

**PROJECT NO. 47669**

<b>RULEMAKING TO ADD 16 TEX.</b>	<b>§</b>	<b>PUBLIC UTILITY COMMISSION</b>
<b>ADMIN. CODE 26.407 SMALL AND</b>	<b>§</b>	
<b>RURAL INCUMBENT LOCAL</b>	<b>§</b>	<b>OF TEXAS</b>
<b>EXCHANGE COMPANY UNIVERSAL</b>	<b>§</b>	
<b>SERVICE PLAN (SRILEC USP)</b>	<b>§</b>	
<b>SUPPORT ADJUSTMENTS</b>	<b>§</b>	
<b>PURSUANT TO S.B. 586</b>	<b>§</b>	

**ORDER ADOPTING NEW §26.407  
AS APPROVED AT THE OCTOBER 12, 2018 OPEN MEETING**

The Public Utility Commission of Texas (commission) adopts new §26.407, relating to Small and Rural Incumbent Local Exchange Company Universal Service Plan Support Adjustments with changes to the proposed text as published in the June 8, 2018 issue of the *Texas Register* (43 TexReg 3714). The addition of §26.407 reflects the development and implementation of a mechanism to determine the annualized Small and Rural Incumbent Local Exchange Company Universal Service Plan support for certain small incumbent local exchange companies (small ILECs). The proposed rule establishes criteria by which a small ILEC may request that the commission determine the amount of Small and Rural Incumbent Local Exchange Company Universal Service Plan support it receives, so that the support, combined with regulated revenues provides the small ILEC an opportunity to earn a reasonable rate of return under this rule, as required by Senate Bill 586, 85th Legislative Session (Regular Session). This new section is adopted under Project Number 47669.

The commission received comments on the proposed amendments and new section from the Texas Cable Association (TCA); Office of Public Utility Counsel (OPUC); and Texas Statewide Telephone Cooperative, Inc. and Texas Telephone Association (collectively TSTCI and TTA).

No party requested that a public hearing be held regarding the proposed rule.

### *General Comments*

TSTCI and TTA provided comments in response to the Chairman's request to create an alternative abbreviation or title in this section for the term Small and Rural Incumbent Local Exchange Carrier Universal Service Plan. TSTCI and TTA suggested that the commission use the title small ILEC plan (SIP) to describe the Small and Rural Incumbent Local Exchange Company Universal Service Plan.

### *Commission Response*

**The commission declines to adopt TSTCI and TTA's suggested change. The commission has determined that the entire term should be used when referring to the Small and Rural Incumbent Local Exchange Carrier Universal Service Plan, instead of using an acronym.**

### *§26.407(a) - Purpose*

TSTCI and TTA recommended that this subsection be revised to include a reference to show that the ILEC or staff may request an adjustment to support.

### *Commission Response*

**The commission declines to adopt TSTCI and TTA's suggested change to this subsection. The commission notes that the purpose of the section is to establish criteria for a small ILEC**

to request adjustments to the monthly support the company receives. Any adjustments to a small ILEC's reported rate of return that may be made by commission staff are a result of the review of information in the small ILEC's annual report. Similar to other types of applications, commission staff will review the information provided from the applicant and make any adjustments it deems necessary.

*§26.407(d) - Notification to the Commission That a Small ILEC Seeks to Participate in This Section*

TSTCI and TTA suggested that the language "is not an electing company under Chapter 58 or 59" be deleted, because the language is also in the statute.

*Commission Response*

The commission declines to adopt TSTCI and TTA's suggested change. The commission finds that the language "is not an electing company under Chapter 58 or 59" provides clarification to the type of ILEC that may seek an adjustment to its support under this section. Furthermore, the commission does not find TSTCI and TTA's argument that the language is already in the statute to be persuasive. Much of the language used in this section is in the statute, but is also used in the rule to provide additional guidance and clarity.

*§26.407(e) - Comments Regarding the Annual Report of a Requesting Small ILEC*

OPUC stated that prior to the commission making a determination of whether an ILEC's universal service support or basic rates should be increased, it must first make an analysis of an ILEC's

regulated revenues. OPUC explained that in order for the commission to perform such an analysis, it needs to have sufficient information regarding revenues, expenses, affiliate transactions, and cost allocations to determine whether the reported rate of return should be adjusted. OPUC commented that it supports the inclusion of the items listed in subsection (e)(2). OPUC further explained that it believes the commission appropriately identified the kind of financial and other information that it needs to make a reasonable determination of whether the ILEC's reported rate of return falls below, within, or above the reasonable rate of return identified in subsection (c)(3). OPUC added that because the commission has the discretion to increase not only universal service support for ILECs whose rate of return falls below the reasonable rate of return but also basic rates, it is critical that the annual report include sufficient information.

In reply comments, TCA stated it concurred with OPUC that the published rule appropriately identifies the information the commission will need in order to make a determination of whether the ILEC's reported rate of return falls below, within, or above the reasonable rate of return identified in subsection (c)(3).

TSTCI and TTA submitted a number of comments on different paragraphs regarding subsection (e). TSTCI and TTA's comments have been summarized below by the applicable paragraph.

**Subsection (e)(1)** - TSTCI and TTA stated that subsection (e)(1) should allow an annual report to be filed within two months after a small ILEC elects to participate in this section, rather than requiring an annual report to be filed within two months after the effective date of this section. TSTCI and TTA explained that the language in the proposal for publication only allows for a one-

time filing deadline that would exclude any small ILEC from filing at a later date. TSTCI and TTA also recommended that the annual reports should be filed in September of each year instead of May. TSTCI and TTA explained that moving the date from May to September would allow the small ILECs to use the current year's cost study jurisdictional percentages rather than the prior year's cost study information. Cost study jurisdictional percentages are developed and reported to the National Exchange Carrier Association by July of each year for the prior year's cost study information. TSTCI and TTA argued that by moving the due date of the report to September, this would ensure the proper matching of cost study separations and financial results of operations.

*Commission Response*

**The commission agrees with TSTCI and TTA that the language in subsection (e)(1) should be changed to allow an annual report to be filed within two months after a small ILEC elects to participate in this section rather than requiring an annual report to be filed within two months after the effective date of this section. The commission also agrees with TSTCI and TTA that the annual reports should be due in September rather than May to ensure the proper matching of cost study separations and financial results of operations. The commission has made the necessary revisions to the proposed rule language and form instructions to incorporate these changes.**

**Subsection (e)(2)(B)** - TSTCI and TTA suggested that it was not clear in subsection (e)(2)(B) whether the commission was asking for more detail than what was being requested in the proposed form. TSTCI and TTA stated that because subsection (e)(2)(K) already requests detail and

supporting documentation, it would be preferable to reference “summary” data in subsection (e)(2)(B).

