STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 99-851

July 11, 2003

PUBLIC UTILITIES COMMISSION
Investigation into Verizon Maine's
Alternative Form of Regulation

ORDER
(POST-REMAND NO. 1)
PART 2

WELCH, Chairman; NUGENT and DIAMOND, Commissioners

I. SUMMARY

In this Order – Part 2, we state the reasons for our conclusions (previously set forth stated in the Part 1 Order) concerning the present level of rates for local exchange service provided by Verizon Maine and interim regulation of Verizon while we consider the issues required by the remand of this case by the Law Court.

Initially, we decide that that Verizon shall continue to charge its present rates for local exchange service. Those rates include the $1.78 increases ordered in the May 9, 2001 and June 25, 2001 orders in this docket. We ordered those increases to offset access rate reductions required by law. Based on our own analysis and our reading of the Law Court's decision in this case, we find that those rate increases were not integral to the vacated AFOR, and that we had and do have authority to order them independently of any AFOR or other form of regulation, both on an interim basis and permanently.

We also decide that until we complete the proceedings following the remand from the Law Court, Verizon Maine will be subject to interim regulation provisions that are identical to those described in the June 25, 2001 order except for the regulation of rates for local exchange service. This interim regulation will consist of rate caps and stayouts for directory assistance and operator services, pricing flexibility for retail toll and optional services, and the Service Quality Index (SQI). For local exchange service, we do not decide at this time whether Verizon is also subject to the local rate cap and stay-out provisions described in the June 25, 2001 Order or if it is subject to price change rules inherent in rate of return (or "cost of service") regulation.[1] If a rate proceeding is filed (or some other precipitating event occurs) before we resolve the issues we must address on remand, it may become necessary to decide those questions.

---

[1] *See* 35-A M.R.S.A. §§ 301-312 and 1302-1309.

II. PROCEDURAL BACKGROUND

On February 28, 2003, the Maine Supreme Judicial Court, sitting as the Law Court, vacated this Commission's June 25, 2001 AFOR Order (*2001 AFOR Order*) and remanded the case for "further proceedings consistent with this opinion." *Office of the Public Advocate v. Public Utilities Commission and Verizon New England, Inc*., 2003 ME 23, 816 A.2d 833 (*OPA v. PUC/Verizon* or 2003 ME 23). On March 19, 2003, we issued a Notice of Further Proceedings Following Remand (NFR). The NFR described a number of issues we must consider in order to determine whether to order a continued AFOR for Verizon. The NFR requested the parties to address the two issues we decide in this Order in a first round of briefing. We will address issues concerning a long-term AFOR in a later order.

Verizon Maine (Verizon) and the Public Advocate (OPA) filed briefs that addressed both of the issues discussed in this Order. The American Association of Retired Persons (AARP) filed a brief that addressed the local rate issue, but not the interim regulation issue.

III. THE $1.78 INCREASE TO LOCAL RATES TO OFFSET ACCESS REVENUE LOSSES

As proposed in the NFR, we decide that the increase in local rates of $1.78, ordered on June 1, 2001, will continue in effect. This increase was implemented for the purpose of offsetting access rate reductions required at that time by 35-A M.R.S.A. § 7101-B. The revenue effect of those access rate reductions continues on a permanent basis. We find that our decision to increase local rates to accommodate this revenue loss is separate from the AFOR and is not dependent on re-implementation of the AFOR. We do not agree with the arguments of the Public Advocate and AARP that the Law Court's vacation of the June 1, 2001 AFOR order precludes us from ordering a continuation of this rate increase.[2]

---

[2] We also do not agree with Verizon's procedural argument that the Public Advocate has waived this issue because, after being informed in an e-mail from the Commission that it did not believe that the $1.78 increase had been reversed, the Public Advocate did not seek clarification from the Law Court. We are not aware of any doctrine, and Verizon cites none, that would require a party to take such an action in order to preserve arguments, before an administrative agency, about the interpretation of an appellate court's opinion following a remand to the agency.

Because we agree with the result argued by Verizon, we also do not find it necessary to reach Verizon's arguments contained in Part I.B.2 of its brief.

Relying on past case law, the Court explicitly ruled that the Commission "acted within its discretion in allowing Verizon to increase its basic service rates." 2003 ME 23, ¶1 and n.2. The Court also vacated the "order creating the alternative form of regulation." A single Commission order contains both the decision to implement the AFOR and the decision to allow Verizon to increase its basic service rates. As discussed below, the Court may have viewed the two decisions as separate orders, notwithstanding the fact that they were both included in a single document labeled "Order."

