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Reply to:
Consumer Advocate and Protection Division
Post Office Box 20207
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November 9, 2001

Mr. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

RE: Joint Petition of Crockett Telephone Company, Inc., Peoples' Telephone Company, West Tennessee Telephone Company, Inc., and the Consumer Advocate and Protection Division of the Office of the Attorney General for the Approval and Implementation of Earnings Review Settlement
Docket No. 99-00995

Dear Mr. Waddell:

Enclosed please find an original and thirteen copies of the State of Tennessee Attorney General's Concluding Brief Supporting the Joint Petition of the TEC Companies and the Consumer Advocate and Protection Division for Approval of the Earnings Review Settlement in the above-referenced docket for filing. If you have any questions with respect to this matter, kindly contact me at (615) 532-3382. Thank you.

Sincerely,

Shilina B. Chatterjee

Shilina B. Chatterjee
Assistant Attorney General

cc: Richard Collier, Esq.
Jack W. Robinson, Esq.
T.G. Pappas, Esq.
R. Dale Grimes, Esq.
Val Sanford, Esq.
Jim Lamoureux, Esq.

SBC:sc
Enclosure

BEFORE THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

IN RE: JOINT PETITION OF TEC COMPANIES AND THE CONSUMER ADVOCATE DIVISION FOR APPROVAL OF EARNINGS REVIEW SETTLEMENT	))))	**Docket No. 99-00995**

ATTORNEY GENERAL'S CONCLUDING BRIEF SUPPORTING THE JOINT PETITION OF THE TEC COMPANIES AND THE CONSUMER ADVOCATE AND PROTECTION DIVISION FOR APPROVAL OF EARNINGS REVIEW SETTLEMENT

INTRODUCTION

The Attorney General of the State of Tennessee, by and through the Consumer Advocate and Protection Division ("CAPD") of the Office of the Attorney General and Reporter for the State of Tennessee ("Attorney General"), submits this brief in support of the Joint Petition of TEC Companies for Approval of Earnings Review Settlement.

DISCUSSION

I. THE AMOUNT OF OVEREARNINGS IDENTIFIED IN THE SETTLEMENT AGREEMENT FOR THE TEC COMPANIES FOR THE YEARS 1999-2001 IS CORRECT

The Attorney General respectfully submits that the first matter concerning overearnings of the TEC Companies identified in the settlement agreement is correct. The overearnings is correct since it is the result of extensive evaluations, reviews and calculations that were made based on what was known and the reasonably anticipated changes that could occur as they relate to the TEC Companies.[1]

The calculations of the overearnings identified in the Settlement Agreement for the TEC Companies for the years 1999-2001 is just and reasonable. The testimony filed by the various

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[1] *See* Direct Testimony of Robert T. Buckner filed September 7, 2001, p. 4.

experts for the parties provide exhaustive evidence as to the accuracy and reasonableness of the settlement agreement. These experts extensively reviewed documentation and each independently determined that the calculation and analysis of the overearnings was correct. There was no objection filed by the experts or the parties in this matter concerning the accuracy of the overearnings calculations. Each one of the parties experts made a thorough review of the calculations and provided filed testimony related to the overearnings. No objections were raised concerning the accuracy of the calculations that were made. Based on our assessment concerning the correctness of the overearnings and the evaluation revealed in the filed testimony by the experts, the CAPD believes that the overearnings identified in the Settlement Agreement for the TEC Companies for the years 1999-2001 is correct.

Additionally, the savings that have been realized as a result of this investigation and settlement concerning the TEC Companies is unprecedented.[2] As stated in the direct testimony filed by Robert T. Buckner, the ratepayers of the State of Tennessee will save $6.4 million over a three year period.[3] The Settlement Agreement that resulted in this matter was the product of an investigation that began in May 1998. Since that time, there have been reviews and analyses of various surveillance reports, responses to data requests, discovery, work papers, exhibits and various other documents. Furthermore, there was a significant amount of calculations and review that was performed by various analysts in the CAPD. After a thorough review and negotiation period, a settlement agreement was finally reached between the TEC Companies and the CAPD.