*Commission Response*

**The commission declines to adopt TSTCI and TTA’s recommendation that subsection (e)(2)(B) be described as “summary” data, as the information in subsection (e)(2)(A) is already characterized as such. Subsection (e)(2)(B) requests details for all revenue, expense, and capital accounts, including all subaccounts and balances, that make up the accounts on the annual report. The detail and supporting documentation required in subsection (e)(2)(K) is a listing of each transaction, affected party, and monetary amount for the information identified in subsection (e)(2).**

**Subsection (e)(2)(C)** - TSTCI and TTA recommended that “long-term” be inserted before “telephone plant under construction” in the Instructions for Schedule II (Invested Capital). TSTCI and TTA claim that this clarification aligns with the annual report and the Federal Communications Commission (FCC) rules.

*Commission Response*

**The commission agrees with TSTCI and TTA’s suggested revision that “long-term” be inserted before “telephone plant under construction” in Schedule II of the Instructions.**

**Subsection (e)(2)(I)** - TSTCI and TTA argued that there is a reference to “other highly compensated employees” in subsection (e)(2)(I), but “highly compensated employee” is not

defined. TSTCI and TTA believe that a definition of “highly compensated employee” should be provided in Attachment B in the instructions for Schedule VIII. TSTCI and TTA recommended that the commission use the Internal Revenue Service guidelines related to 401(k) reporting, which establishes the threshold of a “highly compensated employee” at \$120,000. Additionally, TSTCI and TTA argued that any compensation that was reported in Schedule VIII of the annual report should not be included on Schedule IX to avoid double-counting.

*Commission Response*

**The commission declines to adopt a specific definition of “highly compensated employee.” Instead, it will review the issue on a case-by-case basis to determine what is considered “highly compensated.” Because of the different sizes of the companies that may seek an adjustment to support from the Small and Rural Incumbent Local Exchange Company Universal Service Plan, it is reasonable to determine the amount attributable to “highly compensated” employees for each company. For example, a company with 100 access lines may not have any employee that meets the Internal Revenue Service definition of “highly compensated;” however, the annual salary for the highest paid employees should be reviewed, whereas a company with 5,000 access lines may have numerous employees that meet the Internal Revenue Service definition of “highly compensated.”**

**Subsection (e)(2)(J)** - TSTCI and TTA suggested a change in Schedule IX (Report of Utility Affiliate Transactions) of the instructions to clarify that the amount allocated to the intrastate regulated operations of the small ILEC should be reported for such transactions.

*Commission Response*

**The commission declines to adopt TSTCI and TTA's proposed changes to Schedule IX (Report of Utility Affiliate Transactions) of the annual report instructions that would state the amount allocated to the intrastate regulated operations of the small ILEC should be reported for such affiliate transactions. The commission should be provided the total amount of each affiliate transaction and then the breakdown between intrastate and interstate. The commission will use the cost allocation manual submitted by the ILEC to determine whether the allocation complies with FCC statutes and rules and is reasonable.**

**Subsection (e)(3)** - TSTCI and TTA stated that the cost allocation manual only needs to be provided in the first year and companies will only need to provide updates or changes to the manual in subsequent years. TSTCI and TTA stated that a cost allocation manual gives instructions and formulas for how the separations processes and allocations are to be calculated for each company, and that, to their understanding, the manual is provided once. TSTCI and TTA suggested that the companies will provide only updates or changes to the manual in subsequent years.

*Commission Response*

**The commission declines to adopt TSTCI and TTA's recommendation that the cost allocation manual only be provided in the first year and that updates or changes to the cost allocation manual be provided in subsequent years. A complete copy of the cost allocation manual should be submitted each time it is filed in order to facilitate staff's internal review. Additionally, due to record retention rules, the commission may not always have access to the original cost allocation manual.**

**Subsection (e)(4)** - TSTCI and TTA stated that a new subsection (e)(4) should be added to allow a small ILEC the opportunity to defer filing an annual report during the pendency of a comprehensive base-rate proceeding. TSTCI and TTA concede that comprehensive base-rate proceedings are not imminent, but admit that this language is suggested just as a possibility in the future. TSTCI and TTA also stated that a corresponding addition would be required in the instructions to the annual report.

*Commission Response*

**The commission declines to adopt TSTCI and TTA's recommendation that that a new subsection (e)(4) should be added to allow a small ILEC the opportunity to defer filing an annual report during the pendency of any comprehensive base-rate proceeding. The commission notes that there currently are no base-rate proceedings, and there has not been a comprehensive base-rate case in many years. TSTCI and TTA conceded that a base-rate proceeding is not imminent, but admitted that this language is suggested just as a possibility in the future.**

*§26.407(f) - Commission Staff's Review of Annual Reports*

**Subsection (f)(1)** - TSTCI and TTA commented that subsection (f)(1)(A) and (B) should have language allowing for reasonable extensions by either the small ILEC or the commission staff. TSTCI and TTA argued that even with an agreed-upon delay, it would result in the automatic placement of an ILEC in Category 3. TSTCI and TTA also requested that the rule be changed, so

that the rule would not require the automatic placement of a Category 1 provider into Category 3 for a lack of response to commission staff's requests for information. TSTCI and TTA proffered an alternative to placing a non-responsive ILEC to Category 3. They proposed that an administrative penalty be assessed against the ILEC in lieu of re-categorization to Category 3 for not responding within ten days to the commission staff's request for information.

TCA stated that it opposes TSTCI and TTA's request for extensions of deadlines to the requirements of subsection (f). TCA asserted that TSTCI and TTA's proposal would cause uncertainty for the public and create an unfair opportunity for the small ILEC to delay a test year period to a time that included untimely expenses or a reduction in revenues that would ultimately result in higher universal service fund contributions by all Texans.

### *Commission Response*

**The commission declines to adopt TSTCI and TTA's recommendation that language be added to subsection (f)(1)(A) and (B) that would allow for reasonable extensions by either the small ILEC or the commission. An ILEC's failure to respond to the commission staff's request for information or an ILEC's request for additional time to respond to the commission staff's request for information should be the exception, not the rule. To provide language in the rule that would automatically allow additional time to respond to a request for information may encourage the practice of delaying responses to request for information to become the norm rather than the exception. Subsection (h)(2)(B) provides a mechanism to request re-categorization by an ILEC that has a reported rate of return in Category 1 but**

**is reclassified as a Category 3 by commission staff for failure to timely provide information to commission staff.**

**Subsection (f)(2)** - TSTCI and TTA commented that the commission should include language in subsection (f)(2)(A)(ii) requiring any other adjustments the commission makes be tied to existing commission rules. TCA commented that TSTCI and TTA's request for any other adjustments the commission may make be tied to existing commission rules should be rejected. TCA argued that the commission's recommendations are always governed by the public interest and by applicable laws, so it does not need to be explicitly stated in the rule.