The Court's intent concerning the decision to increase local rates is difficult to discern. Unlike Verizon, then, we do not believe that the Court's decision is completely free from ambiguity.[3] Nevertheless, on balance, we believe the Court did not intend to rule that the local rate increase was an integral part of the AFOR ordered by the Commission, or that the $1.78 increase could not stand because it was necessary to vacate the order creating the AFOR, or that the increase could be ordered only in conjunction with the establishment of a new AFOR.[4] The Court provided no indication that it considered the local rate increase to be an integral part of or dependent on the AFOR. The court could have said, as the Public Advocate argued to the Court, that the Commission did not have the authority to order the $1.78 increase or that it was unsupported by evidence. The Court made no such ruling. Instead, it stated that the Commission had the authority to increase rates to offset the effects of the mandated access rate reductions.

---

[3] Verizon argues:

> …the Law Court took care to separately consider and explicitly address the increase in Verizon Maine's rates that was collateral to the Commission's adoption of the renewed AFOR. The Court's decision could not be more clear on this point.
>
> …
>
> While the Court's opinion vacates and remands to the Commission its AFOR orders for non-compliance with Section 9103(1), that section of the statute – *as the Law Court expressly determined* – has nothing to do with the $1.78 adjustment in rates. (Emphasis added).

Although we agree that the two matters are separate, we do not find an express determination by the Court that Section 9103(1) has "nothing to do" with the $1.78 increase.

[4] The OPA's present position is somewhat at odds with the position it took in the AFOR proceeding, where it objected to "incorporation of the May 2001 access change into this proceeding." *2001 AFOR Order* at 16.

The Court also could have agreed with the Public Advocate that the Commission must conduct a *full* rate proceeding in order to answer the question posed by 35-A M.R.S.A. § 9103(1) and to order a new AFOR. Such a proceeding almost certainly would have resulted in a different local rate as the starting point for the AFOR than the $1.78 adjustment. Nevertheless, the Court made no such ruling. Instead, it stated that a full rate case was not necessary in order to address the finding required by 35-A M.R.S.A. § 9103(1).

Footnote 2 of the Court's opinion recognized the Commission's implied and inherent powers to order, or refuse to order, a basic rate change in connection with enforcing the access parity statute, 35-A M.R.S.A. § 7101-B, The Court stated:

> In order to comply with section 7101-B, the Commission has the authority to order a reduction in access fees charged by NYNEX. It likewise has the authority to allow Verizon to offset some of its losses resulting from the reduced access fees.

2003 ME 23, ¶ 1 n. 2. The footnote recognized this power exists now. It also recognized that it existed in 1997, notwithstanding the original AFOR, which the Court correctly characterized as generally precluding rate changes except pursuant to the pricing rules of the AFOR.[5] There is no

---

[5] Footnote 2 of the Court's opinion states in full:

> Generally, a utility subject to an AFOR is precluded from returning to the Commission for relief if its costs are high or profits low. In *New England Telephone & Telegraph Co. v. Public Utilities Commission*, 1997 ME 222, ¶ 7, 705 A.2d 706, 708-09, NYNEX appealed from a Commission order amending its rules to implement the Access Parity Statute, 35-A M.R.S.A. § 7101-B (Pamph. 2002), and mandating that Verizon reduce its intrastate access charges by twenty percent, without offsetting charges to make the order revenue neutral. We recognized the broad authority of the Commission, and concluded that the 1995 AFOR reserved to the Commission the power to issue such an order. Title 35-A M.R.S.A. § 7101(2) (Pamph. 2002) [sic; citation should be to 35-A M.R.S.A. § 104] provides that the Commission has "all implied and inherent powers under the Title which are necessary and proper to execute faithfully its express powers and functions." In order to comply with section 7101-B, the Commission has the authority to order a reduction in access fees charged by NYNEX. It likewise has the authority to allow Verizon to offset some of its losses resulting from the reduced access fees. *New England Tel. & Tel. Co.*, 1997 ME 222, ¶ 7, 705 A.2d at 708-09.

2003 ME 23, ¶ 1 n. 2.

reason to believe the Commission would not have the same or greater discretion under non-AFOR regulation. The broad authority recognized by the Court in Footnote 2 does not appear to depend in any way on the existence of an AFOR.

There also is no conceptual link between the $1.78 increase and the reason the Court reversed the AFOR order. The Court reversed the order because the Commission failed to make, adequately, the finding necessary to choose an incentive rate plan over ROR regulation. The $1.78 rate increase, on the other hand, was to offset access revenue losses resulting from a statute, unrelated to the AFOR statute, that requires decreases in access rates. The Court made very clear that its reasons for vacating the AFOR Order was the deficient finding under 35-A M.R.S.A. § 9103(1); it did not reverse because of a lack of authority to order an increase to local rates to offset required access rate decreases. The Court stated clearly its reason for its reversal:

> …because we agree, in part, with the Public Advocate that the *Commission failed to fully comply with section 9103(1)*, we vacate and remand to the Commission for further proceedings."

