 C), Cal-Ore Telephone Co. (U 1006 C), Ducor Telephone Company (U 1007 C), Foresthill Telephone Co. (U 1009 C), Kerman Telephone Co. (U 1012 C), Pinnacles Telephone Co. (U 1013 C), The Ponderosa Telephone Co. (U 1014 C), Sierra Telephone Company, Inc. (U 1016 C), The Siskiyou Telephone Company (U 1017 C), and Volcano Telephone Company (U 1019 C) (collectively, the "Small LECs").

³ See, e.g., D.91-05-016, Appendix A, at p. 2 (slip op.).

⁴ See, Public Law 115-97.

⁵ At the time, the Small LECs' authorized revenue requirement was based on a 34 percent federal income tax rate and not the top 35 percent corporate tax rate.

⁶ Adjustments to revenue requirement and CHCF-A support adjustments for these companies are addressed in Res. T-17626 (Calaveras), adopted August 23, 2018, and Res. T-17617 (Cal-Ore), Res. T-17618 (Ponderosa), and Res. T-17619 (Sierra), which were all adopted August 9, 2018.

savings of the TCJA on Commission-jurisdictional revenue requirements. The six Small LECs followed suit, each submitting an Advice Letter on March 30, 2018.

On November 14, 2018, the Commission issued Resolution (Res.) T-17616, authorizing an aggregate reduction of \$1,291,652 in revenue requirement and a corresponding reduction in CHCF-A support for the period April 1, 2018 through December 21, 2018. The reduction in revenue requirement and CHCF-A support amount reflects Staff's recalculation of each of the carriers' last GRC Test Year results of operations from a 34 percent Federal Income Tax Rate (FTIR) to the 21 percent FTIR established by the new law.

On December 14, 2018, all ten Small LECs jointly and timely filed this application for rehearing of Res. T-17616, asserting that the adjustments to Ducor, Foresthill, Kerman, Pinnacles, Siskiyou, and Volcano revenue requirements and CHCF-A support are unlawful because:

- (1) The Resolution fails to proceed in manner required by law and is unsupported by the findings pursuant to Pub. Util. Code § 1757(a)(2) and (3)
- (2) The Resolution is arbitrary and capricious, and an abuse of discretion per Pub. Util. Code § 1757(a)(5)
- (3) The Resolution violates due process rights without hearing or notice and opportunity to be heard; and
- (4) The Resolution is an illegal taking of the companies' property.

The Small LECs claim that the Resolution's incorrect findings may be used to make open-ended adjustments to the Small LECs' CHCF-A support. The ten Small LECs also assert the discussion in Res. T-17616 regarding the treatment of excess deferred taxes using the normalization method in future rate cases constitutes an unlawful predetermination of the outcome of those rate cases.

In our review of this Application for Rehearing, we consider the following issues:

1. Whether the Commission may adjust Small LEC revenue requirement and corresponding CHCF-A support based on tax law changes between GRCs.
2. Whether Res. T-17616 erred by discussing the normalization (disposal) of excess deferred income tax to be raised in the carriers' next GRC.

DISCUSSION

I. THE COMMISSION IS NOT PROHIBITED FROM MAKING CERTAIN ADJUSTMENTS BASED ON FEDERAL TAX LAW CHANGES BETWEEN GENERAL RATE CASES.

A. The Small LECs' narrow reading of the CHCF-A rules adopted by D.91-09-042 conflicts with section 275.6.

The Small LECs argue Res. T-17616 fails to proceed in a manner required by law because “regulatory changes of industry-wide effect” only applies to orders by the Commission or the Federal Communications Commission (FCC). The Small LECs claim the change in tax law embodied in the TCJA cannot satisfy the standards in D.91-09-042 for making adjustments to ratemaking metrics between rate cases because the TCJA is not a “regulatory change” resulting from a Commission or FCC order.⁷ Since the TCJA is an act of Congress and not a change promulgated by a regulatory agency, the Small LECs assert the conclusions in Res. T-17616 constitute a failure to proceed in the manner required by law and are unsupported by the findings.⁸ The Small LECs also argue the adjustments were based on only one component of the companies' costs that have changed since their last GRCs and the Resolution fails to consider any other component that may have changed.⁹ We disagree.

Section 275.6(c) sets forth the Commission's obligations in establishing the CHCF-A program, which we implemented in D.91-09-042. Appendix A of that decision describe the CHCF-A rules, such as the annual Advice Letter process which allow the

⁷ AFR, p. 7.

