

Approved: 2/16/94  
Date

## MINUTES OF THE SENATE COMMITTEE ON COMMERCE.

The meeting was called to order by Chairperson Alicia Salisbury at 8:00 a.m. on February 15, 1994 in Room 123-S of the Capitol.

Members present: Senators Burke, Downey, Feleciano, Gooch, Harris, Hensley, Kerr, Petty, Ranson, Salisbury, Steffes and Vidricksen

Committee staff present: Lynne Holt, Legislative Research Department  
Bob Nugent, Revisor of Statutes  
Mary Jane Holt, Committee Secretary

Conferees appearing before the committee:

Others attending: See attached list

### Staff presentation of telecommunication deregulation in other states

Lynne Holt, Legislative Research Department, informed the Committee that as of June 1993, 23 states had deregulated, partially deregulated, or streamlined regulation for some or all of the telephone companies operating in their jurisdictions. Twenty-six states had adopted incentive plans based on revenue sharing or profit sharing, price caps, or some combination thereof. In some states, the Legislature enacted legislation to allow public utility commissions to use alternatives to traditional rate-base, rate-of-return regulation, and to deregulate certain services because it was determined that such commissions, in contrast to the Kansas Corporation Commission, expressly lacked that authority. However, for the most part, the details of such alternative plans and deregulating procedures have been specified in commission orders and not in legislation.

Ms. Holt reviewed the laws in North Dakota, Idaho, Nebraska and Michigan, where legislation has been enacted to decontrol and, in some cases, deregulate certain telecommunications services. She also presented certain policy implications which may be derived from a review of these states' laws and from discussions with contacts in these states, attachment 1.

Copies of Selected Features of Alternative Telecommunications Regulation by State, attachment 2, and Southwestern Bell's Responses to Questions from Don Low's Testimony Regarding SB 591, attachment 3 were distributed to the Committee.

Ms. Holt, in response to questions, suggested the Committee may wish to incorporate more specificity into SB 591 to spell out the intent of TeleKansas II and expected outcomes. In Michigan the Legislature decided that certain things were going to be deregulated since competition existed. Nebraska and Michigan are required to report the effect of the impact of the laws that were enacted. She also noted there is no state strategy in Kansas, and other states reviewed do not appear to have had a plan at the time the deregulation occurred.

### Committee discussion on SB 591--Limited deregulation of the telecommunication industry

In response to Committee questions, Mr. Sciortino of Multimedia Cablevision replied they are regulated by local franchise as well as the FCC.

Ms. Fox, in reply to the question of why Southwestern Bell asked for SB 591 now, since TeleKansas I does not expire until sometime in February of 1995, stated they need some sort of stability in the way they are regulated. They are investing hundreds of millions of dollars in the infrastructure of the state. They have a plan that includes rural Kansas. They have to make their future construction decisions now in the current environment. The philosophy of the Kansas Corporation Commission changes with different administrations, and has changed since TeleKansas I began.

## CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON COMMERCE, Room 123-S Statehouse, at 8:00 a.m. on February 15, 1994.

The Chairman appointed a subcommittee on SB 591. The members are: Senator Salisbury, Chairman; and Senators Harris, Steffes, Feleciano and Hensley. The subcommittee will meet at 8:00 on Monday and Tuesday, February 21 and 22.

Senator Harris moved and Senator Steffes seconded to adopt the minutes of February 11, 1994. The motion carried on a voice vote.

The Chairman adjourned the meeting at 9:00 a.m.

The next meeting is scheduled for February 16, 1994.



# GUEST LIST

COMMITTEE: SENATE COMMERCE COMMITTEE

DATE: 2/15/94

NAME (PLEASE PRINT)	ADDRESS	COMPANY/ORGANIZATION
Don Grant	Topeka	KCC
Orlan Steppat	Topeka	PETE McGillivray Assoc.
BRIAN LIPPOLD	WICHITA	MULTIMEDIA HYPERION TELECOMMUNICATIONS
BEN SCIORTINO	WICHITA	Multimedia Cablevision
Brian Maline	VICC	KCC
Dana Bradbury	KCC	KCC
Karen Matson-Thanning	Topeka	KCC
Don Low	Topeka	KCC
Barbara Paschke	Topeka	Regents
Lora Powers	"	MCI
Tom Leason, Jr.	Lawrence/Ottawa	Indep. Telecom. Group
Harold Pitts	Topeka	NAACP-CCTF
Rob Holger	Topeka	Ks Telecom Assn.
TOM DAY	TOPEKA	KCC
Jim	Topeka	SWBT
Martha Jenkins	KCMO	Sprint
Mike Reecht	TOPEKA	ATT
Doug Smith	Topeka	SITA
R. Skoog	Topeka	KCHU/Ar
Frank Caro, Jr.	Topeka	Southwestern Bell
Michael Enns	Mission	C.M.I.
HELBY SMITH	Wichita	
Jim Shelley	Topeka	Southwestern Bell
Larry Dimmitt	Topeka	Southwestern Bell
SB Fox	TOPEKA	Southwestern Bell

