

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

GENESEO TELEPHONE COMPANY, :
CAMBRIDGE TELEPHONE COMPANY and :
HENRY COUNTY TELEPHONE COMPANY : Docket 11-0210
:
Petition for Universal Service. :

ILLINOIS INDEPENDENT TELEPHONE :
ASSOCIATION :
:
:
Petition to update the Section 13-301(1)(d) Illinois : Docket 11-0211
Universal Service Fund and to implement Intrastate :
Switched Access Charge reform as described herein : Consolidated
and for other relief. :

LEAF RIVER TELEPHONE COMPANY

BRIEF ON EXCEPTIONS

January 31, 2013

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I. INTRODUCTION

Leaf River Telephone Company (“Leaf River”) agrees with that portion of the January 17, 2013, Proposed Order that establishes an update to the Illinois Universal Service Fund (“IUSF”). Leaf River takes exception, however, to the Proposed Order’s denial of Leaf River’s Motion to Reopen for the purpose of admitting Leaf River Late Filed Exhibits 7.0, 8.0 and 9.0, which establish that Leaf River is a C corporation and its IUSF funding amount should be \$411,801 per year. In addition, Leaf River supports the IITA Member Intervenors¹ Brief on Exceptions for subchapter S companies.

II. LEAF RIVER’S IUSF FUNDING SHOULD INCLUDE STATE AND FEDERAL INCOME TAXES SINCE LEAF RIVER WILL PAY THOSE TAXES IN FUTURE YEARS JUST LIKE EVERY OTHER C COMPANY

The Proposed Order’s conclusions deny Leaf River’s Motion to Reopen based on two points: (1) Staff and AT&T raised “concerns” regarding a possible mismatch of financial data used to determine Leaf River’s IUSF support; and (2) granting the Motion will increase the fund size. *See* Proposed Order at 44. Those points ignore the known and measurable tax costs applicable to Leaf River and are contrary to the legislative purpose of the IUSF.

Leaf River is a C corporation and the Proposed Order erroneously fails to recognize Leaf River’s federal and state income taxes as a C corporation, where the tax cost will actually be paid by Leaf River at the corporate level. Using the 2009 data together with Leaf River’s 2013 tax status to calculate the amount of state universal service support to Leaf River presents no real disharmony and should not form the basis of denying Leaf River’s request. Leaf River’s 2009 tax status is not as important as what Leaf River’s actual tax status will be during the next few years.

¹ Unless indicated to the contrary, all capitalized terms in this brief will have the same definitions assigned to them in the IITA Initial Brief.

220 ILCS 5/13-301(1)(d) provides that proxy costs as determined by the Commission can be used to calculate IUSF support. The HAI cost model indicates the group of companies have costs (after deducting federal USF support) *greater than* their combined rate of return. The Commission then has used the Schedule 1.01 as a rate of return cap on the HAI model and the Schedule 1.01 calculation includes federal and state income taxes for corporations that *in future years* will incur those taxes. The Schedule 1.01 is part of the proxy costs used by the Commission and those costs are useful if they reflect the likely situation of each company in the future. The Schedule 1.01 provides for out of period adjustments on the last page of the Schedule 1.01 to reflect those known and measurable changes. Here, we know Leaf River will incur taxes and Leaf River is asking for the same treatment that every 2013 C corporation will enjoy.

Calculating the amount of income taxes incurred by LRTC based on the 2009 data is a mathematical exercise that is known and measurable. Staff opposed any support for the tax component of S corporations because S corporations do not pay income taxes. Following Staff's policy concerns, LRTC elected to become a C corporation.

Much the same occurred with *Monarch Gas*. In *Monarch Gas Co. v. Illinois Commerce Comm'n*, 51 Ill. App. 3d 892; 366 N.E.2d 945 (5th Dist. 1977), the court upheld the Commission's refusal to allow Monarch Gas as an S corporation to recognize the cost of its shareholders' income tax liability for ratemaking purposes. After the *Monarch Gas* case was decided by the Appellate Court, Monarch Gas rescinded its Subchapter S election and the company was then entitled to full recovery of income taxes as a C corporation. See Order in Docket No. 77-0709, issued Sept. 6, 1978 at p. 3.

Leaf River's tax status as an S corporation in 2009 should not prevent it from receiving funding now as a C corporation. To deny Leaf River the tax support would be harsh and inequitable since Leaf River **will pay** corporate income taxes for 2013 and future years and it is reasonable to provide the company with funding for income taxes as set forth in Leaf River Late Filed Exhibits 7.0, 8.0 and 9.0. Even Staff proposed an adjustment to the state income tax rate from 7.3% (the rate in 2009) to 9.5% (the rate in 2013) (ICC Staff Ex. 2.0 @ 3-4; ICC Staff Ex. 5.0 @ 5-6) to reflect the current corporate income tax rates which is essentially what Leaf River is proposing to do by taking its 2009 tax rate of zero to its 2013 tax rate.

Finally, the Proposed Order (at p. 44) asserts that what Leaf River is proposing will increase its IUSF funding (which it does by \$169,217 but by only \$67,649 if the Commission funds the taxes for S corporations). Reducing (or increasing) the size of the IUSF, however, cannot be an end in itself. One legislative purpose of the IUSF is to support:

telecommunications services should be available to all Illinois citizens at just, reasonable and affordable rates and that such services should be provided as widely and economically as possible in sufficient variety, quality, quantity and reliability to satisfy the public interest.