⁸ *Id.*, citing Pub. Util. Code, § 1757(a)(2) and (3).

⁹ AFR, p. 12.

Small LECs to carry through funding in non-GRC years and request adjustments to address revenue impacts of “regulatory changes ordered by the Commission and the Federal Communications Commission (FCC).”¹⁰ The rules also specify instructions for the inclusion of certain information “*as well as all other regulatory changes of industry-wide effect.*”¹¹ Examples of such changes are also listed, and include changes in levels of interstate high cost funding, interstate Non-Traffic Sensitive (NTS) assignment, other FCC-ordered changes such as rate changes affecting access charges, intraLATA toll or Extended Area Service (EAS) settlements revenues, interLATA separations shifts and the effects of other Commission decisions which increase or decrease settlements revenues or cost assignments.¹²

The Small LECs assert because federal legislation is not an order by a regulatory agency, the rules do not permit the Commission to authorize reductions to revenue requirement or CHCF-A funding. The rehearing application notes that the examples cited in page 2 of the Appendix are “all regulatory changes ordered by the Commission or the FCC,” and that D.91-09-042 permits adjustments only for “known Commission regulatory decisions.”¹³ Based on the rehearing applicants’ interpretation of the rules, the six Small LECs affected by this Resolution should have been permitted to collect on a revenue requirement based on the higher corporate tax rate—at least until a new GRC or other formal proceeding adopts an adjusted revenue requirement that applies the new federal tax laws.

We find no merit to the Small LECs’ arguments. The Small LECs are incorrect that the Commission “must apply the [D.91-09-042] rules as they are written and may not arbitrarily and capriciously decide to make adjustments that are not

¹⁰ D.91-09-042, Appendix A, p. 2.

¹¹ *Id.* (Emphasis added.)

¹² *Id.* IntraLATA (also known as Local Toll Service) is calling within a geographic area known as a Local Access and Transport Area (LATA). EAS refers to a telephone service authorized in designated communities to extend the geographic reach of a local-toll free calling area.

¹³ AFR, p. 7.

authorized by the CHCF-A rules.”¹⁴ First, the rules in D.91-09-042 are not meant to limit the Commission’s actions to make adjustments to a Small LECs’ revenue requirement or CHCF-A support in Non Test-Years. As noted in the Resolution, D.91-09-042 does not preclude the Commission from considering the effects of income tax law changes on the utilities’ Test Year adopted revenue requirement and a corresponding CHCF-A subsidy amount.¹⁵ The Commission issued D.91-09-042 to implement the CHCF-A program and legislative mandates expressed in section 275.6. Thus, the Commission’s interpretation of the statute controls—not the CHCF-A rules themselves—in determining whether the adjustments in Res. T-17616 were proper.¹⁶ The Commission maintains flexibility to alter these rules subject to the constraints promulgated by statute and to also recognize changes such as the TCJA that impact the amount of money from the CHCF-A fund necessary to subsidize the Small LECs’ rates.

The Small LECs’ strict reading of the rules is incompatible with section 275.6. The statute directs the Commission to exercise its regulatory authority to provide CHCF-A support “in amounts sufficient to meet the revenue requirements established by the commission through rate-of-return regulation.”¹⁷ Nothing in the statute precludes the Commission from exercising its own regulatory authority to consider the new tax law impacts on the Small LECs’ Test Year adopted revenue requirement and corresponding CHCF-A subsidy amount needed to fulfill the revenue requirement. In fact, section 275.6(c) requires the Commission to ensure the rates charged by the Small LECs are “just and reasonable” and “in accordance with Sections 451, 454, 455, and 728.” Section 275.6(c) further obligates the Commission to ensure the corresponding CHCF-A support

¹⁴ AFR, p. 8.

¹⁵ Res. T-17616, p. 8.