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[2] *See* Direct Testimony of Robert T. Buckner, September 7, 2001, p. 4, lines 3-4.

[3] *See* Direct Testimony of Robert T. Buckner, September 7, 2001, p. 4, lines 3-4.

The settlement agreement was the result of known and reasonably anticipated changes.[4] It may not be feasible to reach a settlement that is "correct" in every respect. Rather, rate provisions that anticipate reasonably ascertainable and highly probable cost levels during the actual periods of rate use are essential to the successful pursuit of setting prospective rates to recover prospective costs.[5]

Moreover, direct testimony provided by Dwight S. Work of the TEC Companies clearly stated that forecasted amounts fairly present the future results and are reasonable when taken as a whole and considering past performances.[6] The calculations were a reasonable estimate of anticipated rate base and operating results for the forecast period.[7]

Further, the actual results were compared with the forecasted results for a thirty-month period ending June 30, 2001.[8] Mr. Dwight Work of the TEC Companies provided extensive calculations in his Direct Testimony that was filed on September 7, 2001. These calculations were reviewed by all interested parties and no objections were raised.

In addition, AT&T's discovery requests and their own filed direct testimony do not indicate that they object to or have issue with the settlement amount in any way. This provides further support that the accuracy of the amount of overearnings is not a matter of contention and

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4 *See* Direct Testimony of Robert T. Buckner, September 7, 2001, p. 4, lines 14-15.

5 *See* Direct Testimony of Robert T. Buckner, September 7, 2001, p. 4, lines 15-16 (*citing* Accounting for Public Utilities, Robert L. Hahne and Gregory E. Aliff, Accounting for Public Utilities [New York: November 1993], p. 8-4.

6 *See* Direct Testimony of Dwight S. Work, September 7, 2001, p. 3, lines 5-7.

7 *See* Direct Testimony of Dwight S. Work, September 7, 2001, p. 3, lines 11-13.

8 *See* Direct Testimony of Dwight S. Work, September 7, 2001, p. 3, lines 15-16.

is reasonably correct. In addition, when the Tennessee Regulatory Authority ("TRA") asked AT&T whether they contest the amount of over-earnings for 1999-2001 as referenced in the settlement filed by TEC and the CAPD. AT&T's response in their May 21, 2001 stated "AT&T has accepted that amount for settlement purposes."[9]

II. THE RATE DESIGN DESCRIBED IN THE SETTLEMENT AGREEMENT SHOULD NOT BE AMENDED IN ANY MANNER SINCE IT IS JUST AND REASONABLE AND AFFORDS THE RATEPAYERS OF THE STATE OF TENNESSEE SIGNIFICANT SAVINGS

The telecommunications industry has changed significantly since the 1980's, however, little has changed with respect to the purpose of access charges since the March 17, 1988 Order in Tennessee Public Service Commission Docket No. U-87-7492 (the "Megacom Order"). While the directives from the Federal Communications Commission ("FCC")[10] propel the industry and regulators toward change, the regulatory precedent and present policy are the same. Access charges were designed to compensate local telephone service providers for their overall costs and to keep local rates down.[11] The Joint Petition reflects precisely how an over earnings situation should be handled, it reflects the present state of regulatory law now and as it was when the Joint Petition was originally filed.

On the issue of rate design, AT&T just misses the point. Access charges are not set based on cost of the specific rate element. The entire infrastructure and the very existence of the local

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[9] Letter dated May 21, 2001 from Jim Lamoureux, Senior Attorney for AT&T.

