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**Report to the Utilities and Energy Committee on Actions Taken by the Maine
Public Utilities Commission Pursuant to 35-A M.R.S.A. Chapter 91**

**2004 Report on the Alternative Form of Regulation for Telephone Utilities
September 1, 2004**

Section 9105 of 35-A M.R.S.A. requires the Maine Public Utilities Commission to provide the Utilities and Energy Committee with an annual report describing Commission activities under Chapter 91 and the effectiveness of any adopted alternative form of regulation (AFOR) in achieving the objectives of Chapter 91. This report constitutes the Commission's compliance with the annual reporting requirement of Chapter 91.

In 1994, the Maine Legislature enacted Chapter 91 of Title 35-A, which authorized the Commission to adopt an AFOR for any telephone utility in the State, provided that certain requirements were met. By an Order dated May 15, 1995, the Commission adopted an AFOR for Verizon, which at that time operated as NYNEX. Through Orders issued by the Commission on May 9, 2001, June 25, 2001, and October 12, 2001, the Commission extended the Verizon AFOR for an additional five years and also ordered several significant changes to be made to the pricing rules and Service Quality Index (SQI) mechanism. The Public Advocate (OPA) and the American Association of Retired Persons (AARP) appealed that decision to the Law Court. On February 28, 2003, the Law Court remanded the case back to the Commission. On September 28, 2003, the Commission issued its Order Reinstating the AFOR. The OPA and AARP appealed that decision on October 14, 2003. The Law Court received briefs and heard oral argument on the appeal in April 2004, but it has not issued a decision at this time. While the appeal is pending, the modified and extended AFOR remains in effect, and Verizon must adhere to all pricing and service quality mandates contained in the Commission's Order Reinstating AFOR.

In Orders issued on May 28, 2004, and June 8, 2004, the Commission approved Verizon's request to increase local rates in order to offset the access rate reductions required by 35-A M.R.S.A. § 7101-B.¹ The OPA asked the Commission to reconsider its decision, but the Commission reaffirmed its initial decision. The Commission determined that the reduction in intrastate access rates mandated by the statute met the AFOR's definition of an exogenous change, and thus, Verizon was permitted to increase its local rates by approximately \$0.27 per month per access line, effective June 1, 2004. An additional increase of approximately \$0.27 per access line per month will become effective on June 1, 2005.

¹ 35-A M.R.S.A. §7101-B requires that, by May 31, 2005, intrastate access rates be less than or equal to the company's interstate rates that were in effect on January 1, 2003. In December 2, 2003, the Commission ordered Verizon to comply with this statute by reducing its intrastate access rates in two steps, on June 1, 2004 and May 31, 2005. The AFOR permits an increase in local rates if an exogenous change occurs to Verizon's revenues or costs, and defines standards by which a change will be deemed exogenous.

The Verizon AFOR currently contains fifteen service quality metrics with benchmarks against which Verizon's actual performance is measured on an annual basis. If Verizon's actual results fail to meet a benchmark, a penalty is calculated under a formula (established in the initial AFOR) that considers the degree by which the performance failed to meet the benchmark. The penalties for any of the failed metrics are added together to determine the total penalty dollar amount, and Verizon must provide credits on its customers' bills for that total amount. The credit amount is returned to customers either in a lump sum or in monthly increments, depending on the size of the total penalty.

For the AFOR year ended June 30, 2004, Verizon's total penalty amount is \$619,673. Verizon's actual results failed the benchmark in six of the fifteen metrics. The largest failure (and thus the largest penalty amount) was in the metric that measures the percentage of residential trouble reports that are not cleared within 24 hours. Verizon missed the benchmark by over 62% and was able to meet the standard in only two of the twelve months, resulting in a penalty amount of \$469,194 for this metric, which is over 75% of the total calculated penalty amount. The Commission may further investigate the reasons for Verizon's failure to meet this metric to determine if any changes may be needed to the SQI penalty mechanism.

In its 2001 Order Reinstating AFOR, the Commission also adopted a new metric that measures the percentage of call attempts that cannot be completed because of network congestion. Because Verizon did not have a method of capturing and reporting blockages during only peak busy hours, the interim metric implemented in 2001 used data from all hours in the calculation, but the Commission ordered Verizon to capture data so that the benchmark for the call blocking metric could be based on peak hour data. For thirty months, Verizon recorded and reported the data necessary to establish the benchmark, and on July 1, 2004, the call blocking metric was changed to a calculation based on peak hour data. Going forward, Verizon will report its actual results for this metric based on the revised methodology, and the Company will compare its actual performance to the new benchmark.

While not exclusively related to the Verizon AFOR, and therefore not included in this report, the Commission intends to present to the Committee a comparison of prices and services available in 2004 with those available a decade earlier. In general, we expect the comparison will show a substantial decrease in the price of telephone services and an accompanying expansion in service offerings. While many factors contribute to these advances – including rapid technological change and the emergence of competition in most market segments – the Commission's adoption of the Verizon AFOR may have contributed to, and does not appear to have inhibited, Maine's progress in these areas.