ISSUED June 7, 2006

# BEFORE THE PUBLIC UTILITY COMMISSION

# OF OREGON

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| In the Matter of<br><br>QWEST CORPORATION, fka U S WEST COMMUNICATIONS, INC.<br><br>Application for an Increase in Revenues. | )<br>)<br>)<br>)<br>)<br>)<br>) | MEMORANDUM |

The current proceedings in this docket are intended to implement the remand of Commission Order Nos. 01-810 and 02-009 required by the Court of Appeals' decision in *Northwest Public Communications Council v. Public Utility Commission of Oregon*, 196 Or. App. 94, 100 P.3d 776 (2004) and the subsequent judgment of the Marion County Circuit Court remanding the case to the Commission.[1]

The Court of Appeals determined that the rates established by the Commission for Public Access Lines ("PAL") did not comply with certain federal requirements. The Court also determined that the Commission did not adequately consider whether Qwest Corporation's (Qwest or the Company) proposed rates for CustomNet service were subject to the same federal requirements. The Court reversed and remanded the orders for further consideration by the Commission.

On March 31, 2006, pursuant to the schedule established in this proceeding, Qwest filed proposed rates for Public Access Lines and Fraud Protection (formerly known as CustomNet) in order to comply with the federal requirements for those rates as mandated by the Court of Appeals' decision. Qwest's proposed rates are lower than the rates approved by the Commission in Order Nos. 01-810 and 02-009.

Qwest argues that the Court of Appeal's remand order and ORS 756.568 authorize the Commission to reopen this case and to adjust other rates to offset the alleged revenue reduction that results from approving lower rates for payphone services. In fact, Qwest maintains that the Commission must rebalance rates in order to provide the Company with the opportunity to recover its authorized revenue requirement and to avoid "impermissible single-issue ratemaking" that would occur if the Commission were to

[1] The Circuit Court's remand was entered in Case No. 02C12247 on or about May 19, 2005.

adjust only Qwest's rates for payphone services. Staff advances a number of arguments in opposition to Qwest's proposal.

After reviewing the arguments advanced by the parties, I find that there is another approach to analyzing this issue that may be dispositive of Qwest's request to rebalance rates in this docket. Since this analytical approach was not discussed in the opening briefs, the parties should have the opportunity to address the matter in their reply briefs. Accordingly, I have set forth this analytical approach in the form of a proposed decision that the parties may address in their reply briefs. The proposed decision is attached as Appendix A to this Memorandum. In entering its decision in this matter, the Commission will consider this issue, as well as the other arguments advanced by the parties.

Dated at Salem, Oregon, this 7th day of June, 2006.

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Samuel J. Petrillo
Administrative Law Judge

## APPENDIX A

**Proposed Commission Decision**

The fundamental flaw in Qwest's rate rebalancing proposal is that it ignores the terms of the revenue requirement Stipulation approved in Phase I of this docket. In executing the Stipulation, Qwest agreed that the Stipulation should be approved by the Commission "prior to all appeals of the order on the Stipulation having run their course."[2] Indeed, Qwest emphasized that it was making a "major" concession by acceding to Staff's insistence that the refunds incorporated in the Stipulation be issued despite the prospect of any such appeals.[3]

Section I.A. of Qwest's post-hearing brief in the Phase I proceeding describes the circumstances leading to the execution of the Stipulation in this case.[4] At pages 12-13, Qwest states:

> Although Staff and U S WEST reached an agreement in principle on August 5, 1999, several collateral issues had to be resolved before a Stipulation could be executed. Chief among these was U S WEST's refusal to make a refund prior to all appeals having run their course. Staff, however, insisted that the timing of the refund was critical, and insisted that refunds be issued despite any appeals. U S WEST made this concession, which Mr. Inouye describes as 'major':
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> > US WEST agreed to make the refund independent of whether another party appeals a Commission order approving the stipulation so as to eliminate the uncertainty of the current litigation and to allow the rate design portion of the docket to proceed so that permanent rates can be implemented. This is a significant concession by U S WEST. Generally the Company would not agree to proceed with a refund until opposing parties' opportunities for appeal have been exhausted. (Citing U S WEST Exhibit/175, Inouye/10:2-7.)

The foregoing language discloses that Qwest understood the possibility that the refunds and rate reductions authorized by the Stipulation and subsequent Commission orders could be reversed or modified on appeal. The Company also

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[2] Order No. 00-190 at 9.

[3] *Id.*

[4] Qwest Post-Hearing Brief, dated February 11, 2000.

understood that the stipulated revenue requirement would be used to establish permanent rates for basic and non-basic services under the price cap form of regulation that Qwest had elected in 1999.[5] Thus, the "major" concession Qwest made in agreeing to implement the Stipulation prior to resolution of any appeals was the Company's acknowledgment that a Court could require Qwest to make refunds and/or rate reductions in addition to those authorized by Stipulation, notwithstanding implementation of permanent rates.

