15

(Decision No. C92-1377)

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

* * *

REGARDING THE APPLICATION OF THE MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY, D/B/A U S WEST COMMUNICATIONS, INC., FOR APPROVAL OF THE RATE AND SERVICE REGULATION PLAN.	DOCKET NO. 90A-665T DECISION AND ORDER ON APPLICATIONS FOR REHEARING, REARGUMENT, OR RECONSIDERATION

Mailing Date: November 4, 1992
Adopted Date: October 28, 1992

STATEMENT

BY THE COMMISSION:

We issued our decision in this matter on June 30, 1992. U S WEST Communications, Inc ("USW" or "Company"), Commission Staff ("Staff"), and the Office of Consumer Counsel ("OCC") filed timely applications for rehearing, reargument, or reconsideration ("RRR"). By previous order, and to forestall automatic denial of the applications by operation of law (§ 40-6-114(1), C.R.S.), we granted reconsideration. We now issue our decision on the applications for RRR.

As noted, infra, this decision largely confirms our previous determinations that the incentive regulation plan adopted in the original opinion is in the public interest. On reconsideration we have modified the approved plan in only a few respects. These are specified in the discussion which follows. In the applications for RRR, the Company, Staff, and OCC challenge certain elements of our approved plan, essentially rearguing a number of points rejected in the original decision, or reasserting arguments that an incentive regulation mechanism should or should not contain certain elements. For example, the Company takes issue with the reverse taper approved in our prior decision, arguing that negative scores on individual service quality should have no impact other than as part of the net score; the Company also protests our decision not to adopt a rate case moratorium as the quid pro quo for a Part 2 rate freeze; etc.[1] Staff [re]suggests that we incorporate the

[1]The Company can not have been surprised by the Commission's refusal to approve a rate case moratorium in the decision. Even before the commencement of hearings last year, we ruled on various motions to dismiss, and in that ruling notified the parties that the Commission lacked

cost/access line efficiency measure in an incentive regulation mechanism; that we approve certain modifications to the formal procedure when a USW customer complains about his telephone service; that we adopt a schedule for elimination of four- and eight-party service; that we adopt certain penalties for held service orders over 60 days' duration; etc. The OCC, in part, reaffirms its position that sharing should begin at a 12.5 percent return on equity ("ROE"), and that the quality of service criteria approved in the original decision (Exhibit A to Decision No. C92-854) are not reasonable and effective measures of quality of service.

In our prior decision, we gave careful consideration to these arguments, and made determinations adverse to the positions of the parties. We will not revise our rulings on these points since we are satisfied that our original rulings on these issues were fair and reasonable. Additionally, to the extent arguments contained in the applications for RRR are not specifically addressed in this decision, they are rejected.

MODIFICATIONS TO THE COMMISSION-APPROVED PLAN

The applications for RRR have convinced us that the plan should be modified in a few respects. First, the adopted plan requires USW to file a rate case when its ROE reaches 16.5 percent (page 41 of Decision No. C92-854). The Company points out that this requirement is potentially problematic. In light of our ruling that 100 percent of earnings in excess of 16.5 percent ROE will be "returned" to ratepayers, we accept the Company's request to eliminate this aspect of the plan.[2] The approved plan will be modified such that the Company will not be required to file a rate case when ROE reaches or exceeds 16.5 percent. In addition, we now clarify that the plan will not automatically end if the Company's earnings reach or exceed a 16.5 percent ROE. However, earnings at these levels may cause the Commission to initiate an investigation into USW earnings.

The Company also suggests that it should be able to opt out of the plan immediately if anyone initiates a rate case (i.e., a challenge to earnings) for the duration of the plan. Our previous decision provided that, in the event of a ratepayer challenge to Company earnings under AFOR, sharing of overearnings would continue until a final Commission decision on the case. We now amend the

---

proceeded to hearing, requesting that the Commission adopt an alternative to traditional regulation.