220 ILCS 5/13-103(a) (cited as the basis for the Commission's duties in establishing an IUSF in 220 ILCS 5/13-301(1)). In short, the Legislature's policy in establishing an IUSF is to ensure broad access to quality telecommunications services at affordable rates. Denying Leaf River sufficient funding to cover its known costs of service, which includes its annual tax liabilities fundamentally undermines these goals. Denying Leaf River funding for the sole purpose of reducing the fund is contrary to the Legislature's intent.

The Proposed Order should grant Leaf River's Motion and implement an updated interim IUSF at the per-company amounts listed on either Leaf River's Revised Attachment B² or Revised Attachment C attached to this Brief. Alternatively, Leaf River includes a revised page 3 to the Appendix that was included with the Proposed Order.

III. PROPOSED EXCEPTIONS LANGUAGE

1. Leaf River proposes that the following changes be made to Section V.C., "Commission Analysis and Conclusion" at pg. 43, and carrying on after the paragraph reprinted at the end of the excerpt below:

The Commission also notes that on December 18, 2012, Leaf River, which is one of the S Corporations referenced above, filed a "motion to reopen." Leaf River states that it has made a corporate decision to revert back to a Chapter C corporation for tax purposes. By virtue of that decision, Leaf River seeks admission of exhibits on reopening "without hearing" which, according to ~~AT&T Illinois~~, Leaf River Late Filed Exhibit 8.0 would ~~increase~~set Leaf River's annual IUSF funding request ~~at~~to \$411,801.

On or before January 2, 2013, AT&T Illinois and Staff filed responses objecting to Leaf River's motion. Leaf River filed a reply on January 15, 2012.

Among other things, AT&T Illinois and Staff contend that the motion is not timely. They also argue that Leaf River's proposal would be "asymmetrical," in that it uses 2009 financial data while at the same time recognizing a 2012 tax election effective in 2013, without updating other elements of Schedule 1.01, and that such a mismatch would be contrary to prior Commission Orders such as *Alhambra-Grantfork*.

Staff also comments that since the case has already been marked "Heard and Taken," Leaf River is apparently seeking relief under Section 200.870 of the Commission Rules of Practice, entitled "Additional Hearings," which allows a party to request "additional hearings" to offer "additional evidence." Here, however, Leaf River seeks to place the additional evidence into the record, over the objections of other Parties, "without hearing."

Having reviewed the filings, the Commission agrees that as a matter of accuracy and fairness, ~~with AT&T Illinois and Staff that~~ Leaf River's motion seeking admission of the exhibits without hearing should ~~not~~ be granted. Leaf

² Attachment B is IITA Exhibit 5.10 modified only to include Leaf River's funding as a C corporation and as that modifies the fund size. Attachment C is modified the same way.

River is a C corporation and the calculation of that tax impact on its 2009 data is known and measurable. Leaf River's request for taxes are calculated the same way as every other C corporation in this docket using the proxy cost methodology adopted by the Commission. While ~~w~~What Leaf River is proposing through these exhibits would increase its IUSF funding, Exhibit 8.0 accurately reflects Leaf River's identifiable costs of providing the supported services as a C corporation during the operation of the Interim Fund. There is no sound reason why Leaf River should be deprived of funding for its actual cost of taxes during that time. Staff and AT&T Illinois have raised substantive concerns regarding a possible mismatch of financial data used to determine Leaf River's IUSF support. Those concerns are unfounded and its status as a C corporation is what will actually occur in future years. Under the circumstances, ~~allowing~~admitting Leaf River's to simply insert those exhibits into the evidentiary record at this time without hearing, over the objections of other Parties, would not be is appropriate.

2. The first full Ordering Paragraph should be changed as follows:

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that an interim updated Illinois Universal Service Fund in the amount of ~~\$18,984,628~~\$19,784,807 to be allocated as shown in the Appendix to this Order and in Schedules 1 and 2 attached to the Staff initial brief filed September 14, 2012, plus administrative expenses (the "Interim Fund") shall, pursuant to Section 13-301(1)(d) of the Illinois Public Utilities Act, be implemented on the first day of the calendar month following by 60 days the date of this Order and shall, as of that date, supersede the current IUSF.

3. In the event that the Commission adopts Staff's position on the subchapter S matter, the first full Ordering Paragraph should be changed as follows:

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that an interim updated Illinois Universal Service Fund in the amount of ~~\$18,984,628~~\$19,153,845 to be allocated as shown in the Appendix to this Order and in Schedules 1 and 2 attached to the Staff initial brief filed September 14, 2012, plus administrative expenses (the "Interim Fund") shall, pursuant to Section 13-301(1)(d) of the Illinois Public Utilities Act, be implemented on the first day of the calendar month following by 60 days the date of this Order and shall, as of that date, supersede the current IUSF.

Depending on the Commission's ultimate decision on the treatment of taxes for S corporation, either the attached Appendix B (in case the Commission's sides with the IITA) or Appendix C (in case the Commission's sides with the Staff) should be attached to the Order.

IV. CONCLUSION

For the reasons set forth above, the Commission should grant Leaf River's Motion to Reopen and increase the fund size to \$19,784,807 (with the Frontier Companies included) with the individual company qualifying amounts itemized on the Attachment B provided with this Brief on Exceptions or, alternatively Exhibit C, and for such other relief as is deemed just.

Dated this 31st day of January, 2013

Respectfully submitted,

LEAF RIVER TELEPHONE COMPANY

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CERTIFICATE OF SERVICE

Docket No. 11-0211 (Consolidated)

The undersigned certifies that a copy of the foregoing instrument was served upon all parties to the above cause at their address as follows:

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