***Commission Response***

**The commission declines to adopt TSTCI and TTA's request to include language stating that any other adjustments the commission staff may make be tied to existing commission rules. The commission staff is required to act according to the law and in a prudent manner as a representative of the public interest; therefore, any adjustments it makes would be in the public interest and would not be in violation of any statutes or commission rules.**

***§26.407(g)(1) and (j)(1)(A) - Comments Regarding Treatment of Small ILECs Based on Rate of Return Categories***

OPUC stated that the published rule failed to include the language from the statute that states "[a] rate adjustment under this subsection may not adversely affect universal service." OPUC recommended that this language be added to subsection (g)(1) and subsection (j)(1)(A). In support of its position, OPUC explained that there are times when rates can be increased without adversely

affecting universal service; however, under other circumstances, raising rates in lieu of or in addition to providing additional universal service fund support could adversely affect universal service if the existing rates were above FCC benchmarks or at or above comparable urban rates.

### *Commission Response*

**The commission adopts the language proposed by OPUC for subsection (g)(1) and subsection (j)(1)(A) to memorialize the intent of the statute that any proposed rate adjustments under this section do not adversely affect universal service.**

### *§26.407(h) - Contested Case Procedures*

**Subsection (h)(1)** - OPUC stated that in a contested case, intervenors need access to the underlying information to be able to analyze and determine whether the regulated revenues of the small ILEC are sufficient or whether an increase to universal service support or existing rates is reasonable. OPUC supports the requirements outlined in subsection (h) that require a small ILEC to provide not only testimony and workpapers necessary to support the requested adjustments, but also the underlying information that was provided to the commission staff during the review of the annual report. While OPUC agreed with and supported the requirements in subsection (h), it would like the commission to clarify the intent of subsection (h)(1) by stating in the preamble that any

Category 1 proceeding in which a party has intervened and requested a hearing is a case initiated by a small ILEC and the filing requirements included in subsection (h)(1) apply.

In reply comments, TCA agreed with OPUC's comments that subsection (h)(1) applies to a case initiated by a small ILEC and includes both cases eligible for administrative disposition as well as a fully contested case in which parties have intervened and requested a hearing. TCA stated that in both types of cases, the information in subsection (h)(1) should be included in the filing and publicly available for review. TCA also commented that the commission should either adopt OPUC's suggestion that clarification be included in the preamble or by modifying the rule language to explicitly clarify that the treatment of Category 1 proceedings in which a party has intervened and requested a hearing is a case initiated by a small ILEC and that the requirements in subsection (h)(1) apply.

### *Commission Response*

**The commission agrees with OPUC and TCA that subsection (h)(1) should be clarified to state that any Category 1 proceeding in which a party has intervened and requested a hearing is a case initiated by a small ILEC and the filing requirements included in subsection (h)(1) apply. The commission also agrees with OPUC and TCA that subsection (h)(2)(B) should be clarified to indicate that a proceeding initiated by a small ILEC to protest a reclassification and in which a party has intervened and requested a hearing is a case initiated by a small ILEC and the filing requirements included in subsection (h)(1) apply. The commission has made the necessary revisions to the proposed rule language to incorporate these changes.**

**Subsection (h)(2)** - TSTCI and TTA commented that subsection (h)(2)(B) should apply only to small ILECs that reported a rate of return in Category 1, rather than those in Category 1 or Category 2. TSTCI and TTA argued that small ILECs that report a rate of return in Category 2, but who are reclassified as Category 3 because of adjustments made by commission staff, should not have to petition to contest the commission-staff adjusted rate of return and make a support adjustment request. Instead, such small ILECs could petition to contest the commission staff adjustment without requesting a support adjustment, because Category 2 small ILECs are not eligible for a support adjustment.

*Commission Response*

**The commission declines to adopt TSTCI and TTA’s proposal that Category 2 be deleted from subsection (h)(2)(B). Commission staff will review all of the small ILECs annual reports when they are filed and make any adjustments it determines are necessary. Once the commission staff has completed its review, each small ILEC will be placed in either Category 1, Category 2, or Category 3. If a small ILEC’s rate of return on the annual report indicated it was a Category 2, but commission staff made adjustments that caused that small ILEC to fall into Category 1 or Category 3, then the small ILEC has the opportunity in subsection (h)(2)(B) to contest that reclassification.**

**Subsection (h)(5)** - TSTCI and TTA also commented subsection (h)(5) should use the same language to describe “good cause” that is used in the statute. They further commented that a sentence should be added to subsection (h)(5) to clarify that any contested cases initiated solely to

contest commission staff's expense adjustments without adjusting the small ILEC's support should not trigger the three-year waiting period during which no further contested case can be initiated. TSTCI and TTA argued the statutory intent was to avoid adjusting support more frequently than every three years absent good cause.

In reply comments, TCA recommended rejection of TSTCI and TTA's suggestion that subsection (h)(5) be modified to shorten the three-year prohibition from filing a contested case.

In initial comments, OPUC addresses the timeline of a contested case by stating that, to its understanding, once a request for a hearing has been made under this subsection, the case proceeds as any other contested case.

In reply comments, TSTCI and TTA addressed OPUC's comments regarding contested case procedures and asserted that a contested case should be abbreviated and streamlined as compared to a typical rate case. In support of such a position, TSTCI and TTA stated that a time limit, such as 60 days subject to extensions for good cause, might be imposed upon contested cases to avoid such proceedings approaching the involvement, time, and cost incurred with comprehensive rate cases. TSTCI and TTA argued that a 60-day timeframe is consistent with other commission rules for review of certain certification proceedings and streamlined rate adjustments before the commission. In support of its position, TSTCI and TTA provided language for a new subsection (h)(5).

*Commission Response*

**The commission agrees with TSTCI and TTA that the contested case procedures, including the timeline for the contested cases outlined in this section, should be more abbreviated and streamlined as compared to a typical rate case. However, the commission recognizes that the timeline of 60 days as proposed by TSTCI and TTA is not conducive to a contested case. In order to allow time for parties to conduct discovery and to be cognizant of resources of commission staff and the State Office of Administrative Hearings, the commission finds that a 120 day timeline is more realistic. The commission has inserted language as new subsection (h)(5) to implement the timeline.**

*§26.407(i) - Confidentiality of Information*

OPUC supported the recommended treatment of the confidentiality of information in the proposed rule. OPUC stated that the annual review process is not intended to be an open, public process, but that, if the small ILEC initiates a contested case proceeding, the small ILEC cannot rely on a presumption of confidentiality on the underlying data. However, if the small ILEC chooses to dispute commission staff's assessment in a contested case, it is permitted to support a claim of confidentiality in and of itself, and not merely on the fact that it was submitted to commission staff for review under the annual review process. OPUC stated that requiring all "revenues and expenses, invested capital, taxes, weighted average cost of capital, affiliate transactions, and cost allocations" be treated as confidential would go against commission precedent and be unworkable in the context of a contested case proceeding.