[2] Our use of terms such as "returning overearnings to ratepayers" has caused the Company to allege that the approved plan involves unlawful retroactive ratemaking. We address that argument infra.

plan in response to the USW request. In our initial decision we recognized that, in order for the plan to work, rate cases should not be initiated without due recognition of the potential benefits of the sharing mechanism (Decision, at page 43). Additionally, the approved mechanism requires the Company to surrender some of the benefits of regulatory lag inherent in traditional regulation by readjusting rates prospectively when earnings exceed authorized return. The Company is required to share overearnings even though we were unable to adopt a rate case moratorium. These circumstances convince us that, as a matter of equity and to discourage unnecessary challenges to USW earnings, the plan should be modified. Therefore, the Commission-approved AFOR will allow the Company to opt out of the plan immediately and return to traditional regulation in the event of a ratepayer-initiated rate case involving overall earning levels.[3] This means that the Company's obligation to share overearnings will end effective upon its choice to opt out of the plan as a result of a ratepayer-initiated case.

A final change to the adopted plan concerns quality of service. We are amending the prior decision insofar as the quality of service mechanism is concerned. Those changes are discussed infra.

CLARIFICATION OF PLAN

The applications for RRR request clarification of a number of elements of the plan. First, the Company and Staff present several questions involving financial aspects of AFOR. We now respond to these queries. The original decision (pages 41-42) explained that earnings under the plan would be measured using ratemaking principles and that the Company would be required to file earnings reports employing "book numbers" from the previous year. These directives require earnings and financial operations in general to be measured according to the principles and methodologies approved in Docket No. 90S-544T, the last Phase I involving USW. So, for example, any accounting or Commission-ordered disallowances or imputations approved in Docket No. 90S-544T should be used in AFOR.[4] In addition, the term "book numbers" in the original order refers to the monthly reporting ("MR") results discussed by Staff witness Mr. Jorgensen in his testimony (cite). The Company's application for RRR (Attachment A) as well as Staff's (Appendix A) contained illustrations of the parties' interpretation of the

---

[3] By "ratepayer initiated rate case" we are referring to rate cases, including complaints, initiated by parties such as the OCC or Staff.

[4] We do not mean that the actual amounts employed in 90S-544T will be used here, but rather that the principles and methodologies (absent pro forma adjustments) will be utilized in measuring financial operations under the plan.

original order. While we cannot confirm the accuracy of the calculations in those illustrations, it is apparent to us that each party has correctly interpreted the financial aspects of the plan as demonstrated in the attachments to the applications.

In its application, the Company also asserts that the $9,000,000 disallowance for affiliated transactions and rent compensation charges in Phase I was not based upon any methodology, but was a figure reached through compromise of the parties. Therefore, according to the Company, the Phase I decision from 90S-544T does not provide any guidance for purposes of quantification of the disallowance. We emphasize that the Phase I order does establish the principle that a disallowance for affiliated transactions and rent compensation charges is proper. In future measurements of USW financial operations under AFOR, we will proceed under the rebuttable presumption that $9,000,000 is the appropriate disallowance. The parties, including the Company, are free to attempt to rebut that presumption.

The parties have requested clarification regarding the duration of the negative rider which would be imposed to account for ratepayers' share of overearnings. It is our intent that the rider be in effect for one year, expire, and be replaced by a new rider, if any is required the following year. The rider would not establish a new base upon which subsequent riders would operate. Additionally, Staff requests that the sharing amounts be "pumped" for avoided taxes. We do not accept this suggestion.

In the initial decision, we provided for an evaluation of the plan midway through its term (Decision, at 38). The Company suggests that this mid-term review be used solely for evaluation and not for making substantive changes. We reject this request. In our view, an evaluation would be pointless if we were unable to make changes or adjustments which the review indicated should be made. However, we agree that, in the event major changes are made in the plan, the Company will be given the opportunity to withdraw from the plan at that point. We are not suggesting that the Company, at the present time, be forced to accept a plan which might be changed in unknown ways in the future.

In a related point, the OCC requests that we now specify the information which the Company will be required to file as part of the mid-term evaluation, as well as the time and procedure for that review. Our decisions in this case already specify the type of financial data to be examined when reviewing the Company's earnings. In addition, the decisions list particular information to be reviewed with respect to quality of service. We are unaware of any other specific information which we should now order the Company to file for a proceeding which is still years in the future, especially based upon the present record. Nor do we see a present need to specify the exact time and procedure for that proceeding. The parties are free to file appropriate motions and

pleadings in the future (in this docket) which address these issues. Those motions should make the specific suggestions contemplated by the parties. In any event, we do not see a need to specify all these matters in the present decision.