Paragraph 5 of the Stipulation details the rights and obligations of the parties in the event the Stipulation is reversed or modified on appeal. It provides:

> Appeal of the Commission's Order. The parties recognize that the Commission's order implementing the terms of this Stipulation may be subject to suit pursuant to ORS 756.580 by any party aggrieved by the terms of said order (hereinafter in this paragraph 5 referred to as an 'appeal'). In the event of such appeal, the parties shall advocate that the court(s) should affirm said order. Despite the pendency of any such appeal, U S WEST agrees to implement the terms of Paragraphs 1 and 2 of this Stipulation, forty-five days after the Commission has finally disposed of any motions requesting rehearing and/or reconsideration of the order implementing the terms of this Stipulation. The parties further recognize that the order adopting the terms of this Stipulation may be reversed and/or modified on appeal. The parties further recognize that U S WEST's obligation to refund monies to customers and to reduce its ongoing rates may be modified on appeal, either by the issuing of a judgment incorporating or requiring different refunds or rate reductions, or by the Court of Appeals refusing to dismiss the Appellate Litigation. In the event that an order implementing the terms of this Stipulation is reversed or modified on appeal, the parties agree that U S WEST will be entitled to a credit for refunds and rate reductions made under Paragraphs 1 and 2 of this Stipulation against any such increased refund and/or rate reduction obligation imposed by a judgment reversing or

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[5]The 1999 Oregon State Legislature passed Senate Bill 622, now codified as ORS 759.400 *et seq.,* introducing a permanent price cap regulation option to replace rate of return regulation for telecommunications utilities electing that option. Qwest elected price cap regulation effective December 30, 1999. The legislation authorized the Commission to establish rates for basic services for utilities electing price cap regulation. In addition, ORS 759.410 provides for maximum prices (price caps) and minimum prices (price floors) for non-basic services. Qwest's initial price caps were those rates in effect at the time the utility elected price cap regulation. Pursuant to ORS 759.415, the initial price caps were adjusted by permanent price caps established in this docket, Qwest's pending rate case.

> modifying the order adopting the terms of this Stipulation or any subsequent order. Notwithstanding anything herein to the contrary, the parties understand that U S WEST does not waive its rights, if any, to seek recovery of any overpayments – whether in the form of surcharges or rate increases – in the event that U S WEST's refund and/or rate reduction obligation is reduced by a judgment reversing or modifying the order adopting the terms of this Stipulation or any other order. It is the intent of the parties to this Stipulation that the Commission's order implementing the terms of this Stipulation contain provisions implementing the terms of this Paragraph 5 and, in the event that the order does not contain provisions implementing this Paragraph 5, the order will be deemed to be materially different from the terms of this Stipulation.

Whereas paragraph 5 permits Qwest to seek a rate increase in the event a Court determines that Qwest's refund/rate reduction obligation should be *reduced*, it does not provide Qwest with the same opportunity where a Court finds that Qwest's obligation should be *increased*. In the latter circumstance, Qwest is limited to receiving a credit for refunds and rate reductions already made in accordance with the Stipulation. Conspicuously absent from paragraph 5 is any language indicating that Qwest is entitled to increase rates to offset any *increased* refund or rate reduction obligation resulting from an appeal of the Stipulation or other order. This omission stands in stark contrast to Qwest's specific reservation of rights in the event of a Court decision *reducing* its refund/rate reduction obligation. The asymmetry of those provisions constitutes the concession emphasized by Qwest in its Phase I testimony and post-hearing brief. That is, the language of paragraph 5 makes clear that, by agreeing to accept only a credit for the refunds and rate reductions included in the Stipulation, Qwest deliberately relinquished the right to seek an offsetting revenue increase in the event of an adverse ruling on appeal.

In summary, Qwest specifically agreed to accept the risk that subsequent appeals of the Commission's order approving the Stipulation might result in a situation where Qwest was required to make refunds or rate reductions in addition to those set forth in the Stipulation. Qwest's own statements and the provisions of the Stipulation demonstrate that the Company was fully cognizant of the potential consequences of its decision when it executed the Stipulation.[6] Having acknowledged making a "major"

[6] There is no question that Qwest was aware that NPCC (formerly the Northwest Payphone Association or NPA) was challenging the refund mechanism in the Stipulation, including the claim that PAL refunds should be based on the FCC's payphone orders. See Order No. 00-190 at 15. The Commission stated that the existing record was insufficient to resolve NPCC's claims, which were subsequently addressed in the Phase II rate design orders implementing the Stipulation – Order Nos. 01-810 and 02-009. The situation posed by NPCC's appeal was contemplated by paragraph 5 of the Stipulation, which encompasses any "increased refund and/or rate reduction obligation imposed by judgment reversing or modifying the order adopting the terms of this Stipulation *or any subsequent order*."

concession by signing the Stipulation prior to the resolution of any appeals, Qwest cannot now be heard to complain that it is somehow prejudiced by having to reduce rates in response to a judicial determination specifically provided for in the agreement. The simple fact is that Qwest took a calculated risk that did not turn out as expected. Relieving Qwest of the consequences of its agreement by raising other customer rates would contravene the terms of the Stipulation.