**BEFORE THE TENNESSEE REGULATORY AUTHORITY**

**NASHVILLE, TENNESSEE**

**November 30, 2007**

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| **IN RE:** | ) | |
| | ) | **DOCKET NO.** |
| **UNITED TELEPHONE-SOUTHEAST,** | ) | **06-00207** |
| **INC. D/B/A EMBARQ 2006 ANNUAL** | ) | |
| **PRICE REGULATION FILING,** | ) | |
| **INCLUDING THE REINITIALIZATION** | ) | |
| **OF ITS PRICE REGULATION INDICES** | ) | |

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**CONCURRING OPINION OF DIRECTOR RON JONES TO THE *ORDER APPROVING PRICE REGULATION FILING***

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The above-styled docket came before a panel of the Tennessee Regulatory Authority ("Authority") during an Authority Conference on November 20, 2006. At the Conference, the panel unanimously voted to approve the 2006 Annual Price Regulation Filing filed by United Telephone-Southeast, Inc. d/b/a Embarq ("Embarq") and Embarq's request to reinitialize its Service Price Index ("SPI") and its Price Regulation Index ("PRI"). I write separately because my reasoning for approving the reinitialization of the SPI and PRI differs from that of the majority and because it is my conclusion that the Authority should open a docket to update the *Price Cap Annual Filing Methodology* ("Methodology").

## I. RELEVANT LEGISLATIVE AND ADMINISTRATIVE HISTORY

In 1995, the General Assembly enacted Public Chapter 408. Section 10 of Public Chapter 408, now codified at Tennessee Code Annotated section 65-5-109, set forth the procedures for incumbent local exchange carriers ("ILECs") and the Authority to follow when implementing a price regulation plan. Pursuant to section 65-5-109(c), upon the filing of an application by an ILEC to implement a price regulation plan, the Authority is to set the initial rates on which the price

regulation plan is based. Subsection (c) further provides that the Authority may adjust the initial rates pursuant to Tennessee Code Annotated section 65-5-107, the universal service statute.

Also included in Section 10 of Public Chapter 408 and codified at Tennessee Code Annotated section 65-5-109(e) is a limitation on aggregate rate increases. Specifically, subsection (e) creates a maximum annual adjustment for aggregate revenues for basic local exchange telephone services and non-basic services. The calculation of the maximum annual adjustment amount is the focus of this docket.

Embarq became a price regulated company effective October 15, 1995.[1] On September 12, 1996, Embarq filed a tariff, which sought approval of a revenue adjustment pursuant to section 65-5-109(e) resulting from a proposed charge for directory assistance and proposed reductions in certain access charge rates.[2] In the course of considering the tariff, the Consumer Advocate Division of the Office of the Attorney General, Citizens Telecommunications Company of Tennessee, L.L.C., BellSouth Telecommunications, Inc., and AT&T of the South Central States, Inc. were granted leave to intervene.[3] On January 27, 1997, the parties filed a *Stipulation*. Attached to the *Stipulation* is the Methodology dated January 23, 1997. In the recitals of the *Stipulation*, the parties explain that the Methodology is to be "used by [Embarq] in determining its maximum price adjustments under T.C.A. Section 65-5-209(e)."[4] The Authority approved the Methodology at the February 4, 1997 Authority Conference.[5] In a subsequent order the Authority stated that it "approves the methodology and formula for use in calculating the amount of the annual price cap adjustment pursuant to T.C.A. 65-5-209(e) as stipulated to by the parties to this docket."[6]

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[1] *In re: Application of United Telephone-Southeast, Inc. for Approval to Implement Price* Regulation, Docket No. 95-02615, *Order*, 2 (Sept. 20, 1995 ).
[2] *In re: United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, *Order Approving in Part and Denying in Part Tariff No. 96-201*, 1 (Sept. 4, 1997).
[3] *Id.*
[4] *Id. Stipulation*, 1 (Jan. 27, 2006).
[5] *Id. Order Approving in Part and Denying in Part Tariff No. 96-201*, 3 (Sept. 4, 1997).
[6] *Id.* at 6.