¹⁶ “[T]he PUC’s ‘interpretation of the Public Utilities Code should not be disturbed unless it fails to bear a reasonable relation to statutory purposes and language.’” (*Pacific Bell Wireless, LLC v. Public Utilities Com.* (2006) 140 Cal.App.4th 718, 729.) When the issue is the scope of the PUC’s jurisdiction, however, “the general rule of deference to interpretations of statutes subject to the regulatory jurisdiction of agencies does not apply...” (*Ibid.*)

¹⁷ Pub. Util. Code § 275.6(a).

is “not excessive so that the burden on all contributors to the CHCF-A program is limited.”¹⁸ To this end, we adopted a “Means Test” in the CHCF-A rules: “It is reasonable to limit the CHCF funding amount to the current funding level amount for the year for which CHCF is being requested or to the amount which produces no more than the utilities authorized intrastate rate of return, *whichever is lower.*”¹⁹ D.91-09-042 explains, “Using annualized earnings based on at least seven months of recorded data for the year in which the CHCF advice letter is filed and adjusted for known regulatory

¹⁸ Pub. Util. Code § 275.6(c) states, in full:

In administering the CHCF-A program the commission shall do all of the following:

- (1) Continue to set rates to be charged by the small independent telephone corporations in accordance with Sections 451, 454, 455, and 728.
- (2) Employ rate-of-return regulation to determine a small independent telephone corporation’s revenue requirement in a manner that provides revenues and earnings sufficient to allow the telephone corporation to deliver safe, reliable, high-quality voice communication service and fulfill its obligations as a carrier of last resort in its service territory, and to afford the telephone corporation a fair opportunity to earn a reasonable return on its investments, attract capital for investment on reasonable terms, and ensure the financial integrity of the telephone corporation.
- (3) Ensure that rates charged to customers of small independent telephone corporations are just and reasonable and are reasonably comparable to rates charged to customers of urban telephone corporations.
- (4) Provide universal service rate support from the California High-Cost Fund-A Administrative Committee Fund to small independent telephone corporations in an amount sufficient to supply the portion of the revenue requirement that cannot reasonably be provided by the customers of each small independent telephone corporation after receipt of federal universal service rate support.
- (5) Promote customer access to advanced services and deployment of broadband-capable facilities in rural areas that is reasonably comparable to that in urban areas, consistent with national communications policy.
- (6) Include all reasonable investments necessary to provide for the delivery of high-quality voice communication services and the deployment of broadband-capable facilities in the rate base of small independent telephone corporations.
- (7) Ensure that support is not excessive so that the burden on all contributors to the CHCF-A program is limited.

¹⁹ D.91-09-042, Ordering Paragraph (OP) 1(d). (Emphasis added.)

decisions as the baseline for determining eligibility for CHCF support *would be relatively simple and non-controversial.*²⁰

In the case of Res. T-17616, we found it appropriate to utilize the advice letter process and the D.91-09-042 rules to recalculate the six Small LECs' authorized revenue requirement and CHCF-A support to implement the new corporate tax rates established by the TCJA. Ultimately, the Commission does not err in adopting Staff's calculations and consequent reductions in Res. T-17616 as such actions fall within the Commission's authority to establish funding limits as prescribed in section 275.6(c). Thus, the reductions approved by the Commission are lawful and consistent with its statutory obligation to ensure just and reasonable rates and that any corresponding CHCF-A support is not excessive.

Finally, we reject the Small LECs' argument that the Resolution fails to consider any other component of the companies' costs that have changed since the last GRC.²¹ As stated above, the CHCF-A annual advice letter process allows the Commission to make reasonable adjustments in years between GRCs on a limited basis where the change is relatively simple and non-controversial. The application of the Small LECs' corporate tax rate change from 34% to 21% to their revenue requirement is just that—simple and non-controversial—as income tax is an expense in the revenue requirement that uses prevailing tax rates. Accordingly, we reject the Small LECs' arguments that Res. T-17616 fails to proceed in a manner required by law.

Section 455 lends further support to the approach implemented in Res. T-17616 to realize the 2018 tax implications of the six Small LECs outside of their respective GRCs. That statute allows the Commission to adopt rules it considers reasonable and proper for each class of public utility, broadly including “the nature of the showing required to be made in support of proposed rate changes, the form and manner of the presentation of the showing, with or without a hearing, and the procedure to be

²⁰ *Id.* at OP 1(e). (Emphasis added.)