2003 ME 23 at ¶ 1 (emphasis added). In addition, as pointed out by Verizon, the Court's "entry" reads:

> Order *creating the alternative form of regulation* vacated. Remanded to the Commission for further proceedings consistent with this opinion (emphasis added).

The Public Advocate's argument that the Court reversed the $1.78 local rate increase is based *entirely* on the fact that the Court vacated the order that simultaneously established the revised AFOR and ordered the $1.78 increase in rates. The Public Advocate, in both its brief and exceptions, never once addressed the Court's findings concerning the $1.78 increase. Even the language of the entry, however, supports the view that the reason for reversal is the failure to make an adequate finding under 35-A M.R.S.A. § 9103(1) and is not related to the increase in local rates to offset access rate reductions. It is surely consistent with the Court's opinion to find that it did not intend to undo the $1.78 increase in local rates. As the Court's opinion states, "the Commission *acted within its discretion* in allowing Verizon to increase its basic service rates (emphasis added)."

We also find significance in the Court's use of the singular and plural in its references to the Commission's actions. The Court characterized the appeal as from "*orders* of the Commission relating to the establishment of an 'alternative form of regulation' (AFOR)…*and* allowing Verizon to increase its basic service rates (emphases added)." It also referred to the Public Advocate's arguments "that the *orders* should be vacated (emphasis added)." 2003 ME 23, ¶ 1. These

reference to "orders" are in the same paragraph in which the Court ruled that the Commission acted "within its discretion" in ordering the $1.78 increase. By contrast, in its "entry," the Court vacated the "*order* creating the [AFOR]." While we do not place conclusive weight on the Court's differentiation between singular and plural, we cannot lightly assume that the differentiation was accidental.

Even if it were true that the Court's entry reversed the $1.78 increase, we see nothing in the Court's opinion that would prevent reinstatement of components of the order that do not suffer from the legal error that required the reversal. Thus, we decide, in the alternative, that we may order the $1.78 increase at this time. We may do so because, as explained above, the increase is separate from the AFOR decision and because the record previously developed in this proceeding (prior to the appeal) fully supports the need for the increase. We see no reason, on remand, why we are not free to make appropriate decisions based on the existing record. That record establishes the strong likelihood that Verizon will lose substantial access revenues, along with retail toll revenues. We decided at the time of the AFOR Order that it was reasonable to allow Verizon to offset the access revenue losses, but not the retail toll revenues. We reaffirm that decision now. The $1.78 increase was added to the rates for local exchange service that were in effect at the end of the prior AFOR. Those rates were definitionally reasonable at that time, because they were established pursuant to a lawful AFOR.

We also find that this decision is equitable. Verizon has in fact reduced its access rates; its retail toll revenues have also declined by $25.1 million during the year ending December 31, 2002.[6] Accordingly, to the extent that the Court reversed the $1.78 increase to local rates, we establish that increase by this order.[7]

The Public Advocate also argues:

> The Commission does not have the authority to set local rates at the start of an AFOR by adjusting those rates to account for one issue to the

---

[6] The June 22, 2003 AFOR Order required Verizon either to demonstrate that its toll losses were at least as great as those it predicted in the case, $19.8 million, or that it had reduced retail toll rates by that amount. On February 2, 2003 Verizon filed data showing a $25.1 million decline in retail toll revenues.

[7] Under this alternative, an argument might be made that the rate was not in effect between the date of the Court's decision and Part 1 of this Order. We make no ruling on such a hypothetical argument at this point, but note that both the filed rate doctrine (35-A M.R.S.A. § 309(1)) and the prohibition against retroactive ratemaking may prohibit refunds.

exclusion of all others. That is the essence of the Law Court's remand decision.

We do not agree. We believe the Court made abundantly clear that the Commission's authority to order an increase to local rates to offset required access rate decreases does not depend on conducting a comprehensive rate proceeding, but is in fact independent, and can be ordered at any time, without the need to consider other issues. The Court made no statements about the Commission's authority (or lack thereof) to change rates "to account for one issue to the exclusion of all others." The Public Advocate's reference apparently is to the doctrine or policy against "single issue rate cases." The Court did not address that doctrine in this case and, in fact, has never addressed that issue. The only decision that actually addresses the issue of "single issue" rate proceedings is a 1982 Commission decision, *New England Telephone and Telegraph Company, Proposed Increase in Rates*, Docket No. 82-6, Order of Dismissal (May 11, 1982).[8] In at least two cases, however, the Court has upheld Commission orders that permitted rate changes notwithstanding the lack of any examination of the utility's costs and other revenues.[9]

There is substantial precedent supporting Commission's action in this case. As noted above, the Court relied on its own prior decision in *New England Telephone & Telegraph Co. v. Public Utilities Commission*, 1997 ME 222, 705 A.2d 706 (*1997 NET v. PUC*) to support its decision that the Commission acted within its discretion in this case in allowing the increase in local rates to offset access reductions. In the 1997 case, the Court upheld the Commission's discretion to adopt and enforce (against NYNEX) a provision in Chapter 280, § 8 that required local exchange carriers to reduce access rates by 20 percent. The Chapter 280 requirement was unrelated to any other proceeding, including the existing Verizon AFOR.