[10] Docket No. 96-45, *In the Matter of Federal-State Joint Board on Universal Service*; Docket No. 00-256, *In the Matter of Multi-Association Group (MAG) Plan for Regulation of Interstate Service of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*; Docket No. 99-68, *In the Matter of Inter-Carrier Compensation for ISP-Bound Traffic*; and Docket No. 01-92, *In the Matter of Developing a Unified Intercarrier Compensation Regime.*

[11] Megacom Order.

telephone service provider must be taken into consideration. Rising local telephone service rates are likely. It is important that the TRA not divert to AT&T these late vestiges of assistance designed to help the consumer. Until the FCC and/or the TRA reaches the point of recognizing a different approach with generic and universal impact, the issues in the present docket are rather simple.

Most importantly, the access charges are related to all local exchange carriers operating in Tennessee and require an overall review by the TRA and should be applied to all companies operating in the State of Tennessee. AT&T should not be given more favorable treatment and be allowed to have their access charges eliminated merely because they intervened in this docket. Further, no other Interexchange Carrier ("IXC") has intervened in this matter and has participated in dockets where the access rates are at issue. On its own accord, the TRA stated that the access charge adjustment should be considered in Phase III of the Universal Service Docket along with all other potential services of the universal service sources of universal service subsidy.[12]

The most important impact that has occurred for AT&T is not that their access charges are too high but that they have successfully lobbied the legislature for deregulation of pricing. As a result of deregulation, AT&T stands to profit and increase their net income. In fact, their interest in this matter does not rest on their concern for ratepayers but, rather, their self-interest in obtaining significant savings in access charges. In fact, AT&T immediately raised their rates in long distance after detariffing resulted even though they claimed that detariffing would increase

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[12] Order of Tennessee Regulatory Authority dated May 25, 1999, p. 2.

competition and reduce prices.[13] In this docket, AT&T has no interest in reducing rates for ratepayers and it does not believe that it will have to pass on to consumers its savings related to access charge reductions as envisioned in the Megacom Order.

The settlement agreement between TEC and the CAPD does the most to benefit the TEC ratepayers and for that matter, rate payers period. The reductions of access charges to AT&T goes straight to their bottom line.

Moreover, AT&T is simply not a consumer with respect to the over earnings situation presented by the present matter. AT&T has offered neither theory nor authority supporting its idea of how it fits into the category of "consumer." AT&T's claim is clearly inconsistent with the definition found in TRA Rule 1220-4-2-.03 (1)(i). Rather "consumer" should be defined as it was obviously accepted in the previous over earnings review involving TEC.

The last earnings review of TEC resulted in an earnings reduction of $4.95 million in TRA Docket 96-00774. The rate design in that docket is quite similar to the one proposed in the current docket.

Moreover, this matter concerns a simple over earnings investigation which has been repetitively performed over the last decade. Further, no evidence has been presented by AT&T that suggests the TRA should treat this matter any differently than a simple over earnings investigation. As such, it would be appropriate to return to the rate payers through credits or refunds the amounts of the over earnings. AT&T's desired relief should not be considered in this docket because they are seeking access charge reform, as reflected in AT&T's filings in this

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[13] *AT&T Raises Rates*, CNN.COM (visited 11/08/01) <http://money.cnn.com/2001/06/01/companies/att/index.htm

matter.[14] Access charges and competition issues should be more appropriately considered in other dockets that are open before the TRA and the FCC. AT&T's approach has been more specifically addressed in previous filings by this office.[15]

AT&T's problem concerning access is universal in nature in that every access charge from an incumbent local exchange carrier ("ILEC") such as TEC is not based on cost. Under the Megacom Order, the charges are not to be based on cost. Therefore, the level of access charges and their costs should not be in this docket because it not an issue. AT&T should not be allowed to hold the TEC rate payers hostage in order to gain leverage over an issue not present in this docket.

Impact on competition is not the issue in this matter. The access charges are the same for each carrier. AT&T's stab at Vartec is a red herring. AT&T functions in the environment it has publicly sought for years . . . straight competition. It competes with Vartec on a comparable basis. It does not compete with TEC.[16] The arguments by AT&T concerning competitive pressures suggest little that changing the credits to refunds will not cure.