TSTCI and TTA disagreed with the treatment of confidential information in the proposed rule in two respects. First, TSTCI and TTA construed PURA § 56.032(d) to require that any “information” by any part of the rule, including both annual reports and contested cases, should be confidential. As a result, they asked for commission staff to strike the language referring to subsection (e) in subsection (i)(1) of the proposed rule.

Additionally, TSTCI and TTA argued that the language stating that “no claim of confidentiality shall arise from this subsection in such a subsequent contested case” in subsection (i)(3) conflicts with the language in subsection (i)(2) and the statutory language, because of their view that all information provided in compliance with the rule should be confidential. Moreover, they asserted that the meaning of “subsequent contested case” is unclear. TSTCI and TTA cited two Texas Attorney General letter-rulings as justification for this view, because those rulings exempt earnings monitoring reports from disclosure.

In reply comments, TCA stated that it agrees with OPUC’s comments regarding the rule’s treatment of the confidentiality of information and disagreed with TSTCI and TTA’s comments, stating that TSTCI and TTA’s comments expand upon the statutory language. TCA stated that the documents TSTCI and TTA reference from the Texas Attorney General in their initial comments only speak to annual reports and responses to commission staff questions, not subsequent contested cases. TCA argued that, once a contested case arises, then the requirements of the Administrative Procedures Act must apply, including the provisions that relate to confidentiality of information.

*Commission Response*

The commission declines to adopt the changes proposed by TSTCI and TTA. The proposed edits would expand upon the statutory language, because “information” in PURA § 56.032(k) only refers to the mechanism used by the commission to determine the annualized support amount, as described in PURA § 56.032(d), not discovery in a subsequent contested case where a small ILEC chooses to dispute the annualized support amount that was determined by the commission. Additionally, the logistics of conducting a contested case where all of the information is considered confidential would render it unwieldy and potentially unworkable. Finally, the two Open Records Letter Decisions cited by TSTCI and TTA are not binding precedent, and do not address whether the information described in subsection (i)(3) may be disclosed in the process of a contested case proceeding.

*§26.407(j) - Commission Adjustment of the Small ILEC’s Revenue Requirement and Small and Rural Incumbent Local Exchange Company Universal Service Plan Support*

TSTCI and TTA stated that subsection (j)(1)(B) should be clarified to reflect commission staff’s intent that in most cases, support would be adjusted by the minimum amount needed either to bring a Category 1 small ILEC up to the bottom of the reasonable rate-of-return range or to bring a Category 3 small ILEC down to the top of the reasonable rate-of-return range. TSTCI and TTA commented that more than minimum adjustments might be requested in some situations, although small ILECs making such requests would be aware that additional support would be needed.

TTA and TSTCI also stated that subsection (j)(3) should be clarified to refer to the previous December's eligible line counts to calculate competitive eligible telecommunications provider (ETP) support, rather than referring more generally to December line counts.

*Commission Response*

The commission declines to adopt the changes proposed by TSTCI and TTA. The commission finds that the language proposed by TSTCI and TTA does not provide additional clarity rather the language that “a small ILEC that is in Category 1 *should* request an increase in SIP support that would result in a rate of return *equal* to the minimum of the reasonable rate of return” is not accurate. A Category 1 small ILEC is not required to request an increase in Small and Rural Incumbent Local Exchange Company Universal Service Plan support that would result in a rate of return equal to the minimum of the reasonable rate of return, but rather it is optional as to the level of increase in Small and Rural Incumbent Local Exchange Company Universal Service Plan support the small ILEC requests as long as it is not greater than the minimum of the reasonable rate of return. Additionally, clarification regarding which December's line counts will be used for the calculation is unnecessary, because the determination will be used for the December during the test year, not referring more generally to December line counts.

*§26.407 (k) - Recovery of Federal Universal Service Fund support from the Texas Universal Service Fund in accordance with PURA §56.025*

**Subsection (k)(1)** - TSTCI and TTA proposed that both Part 36 and Part 54 of the FCC's rules be referenced in subsection (k)(1) and (2), because this would more accurately include the applicable

FCC rules. This change would also be made in the general instructions #7 and in the General Questions tab, under question #13.

TSTCI and TTA proposed language to clarify subsection (k)(1) regarding the “timing of any FUSF support will be considered when making a determination under subsection (j) of this section.”

TSTCI and TTA suggested that subsection (k)(1) should also address federal universal service fund true-ups as well, similar to paragraph (2).

TSTCI and TTA also recommended that the instructions regarding Schedule I should clarify that any federal universal service fund loss recovery under PURA §56.025 should be entered as part of federal universal service fund support as a contra amount in Schedule I, line 22, column “g”. This change would clarify that any Texas universal service fund support received under PURA §56.025 would replace lost high cost loop funds and must be included on this line and not included as other federal support.

### *Commission Response*

**The commission agrees with TSTCI and TTA that both Part 36 and Part 54 of the FCC’s rules be referenced in subsection (k)(1) and (2), because this would more accurately include the applicable FCC rules. The commission has made the necessary revisions to the proposed rule language to incorporate these changes.**

The commission declines to adopt TSTCI and TTA's proposed language to clarify subsection (k)(1) that the timing of any federal universal service fund support would be considered when making a determination under subsection (j) of this section. This language was included in subsection (k)(2) only to address the concern that small ILECs had regarding the time frame when a small ILEC decided to file an application to recover a particular year's loss in federal universal service fund support from the Texas universal service fund and how the recovery support should be booked for that period.

The commission agrees in part and declines in part to adopt TSTCI and TTA's proposed change to the instructions regarding Schedule I. The commission agrees that language should be included in the instructions to clarify that any federal universal service fund loss recovered under PURA §56.025 should be entered as part of federal universal service fund support as a contra amount in Schedule I, line 22, column "g." The language should also state that any Texas universal service fund support received under PURA §56.025 that replaces lost high cost loop funds must be included on this line. The commission disagrees with TSTCI and TTA that other loss in federal support that is being recovered from the Texas universal service fund should not be included on this line. Any type of federal support that is being recovered from the Texas universal service fund and has intrastate support should be included on this line. The commission has made the necessary revisions to the proposed rule language to incorporate these changes.