The Commission also opened another proceeding in 1997 (a further rulemaking and inquiry) to address the need for Verizon, in 1999, to comply with

---

[8] *See* further discussion of "single-issue" ratemaking, and exceptions, at note 16.

[9] One of these is, of course, the 1997 appeal cited by the Court in note 2 of its opinion in this case, *New England Telephone & Telegraph Co. v. Public Utilities Commission*, 1997 ME 222, 705 A.2d 706 (*1997 NET v. PUC*). That case upheld the Commission's discretion to require NET to decrease access rates without an offsetting increase in local rates. *See also Public Advocate v. Public Utilities Commission*, 1998 ME 218, 718 A.2d 201 (*1998 Public Advocate v. PUC*), upholding the Commission's discretion to order a rate increase to offset revenues lost pursuant to required changes in basic service calling areas (BSCAs).

the access parity statute, 35-A M.R.S.A. § 7101-B.[10] Like the earlier rulemaking, the new proceeding was independent from any other proceeding. In the new proceeding, the Commission accepted a Stipulation that resulted in a $3.50 increase in local rates to offset access revenue losses, notwithstanding the AFOR pricing rule that effectively precluded increases to local rates.[11]

These prior cases, along with the Law Court's ruling in this case, establish that we may lawfully order a revenue-neutral change in local (or any other) rates to offset a legally-required changes in access rates, and that we can do so independently of other, more general rate proceedings or of an AFOR proceeding.

We also see nothing in the Court's opinion that would support the Public Advocate's argument (Brief p. 3) that:

> …the Law Court's earlier ruling does not apply here. The previous decision correctly held that a rate adjustment *during the term of an AFOR* is not always legally precluded. … [I]t did not, and could not, hold that an adjustment made in a materially rewritten AFOR Order is not subject to the express textual terms and conditions of the AFOR statute.

The "earlier ruling" referred to by the Public Advocate is the Court's decision in *1997 NET v. PUC.* The Court relied on that decision in footnote 2 of the opinion in this case. 2003 ME 23, ¶ 1 n. 2. Nothing in the Court's language in the present case suggests that the Commission's authority to order an increase to rates is limited to the middle of an AFOR. If the Court had intended such a limitation, it would have distinguished the 1997 case from the present case, rather than using it as precedent to support its present determination that the Commission "acted within its discretion."

---

[10] *Maine Public Utilities Commission: Proposed Amendment to Chapter 280 to Achieve Parity With Interstate Access Rates by May 30, 1999*, Docket No. 97-319, Notice of Rulemaking; Notice of Inquiry (June 10, 1997).

[11] The result was related to the AFOR only because it was necessary to waive the local rate pricing rule described in the text. Although the $3.50 increase did not cover all of the access revenue loss, under the operation of the AFOR's overall price cap (the PRI), any rate reduction, required or voluntary, could be (and nearly always was) implemented on a revenue-neutral basis. Thus, the access revenue loss was made up by the $3.50 local rate increase and by other rate increases.

The Public Advocate's purported distinction is also illogical. If the Commission had discretion in 1997 to order NYNEX to reduce access rates, *notwithstanding* the existence of the AFOR pricing rules that generally precluded either the utility or the Commission from changing rates, it seems likely that it would have even more discretion at the beginning or end of an AFOR, when no pricing rules were in effect. The 2001 rate increase to offset access revenue losses happened to *coincide* with the implementation of a revised AFOR. The original AFOR expired on May 31, 2001, and 35-A M.R.S.A. § 7101-B required Verizon to reduce access rates on May 30, 2001. The Public Advocate provides no reason why the order allowing the rate increase is *dependent* on the validity of the order creating the AFOR.

The Public Advocate concedes that it is lawful to take action concerning access rates and local rates in the middle of an AFOR, and also advocates a temporary return to the 1995-2001 AFOR, under which any rate change (including even a mandated access rate reduction) could be implemented on a revenue-neutral basis.[12] Illogically, the Public Advocate nevertheless apparently believes that such a revenue-neutral increase in rates is not possible when a mandated access reduction and the commencement of an AFOR happen to coincide. We decline to make this distinction.

Not only did the Court rely on (rather than distinguish) the prior precedent, it also provided no positive indication that the Commission could order the local rate increase only in conjunction with the reestablishment of the AFOR. Enforcement of the access parity statute, and the Commission's discretion and inherent authority (recognized in 35-A M.R.S.A. § 104 and in footnote 2 of the Court's opinion) cannot possibly depend on the existence of an AFOR. If that were the case, the Commission could not require any other local exchange carrier in the state, besides Verizon, to comply with the access parity statute.