A number of questions have been raised as to how certain rate case filings by various parties will affect the plan. The initial decision is clear that Company filings for recovery of costs for post-retirement benefits, and SAFE- or RFIP-type programs will not terminate the plan.[5] With these exceptions, a rate case filing by a party may terminate the plan. We emphasize that, in light of the limitations upon our authority to approve a rate case moratorium, it is not our intent to absolutely preclude the filing of rate cases by any party authorized to do so, including the Company. The more important question relates to the consequences for sharing if a rate case is filed. As noted, supra, a ratepayer-initiated rate case will allow the Company to opt out of the plan and end its sharing obligation immediately. If the Company files a rate case, its sharing obligation will continue until a final Commission decision on the case (i.e., until a ruling on final applications for RRR). As part of the ruling on the Company-initiated rate case, the Commission will determine whether the plan should end before its five-year term.

The Company requests clarification as to whether it may opt out of the plan if unforeseen events occur or in the event the plan is changed. As implied in our discussion relating to the mid-term evaluation, no substantial changes will be made to the plan without giving the Company the opportunity to withdraw from the plan.[6] As for terminating the plan for unforeseen events, this decision clarifies that the Company may choose to revert to traditional regulation by a rate case (with its sharing obligation under the plan continuing until a final Commission decision is issued). This provision allows the Company sufficient flexibility to respond to unanticipated events.

Next, USW seeks the right to file for revenue neutral price changes for Part 2 and Part 3 services as an exception to the Part 2 rate "freeze". The Company represents that this request contemplates "minor adjustments" for "legal reasons (e.g., caused by the MFJ), public policy reasons (see, e.g., Docket No. 92S-295T, on toll restriction), or for other purposes" (USW application for RRR, page 37). According to the Company, such rate changes would be made only through the normal Advice Letter/tariff process, and only for the purpose of obtaining revenue neutral price changes.

---

[5] The decision also clearly states that we make no commitment that such rate requests will be approved. We see no need to decide now whether we will allow for piecemeal consideration of such requests. Those decisions will be made when the rate requests are filed.

[6] If USW withdraws traditional regulation will be reinstated and its sharing obligation will continue through the time of its choice to abandon AFOR.

We approve this request. However, we emphasize that this exception to the Part 2 rate "freeze" is solely for the type of minor and revenue neutral price changes referenced in the Company's application for RRR. The Company is authorized to submit these rate proposals to the Commission as an exception to the rate "freeze" and without placing the plan at risk of termination, and we reserve the right to deny these requests for any proper reason (e.g., the rate change may be found to be a violation of the spirit of this plan, and must be made in a general rate case).

Staff requests that Company reports and audit responses relating to the plan be filed under oath, and that the persons responsible for preparation of, and most knowledgeable about, the contents of the documents be identified. The request to identify responsible and knowledgeable persons in the Company, as related to AFOR reports and information, is reasonable and necessary. Therefore, we adopt Staff's suggestion. However, the request to compel filings under oath is rejected. We do not believe that such a requirement is necessary.

As for implementation of the plan, we modify the original decision and accept Staff's suggestion to begin using calendar year 1993 for the collection and assessment of data for purposes of sharing. The Company will be required to file the first earnings report, in accordance with the financial directives contained in our decisions, by April 30, 1994. Staff will complete its audit within 30 days of the filing.[7] Any interested party, including Staff, may request by June 1, 1994, that a hearing be held to determine disputed issues relating to the AFOR report.[8] If a request for hearing is made by any party, the hearing shall be held and concluded by September 1, 1994.[9] After hearing, the Commission shall issue its order in time for the negative rider, if any, to be implemented by January 1, 1995. The rider will apply to all Part 2 and 3 recurring rates. [10]This procedure shall apply for each of the five years of the plan's duration, unless modified by order of the Commission.

In its application for RRR, Staff questions whether the $10 rebate for missed installation appointments will be placed "above or below the line." Since these rebates would be given for failure of the Company to provide timely service, it is appropriate to place them below the line (i.e., the rebates will not be recovered in rates). With respect to the costs for the 800 hotline service ordered in the initial decision, these are legitimate costs of

---

[7] Interested parties may file discovery requests relating to the reports during this 30-day period. Such requests shall be answered within 20 days.

[8] As noted above, the parties may not relitigate principles or methodologies established in Phase I of Docket No. 90S-544T.

[9] Prehearing procedures (e.g., prefiling requirements) will be established at the time the hearing is set.