The Methodology creates two indexes to use when determining compliance with section 65-5-109(e). The definition of the PRI describes the index as establishing "a ceiling on price changes, in the aggregate, for the Basic and Non-Basic Services categories."[7] The definition further provides that the "PRI, as of the effective date of Price Regulation, is one hundred (100)."[8] The definition of SPI describes the index as indicating "the cumulative annual percentage change in actual prices, by service category (Basic and Non-Basic), since the effective date of Price Regulation, or since the last resetting of the Indexes by the Tennessee Regulatory Authority."[9] Section IV.H. of the Methodology discusses resetting the indexes. The applicable provision states:

> The initial index prices are the service prices in effect on June 6, 1995 or as reset by the Tennessee Regulatory Authority under Tenn. Code Ann. 65-5-[1]07. If the PRI and SPI are reset by the Authority, the same proportional relationship will exist between these two indexes before and after the resetting process.[10]

No other provision of the Methodology discusses resetting the indexes.

In 2005, the General Assembly enacted Public Chapter 71 ("2005 Amendment"), which amended section 65-5-109 to allow price regulation utilities to rebalance certain revenues, expand local calling areas, and regroup rates. The newly enacted language as codified in section 65-5-109(f) provides:

> Nothing in this subsection (f) shall be construed to prohibit or limit residential basic local exchange rate increases or aggregate revenues permitted in subsection (e) caused by:
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> (1) Revenue neutral rate proposals that rebalance access revenue or touchtone revenue to residential basic local exchange service;
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> (2) Revenue neutral rate proposals that expand local calling areas; or
>
> (3) Rate regrouping when it is based on population growth or expanded local calling such that there is an increase in the number of lines that end-users within the rate group can reach by local calling and the rate group no longer corresponds to the rate group definitions in a carrier's approved tariffs.[11]

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[7] *Id. Stipulation*, Attachment - *Price Cap Annual Filing Methodology* at 2 (Jan. 27, 1997).
[8] *Id.*
[9] *Id.* at 2-3.
[10] *Id.* at 5 (The alteration of the original is due to a codification change reflected in the 2004 Replacement edition of Volume 11A of Tennessee Code Annotated.)
[11] Tenn. Code Ann. § 65-5-109(f) (Supp. 2007).

On August 14, 2006, Embarq filed a request to reset the PRI and SPI. Embarq relied on section IV.H. of the Methodology as support for resetting the indexes.[12] On September 13, 2006, Embarq revised its earlier filing by filing substitute documentation. In the September 13th filing, Embarq provided greater detail of its calculations and attached a copy of the Methodology. On October 12, 2006, Embarq requested that the Authority include Embarq's 2006 Annual Price Regulation Filing ("2006 Annual Filing") in this docket. Embarq explained that the calculations in the 2006 Annual Filing are based on the resetting of the PRI and SPI and that the 2006 Annual Filing contains no price changes.[13]

Given the filings, there are two issues before the Authority in this docket: (1) whether to approve Embarq's request to reset the indexes and (2) whether to approve the 2006 Annual Filing, which relies on the reinitialized indexes. In this Concurring Opinion, I address only the first issue as my decision on the second issue is accurately reflected in the *Order Approving Price Regulation Filing* filed in this docket on the same date as this Opinion.