The NOI in this case raised a more specific question about the possible "integration" of the local rate increase with other pricing decisions in the AFOR Order. In particular, the NOI asked whether the decisions that Verizon would not be permitted to recover expected retail toll revenue losses through a local rate increase, and that the retail toll losses would substitute for a formal productivity factor, created a level of integration that precludes the independent treatment of the rate increase.[13] The AARP argues that because of this integration, it is necessary to vacate the local rate increase.

---

[12] *See* note 11 and accompanying text.

[13] The Public Advocate's brief mentions, as another "integrating" factor, our finding in the 2001 AFOR Order that "allowing Verizon to increase its basic rates *by only a portion* of the amount necessary to offset the revenue losses from mirroring interstate access charges" partially satisfied the seventh objective in 35-A M.R.S.A. § 9103 (that the AFOR must "encourage the development,

We disagree with the AARP. As indicated in the NOI, the retail toll and productivity decisions were, in part, an attempt to balance the competing interests. Although we do not believe the Court ruled that the local rate increase was integral to the AFOR, we could nevertheless, on our own, conclude that the decision to order an increase to local rates was so connected to other decisions in the AFOR order that it is not appropriate to allow Verizon to retain the increase, at least while we reconsider whether we can reinstitute the AFOR on a permanent basis. We decline to take such an inequitable course. The primary reason for allowing the increase was our obligation to enforce the access parity statute, the significant revenue loss to Verizon resulting from our enforcement, and the fact that Verizon had little control over the loss. Indeed, as AARP points out, we treated the increase essentially as "exogenous," within the meaning of that term as defined in the 1995 AFOR Order. The "balancing" referred to by the AARP played, at most, a subsidiary role.*

In arguing that the Commission must conduct some form of revenue requirement determination before we can order a continuation of the $1.78 increase to local rates, the Public Advocate claims that:

> Section 9103(1) requires that the Commission compare two sets of local rates: the rates that will go into effect under the AFOR that is being contemplated, and the rates that would be determined in a traditional rate-of-return proceeding. An ROR analysis, by its very nature, requires a bottom-up determination of a cost-based rate for local service. Under rate-of-return (ROR) regulation, the "lost" access revenues may well be offset -- in whole, or in part -- by increases in the Company's other revenues, or by reductions in the Company's expenses, or costs of capital -- in which case the Commission could *not* then necessarily include the full (or any) amount of the $1.78 increase in the rates to be in effect for the new AFOR. [Footnote omitted]

There are two fatal flaws in the Public Advocate's argument. First, it assumes a connection between, or an integration of, the AFOR and the access rate - local rate issue. We have found that the access-local rate issue is

---

deployment and offering of new telecommunications and related services"). This "integration" is substantially less important than the pricing decisions discussed in the text.

* 35-A M.R.S.A. § 9103 (that the AFOR must "encourage the development, deployment and offering of new telecommunications an related services"). The fact that there is a tangential relationship between the price increase and the AFOR structure, however, does not require that the two must stand together or not at all. All decisions have context, but that does not create a regulatory "house of cards" where the failure of any one decision dooms all the rest.

independent form the AFOR, a conclusion we believe is fully consistent with the Court's order. Second, the OPA incorrectly assumes that Section 9103(1) requires a full "bottom-up" revenue requirement and revenue analysis, a position explicitly rejected by the Court. Standing alone, as the Commission and Court have concluded it may, the $1.78 offset to the access charge reduction requires no consideration of other factors that might, in a general rate case, increase or reduce the required net increase in basic rates.

While, of course, it is possible that a full revenue requirements case could have revealed changes in Verizon's cost structure that would have permitted Verizon to absorb the entire access (and related toll) revenue loss with a smaller increase in basic rates, it is just as possible that, had such a proceeding been conducted, that a *greater* increase would have been required. The *one* certainty concerning Verizon's revenues at the time the Commission allowed the $1.78 increase was the immediate reduction in access revenues. The $1.78 was set to create an offset of $12.5 million per year against a projected loss of $14.5 million.[14]

The OPA's reliance on what might have been shown in a full rate case is, in any event, misplaced. The Court clearly held that section 9103(1) does not require a full rate proceeding. 2003 ME 23 at ¶¶ 28-29. As shown above, the Commission is also not constrained – whether inside or outside an AFOR – from allowing an increase in basic rates to offset legislatively required reductions in access rates. The passage of time since the Commission's 2001 order has not diminished the Commission's authority nor altered the basic facts upon which the Commission relied in granting the increase.

The certainty of Verizon's access revenue loss has not changed since 2001. Verizon's access rates continue at the levels required by the statute. The related toll losses have actually exceeded the Commission's estimates. Thus, based on the record in this case and the absence of any intervening factor or event that suggests that basic rates would not have to be raised by at least $1.78 to offset the access reductions, we conclude that Verizon is entitled to continue to collect the rate currently in effect.