²¹ AFR, p. 12.

followed in the consideration thereof.”²² Our determination made in Res. T-17616 did not occur in a vacuum—the adjustments made to the six Small LECs revenue requirement and CHCF-A support was the result of a lengthy process that included “detailed explanations of the impact of the TCJA on the companies’ going-forward tax expectations” in response to the February 9, 2019 data requests sent by Communications Division staff.²³ Later, a March 16, 2019 letter issued by the Director of the Communications Division directed the Small LECs to establish memorandum accounts tracking the impacts of the TCJA and to submit an advice letter on or before March 30, 2018.²⁴ Finally, Staff followed the CHCF-A rules by applying the last general rate case adopted revenue and “Means Test” specified in D.91-09-042. This method serves to limit CHCF-A support to amounts which would provide no more than the utility’s authorized rate of return or current funding level, whichever is lower.²⁵

We also reject the Small LECs’ assertions that the conclusions in Res. T-17616 are unsupported by the Resolution’s findings.²⁶ Nothing in the Public Utilities Code specifically requires the Commission to make findings on all issues raised by the parties. Rather, it is within the Commission’s discretion to determine what factors are material to its decision based on the issues before it.²⁷ The Commission’s findings and

²² Pub. Util. Code § 455.

²³ AFR, p. 4.

²⁴ To address the changes made in the Tax Reform of 1986, the Commission opened a rulemaking to make changes of broad applicability across the industries it regulates. D.88-01-061 authorized adjustments to the revenue requirements and rates in response to the new tax laws but exempted the Independent Small LECs from the filing requirements ordered in the decision, with the tax law impacts to be addressed in the next general rate case, or, General Order 96 filing as appropriate. (D.88-01-061, p. 38.) The Commission clarified, “Any utility exempted from our filing requirement for 1987 effects would not be precluded from making a filing if they believe an adjustment is warranted.” (Id. at 39.) Nevertheless, the decisions the Commission adopted at the time is not determinative in how the Commission in 2018 should have carried out the TCJA tax law changes.

²⁵ D.91-09-042, OP 1(d), OP 1(g), and OP 1(j).

²⁶ AFR, pp. 2, 6-7, 17.

²⁷ *Clean Energy Fuels Corp. v. Pub. Utilities Com.* (2014) 227 Cal. App. 4th 641, 659.

conclusions are sufficient if they provide “a statement which will allow us a meaningful opportunity to ascertain the principles and facts relied upon by the [PUC] in reaching its decision.”²⁸ In other words, “a complete summary of all proceedings and evidence leading to the decision” is not required.”²⁹

We modify Res. T-17616 to provide clarity and to resolve any ambiguity in the CHCF-A rules:

- **The fourth full paragraph on page 8 should be replaced by the following:**

“Fourth, it is not necessary for the Commission to examine the whole financial information of a company to determine the changes in the adopted revenue requirement and the corresponding CHCF-A subsidy resulting from the income tax rate change. The methodology Staff used to determine the reductions is reasonable and based on the last GRC Test Year adopted revenue and the “Means Test” as specified by the CHCF-A rules in D.91-09-042. Also, since the rates are based on the last general rate case adopted revenue, it is appropriate to consider that adopted revenue and adjust any component that has changed, provided such adjustment is relatively simple and non-controversial.”

- **Adopt additional Findings, as provided below:**

19. Pub. Util. Code § 275.6(c) sets forth the Commission’s obligations in establishing the CHCF-A program, which the Commission implemented in D.91-09-042.
20. Pub. Util. Code § 275.6 and D.91-09-042 do not limit the Commission from making certain adjustments using its rate-of-return regulatory authority to reflect legislative changes to the corporate tax rate.
21. The adjustments to the revenue requirement and CHCF-A support for Ducor, Foresthill, Kerman, Pinnacles, Siskiyou, and Volcano for April 2018 through December 2018 are reasonable and consistent with the Commission’s obligations under Pub. Util. Code § 275.6(c) to ensure the rates charged are “just and reasonable” and the corresponding CHCF-A support is “not excessive.”

²⁸ *Id.*, quoting *TURN v. CPUC* (1978) 22 Cal.3d 529, 540.

²⁹ *Id.*

B. With these modifications, there is no need to address Small LECs' remaining arguments asserting legal error.

The Small LECs assert additional legal arguments, including that the Resolution engages in unlawful piecemeal ratemaking based on “arbitrary and capricious” reasoning; an abuse of discretion per section 1757(a)(5); violates due process rights without hearing or notice and opportunity to be heard; and constitutes an illegal taking of property without just compensation.³⁰

These arguments rely on the threshold issue of whether the Commission's actions to reduce the six Small LECs revenue requirement and corresponding CHCF-A support in Res. T-17616 were lawful. We have concluded the reductions authorized in Res. T-17616 substantively conform with the legislative directives of sections 275.6 and 455, the rules in D.91-09-042, and subsequent decisions. Our analysis also provides clarification of the CHCF-A rules regarding the Commission's ability to make certain Non Test-Year adjustments. As Res. T-17616 is lawful and grounded on the Commission's authority under section 275.6, there is no need to address the additional arguments raised here.