## II. DISCUSSION

My initial concern with the filings was whether the Authority could reinitialize the indexes because, as Embarq contends, Embarq engaged in revenue neutral rebalancing activities. This concern developed from my reading of section 65-5-109(c) and Embarq's reliance on the Methodology as support for its request.[14]

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[12] Cover Letter from Laura A. Sykora to Chairman Kyle, dated August 11, 2006 (Aug. 14, 2006).
[13] Cover Letter from Laura A. Sykora to Chairman Kyle, dated October 11, 2006 (Oct. 12, 2006).
[14] Cover Letter from Laura A. Sykora to Chairman Kyle, dated August 11, 2006 (Aug. 14, 2006). In Pre-Filed testimony, Ms. Sykora responded to the question "[w]hy is it important to reinitialize the base year revenues now?" as follows:

> On December 1, 2005, the Company regrouped its exchanges and, on a revenue neutral basis, expanded its local calling scopes and eliminated the residential touch tone charge. The revenue neutral rebalancing shifted approximately $5 million nonbasic revenues to the basic service category. Without reinitialization, the price regulation model would make it appear that the Company had merely increased access line rates in the basic category by $5 million without any offsetting revenue reductions.

Pre-Filed Direct Testimony of Laura A. Sykora, 4 (Nov. 9, 2006).

### A. THE METHODOLOGY

As previously discussed, the Methodology includes language regarding the setting and resetting of the initial index prices. The pertinent language in section IV.H. of the Methodology defines the index prices as the "service prices in effect on June 6, 1995 or as reset by the Tennessee Regulatory Authority under TCA 65-5-[1]07."[15] There is no other allowance in the stipulated Methodology permitting the resetting of initial index prices. Thus, it is my conclusion that the Methodology as currently drafted does not permit Embarq to reset the indexes for the reason it has given, that is, revenue neutral rebalancing.[16] So, the question then is whether the TRA has the authority to otherwise reinitialize the indexes.

In the *Order Approving Price Regulation Filing*, there is very little discussion of the request to reset the PRI and the SPI. However, the order does reflect that the majority found that the 2006 Annual Filing, which includes the calculations using the reset indexes, "complied with the approved methodology."[17] The majority does not reference any particular provision of the Methodology in support of its conclusion, and as I explained in the preceding paragraph, in my opinion there is no provision to cite. Given my conclusion that the Methodology does not permit Embarq to reset the indexes for the reason it provided, it is my opinion that the majority's justification for approving the request to reset the indexes is not supported by the unequivocal language of the Methodology, and therefore, I must reject that justification.

### B. TENNESSEE CODE ANNOTATED SECTION 65-5-109

After thorough review of the Methodology, I next turned to the section 65-5-109 to determine whether this statute permitted the Authority to reset the indexes for the reason offered by Embarq. My initial conclusion focused on the language of 65-5-109(c), which provides that the

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[15] *In re: United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, *Stipulation*, Attachment - *Price Cap Annual Filing Methodology* at 5 (Jan. 27, 1997).
[16] Pre-Filing Direct Testimony of Laura A. Sykora, 3 (Nov. 9, 2006).
[17] *Order Approving Price Regulation Filing*, 3 (Nov. 30, 2007)

initial rates for a price regulation plan are those established through consideration of a price regulation application in accordance with section 65-5-109(c). The only explicit mention in section 65-5-109 of adjusting these initial rates references section 65-5-107. This statute is Tennessee's universal services statute and is not applicable to this case.[18] Thus, at this point in my analysis, I determined that 65-5-109 prevented the requested action.

I continued my analysis, however, and after further examination determined that not only does the panel have the authority to reset the indexes under the circumstances here, but in fact must take some action to ensure revenue neutral rebalancing efforts do not affect a utility's maximum annual adjustment amount calculated pursuant to section 65-5-109(e). To explain, the 2005 Amendment to section 65-5-109 allows a utility to take certain actions to adjust rates while at the same time preserving the utility's ability to increase rates by the full amount permitted by the maximum annual adjustment as calculated by 65-5-109(e). A reasonable approach to preserve this ability is to somehow adjust the calculation of the maximum annual adjustment amount to account for any rate adjustments caused by actions taken pursuant to the 2005 Amendment. Thus, it is necessary when a utility acts pursuant to the 2005 Amendment for the Authority to take steps, such as reinitializing the indexes, to ensure the proper calculation of the section 65-5-109(e) maximum annual adjustment amount.