In summary, we believe that the Court's order did not invalidate the independent decision by the Commission, in 2001, to allow Verizon to increase its basic rates by $1.78 to offset the legislatively-mandated reductions in access

---

[14] Indeed, in a full "revenue requirements" review, Verizon would be able to claim not only a revenue loss of $14.5 million from access but an additional loss from reduced toll revenue related to falling access rates. As noted above, the toll loss was estimated at nearly $20 million per year, which, in a rate case, could have produced an additional increase to basic rates of nearly $2.80 per month.

charges. Even if that portion of the Commission's order was vacated along with the decision to implement an AFOR, however, the record in the case fully supports a decision, and we conclude today, that basic rates should be increased by $1.78 above the levels in effect prior to the Commission's 2001 order.

IV. INTERIM REGULATION

The Law Court "vacated" the AFOR order. As is normal practice for the Court in such cases, its entry stated only: "Order creating the alternative form of regulation vacated. Remanded to the Commission for further proceedings consistent with this opinion." The Court said nothing specific about the form of regulation during the period prior to completion of the proceedings following the remand.

It is clearly necessary, while we consider whether to implement a long-term AFOR, to determine the nature of regulation in the interim. In the NFR, we "tentatively concluded" that Verizon had not "reverted" to the previously existing AFOR (whether called the "old" AFOR or "phase one" of an ongoing AFOR), but that, in the absence of a validly existing AFOR, Verizon would revert to non-AFOR (i.e., rate of return) regulation under 35-A M.R.S.A. §§ 301-312; 1302-14. We suggested that the AFOR effective between 1995 and 2001 had expired. The original AFOR was originally in effect from December 1, 1995 to November 30, 2000 and was extended by an order in this docket to May 29, 2001.

There are three plausible choices for temporary regulation. One is a return to pre-AFOR "traditional" rate of return (ROR) regulation. Another is to re-implement the AFOR that was in effect from 1995 to May 29, 2001. The third is to require Verizon to adhere to the pricing rules and the SQI of the vacated AFOR. We order a combination of the first and third of these options.

The Public Advocate argues that Verizon has reverted to the previously existing AFOR, that the vacation of the order "wipes the slate clean," that the "previously existing status is restored as though the order had never existed," and that "Verizon should be placed back in the position it occupied before the *2001 AFOR Order* was issued, i.e., subject to the terms of the 1995-2001 AFOR." It is not obvious to us that Verizon necessarily must revert to the most recent form of regulation. The original AFOR had a specified term, which expired more than two years ago. The findings that justified our adoption of that AFOR necessarily were made with the explicit time horizons of that AFOR in mind. Although we anticipated that the original AFOR might be renewed, either with or without revisions, we failed in our attempt to do so. We believe that the Public

Advocate's position is not as compelling as the argument that we have reverted to rate of return regulation.[15]

Verizon states that the Commission in the NFR "observes" that Verizon is "now subject to 'normal' regulation under [35-A M.R.S.A.] §§301-312; 1302-14…." In Verizon's view, however, "normal" apparently includes alternative forms of regulation. Verizon argues:

> Under these statutes, the Commission has broad discretion to fashion the regulatory tools that are appropriate to its oversight of Verizon Maine. The Commission can and should…exercise its statutory authority by retaining core principles of the AFOR plan on an interim basis….

Verizon does not state the basis for its conclusion that the statutes governing "normal" regulation provide the Commission with "broad discretion" to implement what in effect amounts to a temporary AFOR. 35-A M.R.S.A. §303 states:

> **§303. Valuation of property for fixing rates**
>
> In determining just and reasonable rates, tolls and charges, the commission shall fix a reasonable value upon all the property of a public utility…which is used or required to be used in its service to the public within the State and a fair return on that property. In fixing a reasonable value, the commission shall give due consideration to evidence of the cost of the property when first devoted to public use and the prudent acquisition cost to the utility, less depreciation on each, and any other material and relevant factors or evidence, but the other factors shall not include current value. ….

Although the Commission may have some discretion under these statutes in fashioning the form of regulation, after it determines the value of a utility's property and establishes a reasonable return, the requirements of Section 303 appear to require a rate base and a rate of return. The statutes governing "normal" regulation do not appear to allow the Commission to establish an alternative form of regulation that departs substantially from "rate base - rate of return" regulation. The fact that the Legislature enacted the AFOR statute, which

---

[15] If the original AFOR really did survive, the OPA's argument that the $1.78 local rate increase should be eliminated collapses completely. As noted above in Part III, under the PRI and API of the original AFOR, Verizon would be permitted to offset any rate reduction with other rate increases that would produce the same amount of revenue. If the original AFOR remained in effect, the $1.78 increase is <u>precisely</u> analogous to the earlier $3.50 increase, made mid-term in the AFOR, to offset the 1999 access charge reduction.

both expressly authorizes the Commission to implement an AFOR and places limits on that discretion, is one indication that sections 301-312 and 1302-14 do not contain the unlimited flexibility argued by Verizon.