II. THE COMMISSION SHOULD REMOVE ANY DISCUSSION REGARDING THE NORMALIZATION METHOD OF DEFERRED TAX IN THE UPCOMING GRC

The Small LECs argue the discussion in Res. T-7616 regarding the treatment of excess deferred taxes using the normalization method in future rate cases constitutes an unlawful predetermination of the outcome of those rate cases, which is unsupported by substantial record evidence.³¹ The rehearing application states, “Normalization of deferred tax amounts is not required by any general rate case decisions of the Independent Small LECs, the CHCF-A rules, or any industry-wide Commission decision.”

³⁰ AFR, p. 2.

³¹ AFR, p. 16.

The Small LECs raise a valid argument. We agree that prescribing a specific method of addressing that ratemaking issue at this time is beyond the scope of the Resolution and improper given the insufficient record addressing the issue. Thus, we will strike the language referenced in Res. T-17616 concerning how to treat excess deferred tax impacts in future rate cases as shown below in our modification of Finding No. 10.

III. CONCLUSION

For the reasons stated above, we determined that good cause exists to modify Resolution T-17616 and deny rehearing.

THEREFORE, IT IS ORDERED that:

1. Resolution T-17616 shall be modified as follows:
2. Modify the first full paragraph on page 5, as shown by the redline changes

below:

~~“While Staff has calculated the tax expense impact of the TCJA for operating expenses, it is not reflecting the additional savings impact of the TCJA on the deferred income tax reserve (which is a rate base component). due to the problematic nature of determining and applying the remaining life of depreciable assets prior to CY 2018 for normalization (disposal) of excess deferred income tax, created as a result of the new lower income tax rate. Staff recommends that such consideration be deferred until each company’s next GRC proceeding, at which time an equitable amount of the excess deferred tax and a reasonable method for their normalization (disposal) can be determined.”~~

3. Strike the language on page 7, at the end of the third full paragraph under “Comments,” as follows:

~~“Therefore, we will defer this issue until each company’s next GRC proceeding, at which time an equitable amount of excess deferred tax and a reasonable method for their normalization (disposal) can be determined.”~~

4. Replace the fourth full paragraph on page 8, as follows:

“Fourth, it is not necessary for the Commission to examine the whole financial information of a company to determine the changes in the adopted revenue requirement and the corresponding CHCF-A

subsidy resulting from the income tax rate change. The methodology Staff used to determine the reductions is reasonable and based on the last GRC Test Year adopted revenue and the “Means Test” as specified by the CHCF-A rules in D.91-09-042. Also, since the rates are based on the last general rate case adopted revenue, it is appropriate to consider that adopted revenue and adjust any component that has changed subject to the Commission’s authority in section 275.6, and provided such adjustment is relatively simple and non-controversial.”

5. Modify No. 10 of the Findings, on page 9, as follows:
 - “10. Staff recommends that consideration of the additional savings impact of the TCJA on the deferred income tax reserve be deferred until each company’s next GRC proceeding, ~~at which time an equitable amount of excess deferred tax and a reasonable method for their normalization (disposal) can be determined.~~”
6. Insert the following additional findings, including:
 - “19. Pub. Util. Code § 275.6(c) sets forth the Commission’s obligations in establishing the CHCF-A program, which the Commission implemented in D.91-09-042.
 20. Pub. Util. Code § 275.6 and D.91-09-042 do not limit the Commission from making certain adjustments using its rate-of-return regulatory authority to reflect legislative changes to the corporate tax rate.
 21. The adjustments to the revenue requirement and CHCF-A support for Ducor, Foresthill, Kerman, Pinnacles, Siskiyou, and Volcano for April 2018 through December 2018 are reasonable and consistent with the Commission’s obligations under Pub. Util. Code § 275.6(c) to ensure the rates charged are “just and reasonable” and the corresponding CHCF-A support is “not excessive.””
7. The application for rehearing is denied.

8. This proceeding is closed.
This order is effective today.

Dated May 6, 2021 at San Francisco, California.

MARYBEL BATJER
President
MARTHA GUZMAN ACEVES
CLIFFORD RECHTSCHAFFEN
GENEVIEVE SHIROMA
DARCIE L. HOUCK
Commissioners