**Subsection (k)(2)** - TCA asserted that the proposed rule has an error at subsection (k)(2) where it states the items included in a small ILEC's revenues. TCA explained the error that occurred relates

to the FCC's accounting treatment of federal universal service fund dollars received by the small ILECs under PURA §56.025(c). TCA explained that this section of PURA is commonly referred to as the "make-whole" provision. Under this provision of PURA, the Texas universal service fund must replace an ILEC's loss in revenue caused by any FCC order that changes the ILEC's federal universal service fund subsidy revenues. TCA claimed that under the terms of subsection (k) of the proposed rule, the commission is ignoring the fact that the small ILECs are already being made-whole by the Texas universal service fund under PURA §56.025 and are therefore, being allowed to double recover from the Texas universal service fund. TCA stated that the small ILEC first recovers their lost federal universal service fund 100% from the Texas universal service fund in their make-whole proceeding and then second, the small ILEC recovers under this rule. TCA argued that the federal universal service fund jurisdiction allocation is irrelevant to the make-whole funding because 100% of the PURA §56.025(c) money comes from the Texas universal service fund. TCA further asserted that if any of the PURA §56.025(c) money is allocated to interstate revenues, then the small ILEC would receive a windfall because they would be receiving both the Texas universal service fund make-whole subsidy and not having to report it as Texas revenues, which may ultimately result in the small ILEC being entitled to higher subsidies from the Texas universal service fund. TCA recommended deleting the language in subsection (k)(2) that says "...that is considered an intrastate expense adjustment under Part 36 of the FCC rules or by FCC order, regardless of the category of FUSF support or type of budget control mechanism placed on FUSF support..."

In its reply comments, TSTCI and TTA recommended that the commission not adopt TCA's suggestions regarding PURA §56.025. TSTCI and TTA stated that the proposed rule accurately

accounts for intrastate and interstate support received under PURA §56.025. TSTCI and TTA claimed that the assertions presented by TCA are inaccurate and that the proposed rule accurately allocates the PURA §56.025(c) support in compliance with the matching principle of generally accepted accounting principles. TSTCI and TTA further explained that PURA §56.025(c) allows the replacement of a reduction in federal universal service fund revenue and PURA §56.025(b) allows the replacement of intrastate support. Because there is a distinction between the federal and state replacement mechanisms, then there should remain a separation in the rule as well.

TSTCI and TTA contended that it is not the source of revenues or expenses that is important but rather making sure that all revenues and expenses are correctly booked, allocated, and accounted for properly. They stated that if the revenues or expenses are not accounted for properly, then a mismatch would occur by including interstate support revenues as intrastate revenues. With TCA's proposal, small ILECs would have to report interstate revenues in its annual report, but would not be allowed to include interstate costs as part of the intrastate cost of service in the same report.

TSTCI and TTA recommended that "budget control mechanism" in subsection (k)(2) be changed to avoid confusion with the specific "budget control" line item.

### *Commission Response*

**The commission declines to adopt TCA's proposed changes to categorize all of the loss of federal universal service fund support that is recovered from the Texas universal service fund as intrastate revenue. The commission disagrees with TCA's claim that under the terms**

of subsection (k) of the proposed rule the commission is ignoring the fact that the small ILECs are already being made whole by the Texas universal service fund under PURA §56.025 and are therefore, being allowed to double recover from the Texas universal service fund. The commission agrees with TSTCI and TTA that the proposed rule accurately accounts for intrastate and interstate support received under PURA §56.025 and is in compliance with the matching principle of Generally Accepted Accounting Principles (GAAP).

The commission declines to adopt TSTCI and TTA's suggestion that "budget control mechanism" in subsection (k)(2) be changed to avoid confusion with the specific "budget control" line item. Budget control mechanism is a tool used by the FCC to keep the budget for certain support in line. This is an FCC term that was outlined in an FCC order, used by both the FCC and the industry and should not be changed. Also, Schedule I does not appear to have a line item titled "budget control."

#### *§26.407(l) Treatment of Federal Income Tax*

**Subsection (l)(1)(B)** - TSTCI and TTA commented that the rule should omit published subsection (l)(1)(B), because the calculation of excess accumulated deferred federal income taxes (ADFIT) occurred in 2017 and has been reclassified as a regulatory liability. The amount is fixed and will be amortized. Therefore, the provisions of published subsection (l)(1)(B), which require a telephone utility to stop recording excess ADFIT, would be unnecessary. TSTCI and TTA also commented that the provisions of published subsection (l)(1)(B) could be construed to conflict with the provisions of published subsection (l)(1)(C).

*Commission Response*

**The commission agrees with TSTCI and TTA that subsection (I)(1)(B) as published should be omitted and modifies the rule language accordingly.**

**Subsection (I)(2)(A)** - TSTCI and TTA commented that the rule should allow for a reasonable alternative calculation of the amount of excess current federal income taxes. TSTCI and TTA commented that, because telephone rates are established based on FCC benchmark requirements and are not based on use of a tax methodology in calculating a revenue requirement, it is difficult or practically impossible for a telephone utility to calculate its excess current federal income tax using the exact terms of the Modified Accounting Order in Project No. 47945. Accordingly, TSTCI and TTA suggested offering a reasonable and simple alternative calculation in subsection (I)(2)(A). The suggested alternative proffered by TSTCI and TTA is the difference in the current period federal income tax expense calculated under the Tax Cuts and Jobs Act of 2017 and the amount that would have been calculated under the federal tax code immediately preceding the Tax Cuts and Jobs Act of 2017.

*Commission Response*

**The commission agrees with TSTCI and TTA that the rule should allow for a reasonable alternative calculation of the amount of excess current federal income taxes. The commission adopts the language recommended by TTA and TSTCI and modifies the rule language accordingly.**

**Subsection (1)(2)(B)** - TSTCI and TTA commented that the rule should use the word “accrue” in place of the word “record” in the published language in subsection (1)(2)(B) to more accurately reflect the proper accounting action needed at that time.

*Commission Response*

**The commission agrees with TSTCI and TTA that the word “accrue” should be used instead of “record” and modifies the rule language accordingly.**

**Subsection (1)(2)(D)** - TSTCI and TTA commented that subsection (1)(2)(D) as published would require a telephone utility to violate GAAP by violating the matching principle. TSTCI and TTA offered an alternative using Schedule VII for Proposed Company Adjustments. Rather than adjust the information on the face of the reported schedules, a telephone utility would supplement those schedules with the requested information. TSTCI and TTA suggested changing the word “adjust” to “supplement” in subsection (1)(2)(D) as published and adding language providing that the changes to 2017 information will be reported as a proposed company adjustment.