We decide that it is unnecessary to determine the form of regulation to which Verizon may have "reverted" or whether there is sufficient flexibility under 35-A M.R.S.A. §§ 301-312 and 1302-14 to fashion an interim alternative form of regulation. We conclude instead that 35-A M.R.S.A. § 104 confirms that we have sufficient authority and discretion to choose among the various alternatives for temporary regulation. 35-A M.R.S.A. § 104 states:

> The provisions of this Title shall be interpreted and construed liberally to accomplish the purpose of this Title. The commission has all implied and inherent powers under this Title, which are necessary and proper to execute faithfully its express powers and functions specified in this Title.

The most fundamental "express power and function" in Title 35-A is to ensure that a utility's rates are "just and reasonable." 35-A M.R.S.A. § 301. Another significant power and function is the authority to establish an alternative form of regulation for a telephone utility. 35-A M.R.S.A. §§ 9101-9103. In the course of that second function, it is necessary, because the Law Court vacated the Commission's Order establishing the 2001-2006 AFOR, to conduct further, corrective proceedings. Those proceedings necessarily take some amount of time, during which a regulatory vacuum is not possible. It would surely be unlawful to have no regulation at all. We find that we inherently have the necessary power to establish a temporary form of regulation in conjunction with our execution of the express powers and functions in Title 35-A to ensure just and reasonable rates and to determine whether to establish an alternative form of regulation.

We find that it is most reasonable, and least disruptive, to order a form of interim regulation that adheres to those features of the vacated AFOR that were not questioned on appeal and whose legality is not cast in doubt by the infirmity found by the Court. Those features include all aspects of the AFOR except those governing local rates. The Court ruled that the Commission's finding concerning *local rates* (that they would be no greater under the AFOR under traditional ROR regulation) was not sufficiently supported. We therefore believe that any re-implementation, even on an interim basis, of the AFOR's treatment of local rates is at least suspect. By contrast, the other features contained in the vacated AFOR are not directly related to the finding that the Court ruled to be inadequately supported.

Thus, while we do not "reinstate" the vacated AFOR, we order interim regulation consisting of the following features that were described in June 25, 2001 Order:

- ? Caps on operator services and directory assistance rates;
- ? Pricing flexibility for retail toll service rates;
- ? Pricing flexibility for optional services;
- ? The ability, with Commission approval, to change rates for exogenous changes[16]; and
- ? The Service Quality Index.[17]

We order this interim regulation based on our inherent and implied powers to enforce our express legal obligation to ensure just and reasonable rates and on the record in this proceeding developed prior to the June 25, 2001 Order.

As discussed above, we have strong doubts that we have "reverted" to the original AFOR, although we do not decide that question. We nevertheless reject interim implementation under the expired AFOR on policy grounds. A return to that AFOR would be far more disruptive than reimplementation of the

---

[16] The general ability to make rate changes for exogenous changes has been permitted by the Commission only as a feature of an AFOR or in conjunction with "stay-out" provisions in some rate stipulations. That ability is not well established in other contexts, particularly ROR regulation, where the policy against "single Issue rate cases" may apply. Under that doctrine, a utility cannot change rates to accommodate a major cost change without examining other changes in costs and revenues on the ground (at least under ROR) that it is not possible to ensure that rates are "just and reasonable" unless other costs and revenues are examined. *New England Telephone and Telegraph Company, Proposed Increase in Rates*, Docket No. 82-6, Order of Dismissal (May 11, 1982). (In that case NET proposed a rate increase to offset changes in depreciation rates, the expensing of station connections, and two wage increases.)

On the other hand, we have permitted rate changes for BSCA and access rate changes without an examination of other costs and revenues and without regard to the form of regulation. Both of these types of rate changes are revenue neutral, to offset changes in revenues that have occurred because of statutory requirements or orders of the Commission. Both types of changes have been specifically approved in decisions of the Law Court. *Public Advocate v. Public Utilities Commission*, 1998 ME 218, 718 A.2d 201; *OPA v. PUC/Verizon, supra.* Verizon is permitted to request rate changes for these reasons during the interim period, although that period should be long over before the addition of contiguous exchanges to BSCAs or any change in Verizon's rate groups.

[17] Our ordering of an SQI for Verizon in this proceeding, on an interim basis, should not be taken as an assertion of any general authority to order service quality indices in other (e.g. non-AFOR) circumstances.

uncontested features of the second, or revised, AFOR. In the vacated AFOR order, we found that the degree of regulation included in the original AFOR was not as necessary for Verizon during the subsequent period. The OPA, on appeal, did not object to that general conclusion.