The TRA seeks to perform its duties consistent with the legislature's intent as interpreted by the TRA and/or the judiciary. In doing so, the TRA relies on the law, the facts and its own policy, which certainly include its own established policies. Consequently, AT&T is bound by the TRA's May 25, 1999 Order in the Access Charge Reform Docket, No. 97-00889. As noted

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[14] Statement of Issues by AT&T Communications of the South Central States, Inc., dated 6/5/00, pp. 1-3; AT&T Communications of the South Central States, Inc. First Set of Discovery Requests to the Consumer Advocate Division, dated 3/23/00, pp. 1-6.

[15] Consumer Advocate Division's Comments on AT&T's Statements of Issues, dated 6/14/00, pp. 1-5.

[16] *See* Rebuttal Testimony of Robert T. Buckner filed September 7, 2001, p. 7, lines 2-10.

by Director Malone at the May 15, 2001 TRA Conference, where the TRA has clearly spoken on an issue that issue should be consider resolved. AT&T's position in the present docket is unequivocally addressed in the TRA's decision of May 25, 1999 in the Access Charge Reform Docket No. 97-00889:

> If access rates are reduced, is it appropriate to do so in this proceeding or during the one time rate rebalancing phase in the Universal Docket as required by Tenn. Code Ann. § 65-5-207(c)?
>
> If access rates are reduced, it is appropriate to do so in the one time rate balancing phase of the Universal Service Docket (Phase III). Tenn. Code Ann. § 65-5-207 requires that the Authority consider access charges as part of universal service. Tenn. Code Ann. § 65-5-207(c)(8)(iii) states that, at a minimum, the Authority must consider intrastate access rates and the appropriateness of such rates as a significant source of universal service support. It does not, however, dictate whether this should be done in developing the universal support mechanism or during rate re-balancing. In Phase II of the Universal Service Docket, the Authority identified the amount of the universal service subsidy, while the purpose of rate rebalancing in Phase III is to identify rate adjustments needed as a result of the support mechanism created in Phases I and II. To facilitate the orderly handling of access charges, the Authority concludes that access charge adjustments should be considered in Phase III of the Universal Service Docket, along with all other potential sources of the universal service subsidy.

AT&T offers no reason to justify injection into the present docket of the broader issues more appropriately handled in the Access Charge Reform or the Universal Service dockets. The Attorney General does not object to AT&T's presentation of its claim for access charge reform. However, the present docket is not the appropriate place for presentation of issues that do not impact review of the TEC Companies' earnings.

From AT&T's complaint as set forth in its Petition for Intervention, it is clear that AT&T's purpose in intervening is to reduce the access charges it pays to TEC. This access charge issue, however, would be better handled in the Access Charge Reform Docket, No. 97-

00889, where all access charges, not just those involving one company, are at issue. Significantly, this Access Charge Reform Docket was initiated by AT&T and bears the caption: Petition of AT&T Communications of the South Central States, Inc. for the Convening of a Generic Contested Case for the Purpose of Access Charge Reform. Clearly, AT&T has recognized that access charges are best addressed on a state-wide rather than a piecemeal basis.

By an Order dated May 25, 1999, the TRA ordered that certain issues in the Access Charge Reform Docket should be considered in Universal Service Docket, No. 97-00888. Thus, the TRA has already recognized that changing access rates has an impact on other broader issues.

Ironically, AT&T came to the same realization at the October 4, 2001 prehearing conference regarding this matter. At the time, counsel for AT&T made the following admissions in its attempt to force TEC to respond to discovery requests:

HEARING OFFICER: 4, the subparts have been withdrawn. No. 5, the subparts have been withdrawn. No. 6. A and B appear to be a yes or no answer; C is giving a reason for that answer.

MR. COKER: Again, this goes to the validity of the rate design and whether it's appropriate to give a credit for a rate that's already priced below its cost. And also whether the TRA should

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do something, in this case, that could very well adversely affect the results of another case, the universal service case. And it goes to the reasonableness of the design.