*Commission Response*

**The commission disagrees with TSTCI and TTA’s assertion that the rule as published would have forced a telephone utility to violate GAAP, because the rule addresses a utility’s filing with the commission and does not address quarterly or annual filings with the Securities and Exchange Commission or any other report of financial information governed by the GAAP accounting framework. The commission agrees, however, with TSTCI and TTA’s other suggestion to supplement the schedules using Schedule VII for Proposed Company**

**Adjustments instead of adjusting the information on the face of the reported schedules. The commission makes the suggested modifications to the rule.**

**New subsection (l)(3)** -TSTCI and TTA commented that subsection (l) should include a new paragraph (3) to provide for the expiration of the subsection. Because subsection (l) addresses regulatory concerns that will exist only for a limited time, TSTCI and TTA recommended officially noting in the rule that the subsection would expire on December 31, 2019, and that the amortization of any regulatory liability would continue until completed.

TSTCI and TTA also stated that the instructions regarding Schedule III (Federal Income Taxes) errantly refer to Schedule IX instead of Schedule V.

***Commission Response***

**The commission agrees with TSTCI and TTA that there should be an official notice of the expiration date for subsection (l) and modifies the rule accordingly. The commission also agrees that the instructions should include the correct references to Schedule IX and has modified the rule accordingly.**

This new section is adopted under the section 14.002 of the Public Utility Regulatory Act, Tex. Util. Code Ann. §14.002 (West 2016) (PURA) that provides the commission with the authority to make and enforce rules reasonably required in the exercise of its powers and jurisdiction, and, specifically, §56.032, which requires that the commission develop and implement a mechanism to

determine the annualized Small and Rural Incumbent Local Exchange Company Universal Service Plan support for certain small ILECs.

Cross reference to statutes: Public Utility Regulatory Act §14.002 and §56.032.

**§26.407. Small and Rural Incumbent Local Exchange Company Universal Service Plan Support Adjustments.**

- (a) **Purpose.** This section establishes criteria for a small incumbent local exchange company (small ILEC) to request adjustments to the monthly support the company receives in accordance with §26.404 of this title (relating to the Small and Rural Incumbent Local Exchange Company Universal Service Plan).
- (b) **Application.**
- (1) **Small ILECs.** This section applies to a small ILEC that has been designated as an eligible telecommunications provider (ETP) by the commission in accordance with §26.417 of this title (relating to Designation as Eligible Telecommunications Providers to Receive Texas Universal Service Funds (TUSF)).
  - (2) **Other ETPs providing service in small or rural ILEC study areas.** This section applies to a telecommunications provider other than a small ILEC that provides service in small ILEC study areas that have been designated as an ETP by the commission in accordance with §26.417 of this title.
- (c) **Definitions.** The following words and terms, when used in this section, will have the following meaning, unless the context clearly indicates otherwise:
- (1) **Eligible telecommunications provider (ETP)** -- A telecommunications provider designated by the commission in accordance with §26.417 of this title.
  - (2) **Federal Communications Commission (FCC) Rate of Return** -- The FCC's most recently prescribed rate of return as of the date of any determination, review,

or adjustment under this section, to be no greater than 9.75 percent prior to July 1, 2021. If the FCC no longer prescribes such a rate of return, commission staff will initiate proceedings as necessary for the commission to determine or modify the FCC rate of return to be used for purposes of this section.

- (3) **Reasonable Rate of Return** -- An intrastate rate of return within two percentage points above or three percentage points below the FCC rate of return.
  - (4) **Small incumbent local exchange company (small ILEC)** -- For purposes of this section, a small ILEC is a small provider as defined by PURA §56.032(a)(2).
- (d) **Notification to the commission that a small ILEC seeks to participate in this section.**
- A small ILEC that is not an electing company under Chapters 58 or 59 may file a written notice to the commission to participate in this section to have the commission determine the amount of Small and Rural Incumbent Local Exchange Company Universal Service Plan support it receives, so that such support, combined with regulated revenues, provides the small ILEC an opportunity to earn a reasonable rate of return if the reported rate of return of such small ILEC is based on expenses that it believes are reasonable and necessary. When adjusting monthly support, the commission will consider, among other things described in this section, the adequacy of basic rates to support universal service. A small ILEC that submits a written notice to participate in this section will continue to receive the same level of Small and Rural Incumbent Local Exchange Company Universal Service Plan support it was receiving on the date of the written notice until the commission makes a determination or adjustment under this section.

(e) **Annual report of a requesting small ILEC.**

- (1) A small ILEC that submits a written notice under subsection (d) of this section must file an annual report each year with the commission, using commission-prescribed forms that are available on the commission's website. The initial annual report for a small ILEC that files a written notice under subsection (d) of this section must be filed within two months after a small ILEC elects to participate in this section. Subsequent annual reports must be filed no later than September 15<sup>th</sup> of each year. All annual reports must be related to the most recent calendar year prior to the filing of the annual report.
- (2) The annual report filed by a small ILEC under this subsection must include information on the following:
  - (A) Summary of revenues and expenses;
  - (B) All revenue, expense, and capital accounts;
  - (C) Invested capital;
  - (D) Intrastate federal income taxes calculated at the applicable tax rate;
  - (E) Network access service revenue;
  - (F) Weighted average cost of capital (for investor-owned utilities);
  - (G) Historical financial statistics;
  - (H) Proposed company adjustments;
  - (I) The name, job title, and total annual compensation of each officer, director, and, for investor-owned companies, owners and former owners (including each general manager and any other highly compensated employee that may not be designated as an officer of the company), and the name and

compensation of each family member of officers, directors, owners, and former owners employed by the small ILEC;

(J) The amount and nature of each affiliate transaction, including transactions with family members of officers, directors, and, for an investor-owned company, owners and former owners;

(K) All detail and supporting documentation necessary to support each of the items in subsection (e)(2); and

(L) An authorized official's signature.

(3) The small ILEC must also provide its full and complete cost allocation manual.

(f) **Commission staff's review of annual reports.** Annual reports submitted under this section will be reviewed by commission staff to determine whether a small ILEC's support, when combined with regulated revenues, provide the small ILEC an opportunity to earn a reasonable rate of return and whether the reported rate of return of the small ILEC is based on expenses that the commission staff determines are reasonable and necessary.

(1) **Timeline for review of the annual reports.**

(A) During the review of an annual report, commission staff may submit requests for information to the small ILEC. Responses to such requests for information will be provided to the commission staff within ten days after receipt of the request by the small ILEC. If a small ILEC fails to timely provide information to commission staff, the small ILEC will be considered to be a Category 3 provider.