It is my understanding from the testimony filed in this docket that the request to reinitialize the SPI and PRI is necessitated by Embarq's decision in 2005 to regroup its exchanges, expand its local calling scopes, and eliminate the residential touch tone charge.[19] These actions are permitted by the 2005 Amendment. Therefore, Embarq is entitled to an adjustment necessary to ensure the proper calculation of the maximum annual adjustment amount.

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[18] *See* Tenn. Code Ann. §§ 65-5-107 (2004 Repl.), 65-5-109(c) (Supp. 2007).
[19] Pre-Filing Direct Testimony of Laura A. Sykora, 3 (Nov. 9, 2006).

It is my opinion that Embarq's proposal to accomplish the adjustment through a reinitialization of the indexes while maintaining the relationship of the indexes is a proper means for ensuring the proper calculation of the maximum annual adjustment amount. The proposed approach is consistent with the Methodology, although not specifically provided for, in that the Methodology requires that when index prices are reset pursuant to section 65-5-107, the "the same proportional relationship will exist between these two indexes before and after the resetting process."[20]

## III. AMENDMENT OF THE METHODOLOGY

It is my conclusion that the request to reinitialize the SPI and PRI should be granted. The 2005 Amendment to section 65-5-109(f) places a duty upon this agency to ensure the proper calculation of the 65-5-109(e) maximum annual adjustment amount and Embarq's proposed calculation approach is acceptable. Despite this determination, however, as previously discussed, I am also of the opinion that the requested reinitialization is not provided for in the Methodology. Currently, the Methodology does not permit the Authority to reset the indexes as a result of Embarq's decision to exercise the options afforded it by the 2005 Amendment. In other words, the Methodology is stale.

It is incumbent upon this agency to ensure that policies are updated to reflect the current regulatory environment and that alterations to previously established policies are memorialized in a manner that will leave a trail for future research efforts. In order to further such efforts, it is my opinion that a docket should be opened to amend the Methodology to provide for the provisions of the 2005 Amendment to section 65-4-109. In addition, during the course of my study of this docket, I discovered that in Docket No. 98-00626 the Authority took certain actions to adjust the

[20] *In re: United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, *Stipulation*, Attachment - *Price Cap Annual Filing Methodology* at 5 (Jan. 27, 1997).

section 65-5-109(e) maximum annual adjustment amount[21] and the Methodology did not at that time and does not now provide for the adjustments.[22] Based on this, it is my opinion that the newly opened docket should consider, in addition to the 2005 Amendment, the adjustments ordered in Docket No. 98-00626.

## IV. CONCLUSIONS

Based on the foregoing, I agree with the majority's conclusion that the indexes should be reset, but disagree that the reason for doing so is because the request complies with the Methodology. I further conclude that a docket should be opened to update the Methodology.

Ron Jones, Director

[21] In Docket No. 98-00626, the Authority found that it was contrary to section 65-5-108(c) (then 65-5-208(c)) and the public interest to allow United to recover a reduction in the revenues it received from an affiliate through rate increases to consumers. To give meaning to this finding, the Authority directed United to "remove the directory listing revenues received from its affiliate publishing company from the base year and current year calculations." *In re: United Telephone Southeast, Inc., Tariff to Reflect Proposed Changes Under Price Regulation Plan*, Docket No. 98-00626, *Order Reflecting the Decision Regarding the 1998 Price Regulation Plan Adjustment for United Telephone-Southeast, Inc.*, 17 (Oct. 13, 1999). In this same docket, the Authority ordered United to restate the base year (1995) revenues to "reflect the access rate reduction made for the removal of the payphone subsidy." *Id.* at 19. The Authority reasoned that failing to adjust the base rates would be inconsistent with 47 U.S.C. § 276(b)(1)(B) and 65-5-108(c). *Id.* at 19-20.

[22] My comments should not be construed as critical of the ordered adjustments. My intention is only to point out that, as is the case here, there is no provision in the Methodology allowing for the adjustments.