We believe there are also practical reasons for rejecting a temporary return to the 1995-2001 AFOR. It would be necessary for Verizon to reinstitute the price index (the Price Regulatory Index or PRI) that served as an overall rate cap and to make an "annual filing" to establish that its overall rate level (measured by the Actual Price Index or API) did not exceed that level. Under the 1995-2001 AFOR, it normally took Verizon about three months to prepare its annual filings. We intend to complete this proceeding within that period. The pricing rules, for services other than local, and the SQI of the vacated AFOR are the *de facto* status quo. Since the remand, Verizon has taken no action that is inconsistent with those terms. It has not argued that they should not apply on an interim basis. Indeed, Verizon argued that the Commission should apply the "core principles" of the vacated AFOR. Notwithstanding the OPA's advocacy of an interim return to the 1995-2001 AFOR, the OPA also appeared willing to accept the pricing rules and SQI of the vacated AFOR during the interim. The OPA states that it:

> is willing to stipulate that the Service Quality Index (SQI) instituted by the *2001 AFOR Order* should remain in operation. We will also discuss with Verizon further stipulations that would put into place other features of the 2001 AFOR, including (a) caps on the rates for operator services and directory assistance, (b) pricing flexibility for optional services, and (c) pricing flexibility for retail toll.

In short, the Public Advocate has indicated a willingness to retain *all* of the features that constituted the vacated AFOR other than those governing local rates.

We impose no specific interim rules concerning rates for local exchange service at this time. It may become necessary, during the interim period, to decide whether Verizon is subject to price change rules inherent in the statutes governing rate of return (or "cost of service") regulation (35-A M.R.S.A. §§ 301-312 and 1302-1309) or whether we should order interim local rate cap and stay-out provisions similar or identical to those contained in the vacated AFOR. These questions may arise if a rate proceeding is filed[18] or some other

---

[18] While there is no bar to Verizon or persons subject to the provisions of 35-A M.R.S.A. § 1302 from filing a rate case or complaint about Verizon's local rates, we do not encourage such filings. We believe the resources of all parties are better spent in determining whether we can fashion an AFOR that meets the requirements of the law. Under the Court's ruling, some form of determination concerning cost of service may be necessary.

precipitating event occurs before we resolve the issues we must address on remand.

It is also possible that it may be necessary to consider whether rate increases should be allowed for changes to basic service calling areas (BSCAs), the possible elimination of rate groups[19], or further required access rate reductions.[20] We expect, however, to complete this proceeding prior to the BSCA changes and any changes in Verizon's rate groups.

Accordingly, we

O R D E R

1. That the rate increase in rates for local exchange service of $1.78 (implemented in June of 2001 to offset access rate decreases and access

---

[19] Under the BSCA Rule, Chapter 204, the Commission could order an increase in local rates in conjunction with expanding a BSCA. Pursuant to recent amendments to the BSCA rule, all BSCAs will include all contiguous exchanges. That expansion is not expected until December, 2003, which will be after the interim period in this case. If the Commission allows Verizon to eliminate rate groups, that event would probably occur at the same time as the BSCA expansion. Any elimination of rate groups would be on a revenue-neutral basis, so that rates for rate groups with smaller calling areas would increase and those for rate groups with larger calling areas would decrease.

[20] We discussed this possibility in the *2001 AFOR Order* at 18-19. We noted that future expected access rate decreases are likely to be much smaller than the 2001 decrease, that "their size may raise questions about whether they should be considered exogenous and subject to a pass-through in rates," and that Verizon was free "to decide whether it should seek to justify, under the rules of the revised AFOR, any changes to basic rates based on the 2003 access reductions." Recent changes to 35-A M.R.S.A. § 7101-B (effective on May 2 , 2003, pursuant to emergency legislation enacted by P.L. 2003, ch. 101) moved the next absolute deadline for reducing intrastate access rates to interstate levels to May 31, 2005. The statute, however, grants the Commission some discretion to order parity by an earlier date. We have opened a proceeding to require Verizon to propose a schedule for compliance with the amended statute. *Public Utilities Commission, Investigation of Compliance of Verizon Maine with Amended 35-A M.R.S.A. § 7101-B,* Docket No. 2003-358, Notice of Investigation (May 28, 2003). Verizon has filed a proposal to delay any further access rate reductions until May 31, 2005. A notice of an opportunity to intervene in that proceeding and to file comments about Verizon's proposal has been sent to carriers and other persons.

revenue loss required by 35-A M.R.S.A. § 7101-B) shall remain in effect until further order.

2. That between the date of this Order and the completion of proceedings following the remand by the Supreme Judicial Court, sitting as the Law Court, Verizon shall be subject to interim regulation as described in Part IV of this Order.

Dated at Augusta, Maine, this 11th day of July, 2003.

BY ORDER OF THE COMMISSION

_____

Dennis L. Keschl
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Diamond

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within **21** days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.