(B) Within 90 days after an annual report has been filed, commission staff will complete its review of the annual report and file a memorandum for the commission's consideration regarding a final recommendation on the reported or commission-staff adjusted rate of return.

(2) **Commission staff's review of an annual report.**

(A) Commission staff will review and may make adjustments to information contained in the small ILEC's annual report, such as:

- (i) expenses that are not reasonable or necessary;
- (ii) expenses listed under §26.201(c)(2) of this title (relating to Cost of Service);
- (iii) expenses that are not in compliance with FCC rules;
- (iv) inappropriate affiliate transactions;
- (v) inappropriate cost allocations;
- (vi) inappropriate allocation of federal universal service support; and
- (vii) any other adjustments that commission staff may find appropriate.

(B) Commission staff will recalculate the small ILEC's reported rate of return and provide an adjusted rate of return if any adjustments were made in paragraph (2)(A) of this subsection.

(3) **Separation of small ILECs into rate of return categories.** Upon completion of commission staff's review of a small ILEC's annual report, commission staff will determine the appropriate category for the small ILEC within the following three categories based on the small ILEC's reported or commission-staff adjusted rate of return:

- (A) Category 1. A rate of return of more than three percentage points below the FCC rate of return;
  - (B) Category 2. A rate of return within two percentage points above or three percentage points below the FCC rate of return; and
  - (C) Category 3. A rate of return of more than two percentage points above the FCC rate of return.
- (4) Commission staff will file a memorandum for the commission's consideration of the categorization of each small ILEC in accordance with paragraph (1)(B) of this subsection.
- (g) **Treatment of small ILECs based on rate of return categories.** Each category will be processed as set forth below.
- (1) **Category 1** - A small ILEC that has a reported or commission-staff adjusted rate of return in Category 1 may file an application for an adjustment to have its annual Small and Rural Incumbent Local Exchange Company Universal Service Plan support or basic rates increased to a level that would allow the small ILEC to earn an amount that would be considered a reasonable rate of return, except that the adjustment may not set a small ILEC's support level at more than 140 percent of the annualized support the provider received in the 12-month period before the date of the adjustment. Any rate adjustments may not adversely affect universal service.
  - (2) **Category 2** - A small ILEC that has a reported or commission-staff adjusted rate of return in Category 2 will be considered to be earning a reasonable rate of return and will not be eligible to file for an adjustment to its Small and Rural Incumbent

Local Exchange Company Universal Service Plan support, except as described in subsection (h)(2)(B) of this section. The commission may not initiate a proceeding against a small ILEC that has a reported or commission-staff adjusted rate of return within Category 2.

- (3) **Category 3** - For a small ILEC that has a reported or commission-staff adjusted rate of return in Category 3, the commission staff may initiate a proceeding to review and adjust the small ILEC's Small and Rural Incumbent Local Exchange Company Universal Service Plan support or basic rates to adjust the small ILEC's rate of return into the reasonable rate of return range. A small ILEC that has a commission-staff adjusted rate of return in Category 3 is not eligible to file for an adjustment to its Small and Rural Incumbent Local Exchange Company Universal Service Plan support, except as described in subsection (h)(2)(B) of this section.

(h) **Contested case procedures.**

- (1) **Documents to be submitted.** At a minimum, the following information must be provided by a small ILEC in a contested case proceeding, irrespective of whether such case is initiated by a small ILEC or commission staff. Any proceeding filed under this section in which a party has intervened and requested a hearing is a case initiated by a small ILEC or commission staff and the filing requirements listed below apply to such cases.
- (A) all the data required by subsections (e) and (f) of this section;

- (B) responses to commission staff's requests for information in connection with the review of each small ILEC's annual report;
  - (C) the requested Small and Rural Incumbent Local Exchange Company Universal Service Plan support or rate adjustments; and,
  - (D) testimony and workpapers necessary to support the requested adjustments.
- (2) **Qualification for contested case proceeding.**
- (A) **Category 1 small ILECs.** A small ILEC in Category 1, as identified in subsection (f)(3) of this section, may file an application that is eligible for administrative review or informal disposition to request an adjustment to its Small and Rural Incumbent Local Exchange Company Universal Service Plan or basic rates to allow the company to earn a reasonable rate of return.
  - (B) **Category 2 or Category 3 small ILECs subsequent to rate of return adjustment by commission staff.** A small ILEC that has a reported rate of return in Category 1 or Category 2, as identified in subsection (f)(3) of this section, but that has a commission-staff adjusted rate of return in Category 2 or Category 3, may file a petition to contest the commission-staff adjusted rate of return and may also request an adjustment to its Small and Rural Incumbent Local Exchange Company Universal Service Plan support or basic rates in the same proceeding. A small ILEC that has a reported rate of return in Category 2 but because of commission-staff adjustments the small ILEC is in Category 3, may file a petition to contest the commission-staff adjustments. However, the small ILEC may not request an adjustment to its Small and Rural Incumbent Local Exchange Company Universal

Service Plan support or basic rates. Any proceeding that is initiated by a small ILEC to protest a reclassification and in which a party has intervened and requested a hearing is a case initiated by a small ILEC and the filing requirements listed below apply to these cases.

- (C) **Category 3 small ILECs.** A small ILEC in Category 3, as identified in subsection (f)(3) of this section, is subject to a commission staff-initiated proceeding to review the company's annual report and reported rate of return, must submit the information listed in paragraph (1) of this subsection.
- (3) **Notice.** Each small ILEC that files a contested case proceeding will provide notice as required by §22.55 of this title (relating to Notice in Other Proceedings). At a minimum, notice will be published in the *Texas Register* and will be provided to the Office of Public Utility Counsel. Each Category 1 small ILEC that files an application under this section must provide notice to its customers that the company may be required to increase its rates as part of the adjustment to have its annual Small and Rural Incumbent Local Exchange Company Universal Service Plan support increased.
- (4) **Burden of proof.** A small ILEC will bear the initial burden of production and the burden of persuasion.
- (5) **Timing for contested cases.** The commission must grant or deny an application filed under subsection not later than the 120<sup>th</sup> day after the date a sufficient application is filed. The commission may extend the deadline upon a showing of

good cause. The application will be processed in accordance with the commission's rules applicable to docketed cases.

- (6) **Timing to file a subsequent contested case.** Once the commission issues an order in a contested case under this section, the small ILEC and commission staff may not file a subsequent contested case before the third anniversary of the date on which the small ILEC's most recent application for adjustment is initiated, unless good cause is proven.
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- (i) **Confidentiality of information.**
    - (1) A report or information that a small ILEC is required to provide to the commission under subsection (e) of this section is confidential and not subject to disclosure under Chapter 552, Government Code.
    - (2) A third party may only access confidential information filed according to subsection (h) of this section, or proceedings related to that filing, if the third party is subject to an appropriate protective order.
    - (3) This subsection does not apply to a subsequent contested case initiated under subsection (h) of this section, and no claim of confidentiality will arise from this subsection in such a subsequent contested case.

