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2003 Report on the Alternative Form of Regulation for Telephone Utilities

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

Section 9105 of 35-A M.R.S.A. requires the Maine Public Utilities Commission (Commission) to provide the Utilities and Energy Committee with an annual report describing the Commission's 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. By Order dated May 15, 1995, the Commission adopted an AFOR for Verizon. 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.

At the start of the extended AFOR period, the Commission simultaneously allowed Verizon to increase its basic exchange rates by \$1.78 per month for all customers, except those under the Lifeline rates available to low-income customers. The basic rate increase was granted in order to allow Verizon to recover most of the access revenue loss that occurred when Verizon lowered its intrastate access rates on June 1, 2001, to the interstate level, in compliance with 35-A M.R.S.A. § 7101-B.

As part of the extended AFOR, the Commission capped basic rates at the level that included the \$1.78 increase described above, and also gave Verizon flexibility to change all other rates, except operator services and directory assistance, at the Company's discretion by filing revised tariffs and providing proper notice to customers. In the AFOR extension Order, the Commission also adopted 15 SQI measures that contain standards that Verizon must meet. If Verizon fails to meet any of the SQI measures on an annual basis, it will be required to rebate to customers up to \$1.135 million per measure, with an annual cap of \$12.5 million.

On November 9, 2001, the Office of the Public Advocate (OPA) filed with the Maine Law Court a Notice of Appeal from the Commission's AFOR Order. The OPA challenged several aspects of the Commission decision. On February 28, 2003, the Law Court vacated and remanded the matter back to the Commission, because it found that the Commission had failed to perform the

analysis and make the finding required in Subsection 9103(1)¹ of Title 35-A. On March 19, 2003, the Commission sought comments on how it should address the issues raised in the Law Court's decision. The Commission divided the proceeding into two phases. The first phase addressed whether the Commission has the authority to keep the \$1.78 rate increase in effect, and if so, whether the increase should remain in effect. The first phase also addressed the issue of the interim form of regulation that would apply to Verizon while the Commission completed the proceedings required by the Law Court. The second phase, set out in the Commission's March 19th Order, established the schedule for addressing the broader Remand issues.

After considering comments from interested parties, the Commission issued orders on June 23rd and July 14th that kept the \$1.78 basic rate increase in effect, because the Commission found that it had authority to do so that was independent from the AFOR, and the increase was designed to allow Verizon partial recovery of its lost access revenues mandated by Section 7101-B. The Commission also decided that in the interim period, Verizon would be governed by the pricing provisions contained in the extended (but now vacated and remanded) AFOR for all services other than basic local service. Further, the Company would be subject to the revised SQI metrics that were established in the extended AFOR. The Commission indicated that it was making no further decision on local rates at that time.

The Commission has received comments on how it should proceed to address the Phase 2 issues, and it will move forward on this phase in the near future. There are several complex policy, legal and practical matters that must be considered carefully before the Commission proceeds.

On August 1, 2003, the OPA and the AARP appealed the Commission's June 23rd and July 14th Orders to the Law Court, arguing that the Commission's decision to keep the \$1.78 increase in effect was unlawful because of the Law Court's earlier decision. The petitioners argue that the Commission, contrary to its finding, did not have independent authority to increase rates until it conducted the examination required in Subsection 9103(1). On August 4, 2003, the OPA sought a stay of the Commission's June 23rd and July 14th Orders and asked the Court to roll back the \$1.78 increase immediately, while its appeal was pending. The Commission has filed its initial response to the stay request. The Court has not acted on the stay request, but has established a schedule for briefing of the issues covered by the appeal.

¹ Subsection 9103(1) states: "For the period of the alternative form of regulation, which may not be less than 5 years nor exceed 10 years without affirmative reauthorization by the commission, ratepayers as a whole, and residential and small business ratepayers in particular, may not be required to pay more for local telephone services as a result of the implementation of an alternative form of regulation than they would under traditional rate-base or rate-of-return regulation."