HEARING OFFICER: How would that impact the universal service case?

MR. COKER: The question is, if basic local rates are effectively reduced from their current level by giving these credits, is that going to cause a need -- are they going to measure these lower rates even -- rates that are even further below cost in determining the universal service requirements.

If basic local service is already priced below its cost and that creates a need for a universal service fund, and you're reducing them even further, is that going to increase the need for universal service fund? Technically, universal service funds, you're looking at the cost of the deficit created between the revenues received for basic local service and its cost. So you're reducing the revenues here. And, like I say, it's basically a yes or no.

HEARING OFFICER: Would that issue not be reviewed by the TRA in the universal service docket?

MR. COKER: Well, in the universal -- for the universal service it would. But in planning

this rate design in this case, if it's their intent to say, Hey, basic local service rates, the revenues we're getting from basic local service is even further reduced by virtue of this agreement, I think that has a bearing on the reasonableness of this rate design if

this rate design is going to be used to increase the universal service requirements. Hopefully, it's not.

HEARING OFFICER: Is that the nut of the question?

MR. COKER: Yes.

HEARING OFFICER: Will this rate design be used --

MR. COKER: To increase the requirements for a universal service fund, the size of a universal service fund.

If the TRA follows AT&T's plan and reviews access charges in the present docket, there is a strong likelihood that precedents may be set with regard to access charges that would prejudice companies not parties to the present case.

AT&T's access charge claim should be transferred to the Access Charge Reform Docket, No. 97-00889, which is now also being considered in the Universal Docket No. 97-00888.

CONCLUSION

We strongly urge the TRA to approve the Joint Petition of the TEC Companies and the Consumer Advocate and Protection Division for the earnings review settlement. The amount of the overearnings for 1999-2001 as referenced in the settelment agreement is correct and the rate design described in the Settlement Agreement is proper and should not amended.

The Attorney General and AT&T agree that the present case is "separate and distinct" from the Access Charge Reform Docket. The present case is about the TEC companies and the money they owe their customers. Reducing AT&T's access rates has nothing to do with this focus. The present docket and the Access Charge Reform have different purposes, involve

different parties (in that the Access Charge Reform Docket is more inclusive), and raise different issues. This is an over-earnings matter. AT&T's interest in reducing access charges belongs in the Access Charge Reform Docket or the Universal Service dockets. AT&T will have all appropriate opportunities to persuade the Authority to reduce access charges in the Access Charge Reform Docket or the Universal Service dockets. Removal of AT&T from the present docket will not preclude it from pursuing access charge reform in the appropriate docket.[17]

The rate design should approved as proposed in the Settlement Agreement between the TEC Companies and the CAPD. The issue of access line charges should not be incorporated in the rate design. The CAPD and the TEC Companies have stated that the issues raised by AT&T did not belong in this proceeding.[18] The efforts of AT&T in this matter were to delay and wring additional profits out of the ratepayers of Tennessee consumers and therefore, the Joint Petition should be approved with all due speed.

RESPECTFULLY SUBMITTED,

Timothy C. Phillips by SBC

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[17] AT&T's argument to the contrary in its Reply to the Attorney General's motion is inaccurate.

[18] Transcript of Proceedings (June 9, 2000) pp. 17-18.

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November 9, 2001

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CERTIFICATE OF SERVICE

The undersigned certifies that on November 9, 2001, an exact copy of the foregoing was delivered via facsimile transmittal and mailed, via U.S. Mail, postage prepaid, to **Jack W. Robinson, Esq.**, Gullett, Sanford, Robinson & Martin, PLLC, 230 Fourth Avenue North, 3rd Floor, P.O. Box 198888, Nashville, TN 37219-8888; and **T.G. Pappas, Esq. and R. Dale Grimes, Esq.**, Bass, Berry & Sims, 2700 First American Center, 313 Deaderick Street, Nashville, TN 37238-2700.

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