(j) **Commission adjustment of the small ILEC's revenue requirement and Small and Rural Incumbent Local Exchange Company Universal Service Plan support.**

(1) **Revised revenue requirements.**

(A) In a proceeding conducted in accordance with subsection (h) of this section, the commission will determine the small ILEC's new revenue requirement necessary to allow the company to earn a reasonable rate of return; however, the commission may not set a small ILEC's support level at more than 140 percent of the annualized support the small ILEC received in the 12-month period before the date of the adjustment, nor may the rate adjustment adversely affect universal service.

(B) A small ILEC that is in Category 1 cannot request an increase in the Small and Rural Incumbent Local Exchange Company Universal Service Plan support that would result in a rate of return greater than the minimum of the reasonable rate of return. In a proceeding for a small ILEC in Category 3, a small ILEC or commission staff may not request a decrease in the Small and Rural Incumbent Local Exchange Company Universal Service Plan support that would result in a rate of return greater than the maximum reasonable rate of return.

(2) **Small and Rural Incumbent Local Exchange Company Universal Service Plan support payments to small ILECs.** The commission will determine the amount of adjustment to the annual Small and Rural Incumbent Local Exchange Company Universal Service Plan support or basic rates for the small ILEC that will be needed to meet the new revenue requirement identified in this paragraph.

The commission will determine the fixed monthly support payment for a small ILEC by dividing the Small and Rural Incumbent Local Exchange Company Universal Service Plan support by 12. Each small ILEC that has Small and Rural Incumbent Local Exchange Company Universal Service Plan support adjusted under this section must provide the TUSF administrator with a copy of the final order indicating the adjusted amount of Small and Rural Incumbent Local Exchange Company Universal Service Plan support.

- (3) **Small and Rural Incumbent Local Exchange Company Universal Service Plan support payments to ETPs other than small ILECs.** The Small and Rural Incumbent Local Exchange Company Universal Service Plan support for ETPs other than a small ILEC will be determined by calculating the per-line support for each small ILEC's study area based on the most recent monthly support using December line counts for the small ILEC. The payment to each ETP other than a small ILEC will be calculated by multiplying the computed per-line amount for the given small ILEC study area by the number of eligible lines served by the ETP in such study area for the month.

(k) **Miscellaneous items.**

- (1) **Federal Universal Service Fund (FUSF) support.** The amount of annual FUSF support received by the small ILEC that is considered to be an intrastate expense adjustment under Part 36 and Part 54 of the FCC's rules or by FCC order, regardless of the category of FUSF support, will offset the total intrastate expenses and be reflected as such in the small ILEC's annual report. The timing of any FUSF

support will be considered when making a determination under subsection (j) of this section.

(2) **Recovery of FUSF support from the TUSF in accordance with PURA §56.025.**

The amount of FUSF support recovered from the TUSF in accordance with PURA §56.025 that is considered an intrastate expense adjustment under Part 36 and Part 54 of the FCC rules or by FCC order, regardless of the category of FUSF support or type of budget control mechanism placed on FUSF support, will be shown as an offset to the total intrastate expenses in the small ILEC's annual report. The timing of any recovery of FUSF support from the TUSF in accordance with PURA §56.025 and the timing of any true-ups must be considered when making a determination under subsection (j) of this section.

(3) **Commission authority.** Nothing in this section prohibits the commission from conducting a review in accordance with PURA, Chapter 53, Subchapter D.

(1) **Treatment of federal income tax expense.**

(1) **Accumulated deferred federal income taxes (ADFIT).**

(A) For a small ILEC investor-owned utility (IOU) subject to federal income tax, the IOU must record on its books a regulatory liability for amounts of excess ADFIT resulting from the Tax Cuts and Jobs Act of 2017 (TCJA), in accordance with the commission's order in Project No. 47945. An IOU must include this information on the annual report required by this rule. For the purposes of this section, excess ADFIT is defined as the difference between the amount of ADFIT on the IOU's books after incorporating

changes from the TCJA and the amount of ADFIT that would have been on the IOU's books had the tax changes in the TCJA not occurred.

- (B) IOUs will either amortize the excess ADFIT regulatory liability over a period not to exceed five years or allow it to reverse along with the associated ADFIT according to the transaction that resulted in the ADFIT.

(2) **Current federal income tax expense.**

- (A) For an IOU subject to federal income tax, the IOU must record on its books a regulatory liability for amounts of excess current federal income taxes resulting from the TCJA, in accordance with the commission's order in Project No. 47945. An IOU must include this information on the annual report required by this section. For purposes of this section, excess current federal income tax expense is defined as the difference between the amount of revenue collected under current rates related to current federal income tax expense and the amount of revenue related to current federal income tax expense that should have been collected under rates reflecting changes in the TCJA. An acceptable alternative calculation of an appropriate regulatory liability for purposes of this rule is the difference in the current period federal income tax expense calculated under the TCJA and the amount that would have been calculated under the federal tax code immediately preceding the TCJA.
- (B) At such time that commission staff files a memorandum for the commission to categorize the IOUs' rate of return for 2017, the IOUs will no longer

accrue on the books the regulatory liability for excess current federal income tax expense.

- (C) An IOU will amortize the regulatory liability for the excess current federal income tax expense over a period not to exceed five years.
  - (D) An IOU will supplement its 2017 reported financial information to reflect the amount of current federal income tax expense for 2017 calculated as if the terms of the TCJA had applied to 2017 operations to calculate potential support from the Small and Rural Incumbent Local Exchange Company Universal Service Plan. The IOU will report this information as a proposed adjustment.
- (3) This subsection will expire on December 31, 2019. Any amortization of a regulatory liability resulting from application of this subsection would continue until completed.

This agency certifies that the adoption has been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority. It is ordered by the Public Utility Commission of Texas that §26.407 relating to Small and Rural Incumbent Local Exchange Company Universal Service Plan Support Adjustments Pursuant to S.B. 586 is adopted with changes to the text as proposed.

**Signed at Austin, Texas the \_\_\_\_\_ day of October 2018.**

**PUBLIC UTILITY COMMISSION OF TEXAS**

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**DEANN T. WALKER, CHAIRMAN**

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**ARTHUR C. D'ANDREA, COMMISSIONER**

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**SHELLY BOTKIN, COMMISSIONER**