[10]Consistent with Staff's suggestion, the rider will not be applied to nonrecurring charges.

providing service, and, therefore, prudently incurred costs for the hotline will be treated as valid ratemaking expenses.

QUALITY OF SERVICE

Many of the comments made in the applications for RRR relate to our determinations on quality of service. In large part, the three applications for RRR follow a common theme: the original decision left undetermined a number of issues regarding the quality-of-service mechanism. For example, we noted that certain criticisms leveled at Exhibit A, the approved quality-of-service measure, by American Telephone and Telegrpah Association ("AT&T") and the OCC appeared to be valid. Exhibit A was the result of a stipulation between Staff and the Company. However, even those two parties were unable to agree to an acceptable survey of customer opinion during years 2 through 5 of AFOR. Staff still objected emphatically to the use of customer service measurement ("CSM") and recommended that an acceptable alternative be developed after year 1. In light of these still undetermined issues the Company, in its application for RRR, requested that the quality-of-service issues be finally resolved. According to the Company, it cannot commit to AFOR while significant aspects of the quality-of-service mechanism are undetermined. The OCC makes similar arguments in its application.

We regard the factors and specific measurements listed on Exhibit A to the initial decision as reasonable measures of quality of service. Additionally, we believe our findings and conclusions are workable regarding quality-of-service scores and their effect on sharing (pages 52-54 of original decision are workable).[11] However, we believe rehearing should be granted to resolve outstanding issues regarding quality of service, and to allow parties to address suggested modifications to the scores and their effect on sharing, including the issues raised in Commissioner Nakarado's dissent.

A hearing will be held beginning on November 23, 1992, and continuing, if necessary, on November 24, 1992. The parties may offer additional criteria or standards which they believe are appropriate for inclusion in the quality-of-service mechanism (e.g., the factors which have already been suggested by AT&T and the OCC). In addition, the parties shall address the issue regarding a replacement for the CSM. Finally, the parties shall

[11]Staff and the Company insist that the proportionate change concept approved in the decision is unworkable. We do not understand the objections, since the method involves a simple calculation. In the event the parties simply misunderstand our concept, we are attaching a detailed explanation (Attachment 1). If, after considering the attachment, Staff and the Company still believe the concept to be unworkable, they may explain their objections in the hearing we are setting in this order.

also suggest how all factors, including those listed on Exhibit A, shall be weighted for purposes of determining sharing amounts under AFOR.

In light of the hearing dates, parties may begin discovery immediately. Response time for interrogatories shall be ten days. The parties shall file summaries of their testimony, including suggested replacements for CSM, by November 16, 1992, with direct and cross examination to take place at hearing. It is the Commission's intent, based upon the rehearing, to finally resolve all issues relating to quality of service. After those determinations, the AFOR scheme will be completely defined.

Retroactive Ratemaking

We finally address the Company's contention that, even with prospective rate adjustments, the adopted plan involves illegal retroactive ratemaking. In its application for RRR, the Company asserts that the plan adjusts rates prospectively to make up for previous overearnings, and is therefore unlawfully retroactive. The Company is incorrect.

Although our decisions in this case often speak of "returning ratepayers' share of overearnings" via a rate reduction, this terminology was merely a shorthand reference for our decision to readjust rates prospectively in accordance with the approved formula. The plan does not reset rates in order to make up for past excess earnings. Rather, the plan adjusts rates prospectively, based upon the adopted formula (e.g., consideration of actual earnings, previously established ratemaking principles, and performance of quality of service), essentially eliminating some of the regulatory lag inherent in traditional regulation. This mechanism is similar to the use of a historical test year in traditional ratemaking--a practice which is well-established as being lawful. As such, the plan is not illegally retroactive. Our review of cases such as Colorado Energy Advocacy v. Public Service Company, 704 P.2d 298 (Colo. 1985) convinces us of the legality of the plan.

Moreover, the Company advances this argument as support for its theory that the Commission may not impose AFOR upon it. From this premise, the Company concludes that only if it consents to the plan will it waive its claims of illegal retroactivity and accept the plan. It is not our intent to impose incentive regulation upon the Company in this docket. Therefore, the assertion regarding unlawful retroactive ratemaking is largely academic.

THEREFORE THE COMMISSION ORDERS THAT:

1. The applications for rehearing, reargument, or reconsideration are granted consistent with the above discussion, and in all other respects are denied. The Commission-approved plan

for incentive regulation for U S WEST Communications, Inc., is modified in accordance with the discussion on pages 3 through 5.

2. The Commission-approved plan for incentive regulation for U S WEST Communications, Inc., is clarified consistent with the above discussion.

3. Rehearing in this matter regarding the quality of service issues referenced above is set for Hearing Room A, 1580 Logan St., Denver, Colorado, beginning at 9:00 a.m. on November 23 and 24, 1992. The parties may begin discovery immediately with response time to written discovery shortened to ten days.

4. The parties shall file written summaries of their testimony and any proposed replacement to the Company's customer service measurement seven days before hearing. Copies shall be served upon other parties at the same time.

5. Any proprietary information will be treated in accordance with the protective order previously entered in this case.

6. Applications for rehearing, reargument, or reconsideration to this Order shall not be due until after a Commission decision on rehearing.

This Decision is effective upon its mailed date.

ADOPTED IN OPEN MEETING October 28, 1992.

(S E A L)

ATTEST: A TRUE COPY

Bruce N. Smith
Executive Secretary

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

ROBERT E. TEMMER

GARY L. NAKARADO

CHRISTINE E. M. ALVAREZ

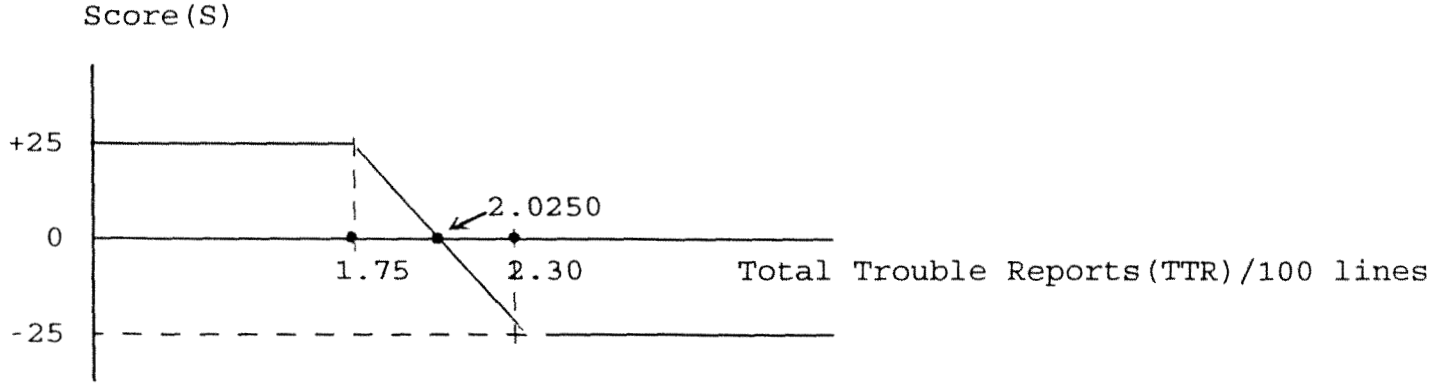
Commissioners

THE COMMISSION-ORDERED CONSTRUCTION OF A SERVICE QUALITY INDEX IN THE USWC AFOR PLAN (DOCKET NO. 90A-665T)

This attachment is designed to demonstrate the Commission-ordered, straight-line approach to the construction of each component of the service quality index.

To do so, numbers will be used from the first year of the plan for the criterion, total trouble reports/100 lines. This criterion is chosen at random; everything said here is equally applicable to the others.

This criterion is assigned a weight of 25%. The utility will receive a score of +25 if the number of total trouble reports/100 lines is equal to or less than 1.75 and the score will be -25 if the number of total trouble reports/100 lines is equal to or greater than 2.30. Using the Commission-ordered, straight-line approach, we have the following graph:



The equation for this straight line is

$$S = 25 - (TTR - 1.75)\left[\frac{(25)(2)}{2.30 - 1.75}\right]$$

$$= 25 - (TTR - 1.75)\ (90.91)\ .$$

Using this equation to generate the scores from the Commission method, we get the following table:

TTR/100 lines	Commission Score
1.75	25
1.80	20.45
1.85	15.91
1.90	11.36
1.95	6.82
2.00	2.27
2.05	-2.27
2.10	-6.82.
2.15	-11.36
2.20	-15.91
2.25	-20.45
2.30	-25

This concludes the demonstration of the Commission-ordered method.

G:\MARQUEZ