## GUEST LIST

COMMITTEE: SENATE COMMERCE COMMITTEE

DATE: 2/15/94

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# MEMORANDUM

## Kansas Legislative Research Department

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Room 545-N -- Statehouse  
Topeka, Kansas 66612-1504  
Telephone (913) 296-3181 FAX (913) 296-3824

February 14, 1994

**To:** Senate Commerce Committee  
**From:** Lynne Holt, Principal Analyst  
**Re:** States with Deregulation Policies in Statutes

As of June, 1993, 23 states had deregulated, partially deregulated, or streamlined regulation for some or all of the telephone companies operating in their jurisdictions. Twenty-six states had adopted incentive plans based on revenue sharing or profit sharing, price caps, or some combination thereof.<sup>1</sup> In some states, the Legislature enacted legislation to allow public utility commissions to use alternatives to traditional rate-base, rate-of-return regulation, and to deregulate certain services because it was determined that such commissions, in contrast to the Kansas Corporation Commission, expressly lacked that authority.<sup>2</sup> However, for the most part, the details of such alternative plans and deregulating procedures have been specified in commission orders and not in legislation.

There are, nonetheless, a few exceptions. The intent of the first part of this memorandum provides a brief outline of laws in four states where legislation has been enacted to decontrol and, in some cases, deregulate certain telecommunications services. The states under consideration are: North Dakota, Idaho, Nebraska, and Michigan. The second part of this memorandum explores certain policy implications which may be derived from a review of these states' laws and from discussions with contacts in these states.

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<sup>1</sup>See National Regulatory Research Institute Update to the Maine and Missouri Reports on Alternative Regulation Plans in Telecommunications, ed. by Vivian Witkind Davis and Nancy N. Zearfoss, June 1993, p. i.

<sup>2</sup>See K.S.A. 66-1,188, which states: "The Commission is given full power, authority and jurisdiction to supervise and control telecommunications public utilities, as defined in K.S.A. 66-1,187, doing business in Kansas, and is empowered to do all things necessary and convenient for the exercise of such power, authority, and jurisdiction." The Commission construes its statutory broad authority to allow it to adopt alternative regulation policies and to deregulate telecommunications services.

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Commerce

Attachment 1-1

## Part I -- Legislation in Other States

An outline of each state's law is found below. This is by no means an exhaustive overview of those laws.

### I. North Dakota

**Law Enacted.** 1989; amended 1993.

**Companies Affected.** Any telecommunications company may elect not to be subject to rate of return regulation. For companies with over 50,000 subscribers (US West), the election is one-time and irrevocable.

**Method of Regulation.** The 1989 law separated services into "essential" and "nonessential." The definition of an "essential" service, which was modified in the 1993 legislation, refers to a "service that is necessary for switched access to interexchange telecommunications companies and necessary for two-way switched communications for both residential and business service within a local exchange area." A section was added to the 1993 law which defines nonessential services. Such services exclude essential services and apply to services "that a customer has the option to purchase either in conjunction with or separate from any telecommunications service." Specific services are outlined under the rubric of both essential and nonessential services.

Although companies participating in this regulatory plan must file rates for nonessential services, the North Dakota Public Utility Commission has no authority to regulate rates for nonessential services. The North Dakota law, in effect, also deregulates prices for essential services. Prices for such services may only be changed in accordance with a price factor. This price factor was changed by the 1993 law to tie rate increases to inflation through the GNP-PI. The price factor, which was replaced, had equaled an input cost index less one-half of a productivity incentive.

**Regulatory Oversight.** The North Dakota Public Utility Commission has essentially no authority to determine rates (other than being required to publish the telecommunications price factor on an annual basis), but it is authorized to investigate complaints concerning service quality and the reasonableness, fairness, and adequacy of any price for essential or nonessential service. The Commission also has authority to order remedies for deficient service and pricing violations.

**Cross-Subsidization.** Regulated essential or nonessential telecommunications services may not subsidize unregulated telecommunications services, and essential services may not subsidize nonessential services. Moreover, the price charged for an unregulated or nonessential telecommunications service must cover the cost of providing that service.

### II. Idaho

**Law Enacted.** 1988.

**Companies Affected.** The law applies to local exchange companies and interexchange carriers. Local exchange companies that choose to deregulate nonbasic local services must surrender their certificate of public convenience and necessity to be the exclusive provider of such telecommunications

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services for a designated geographic area.<sup>3</sup> Basic local services for residential and small business customers with five lines or less would continue to be price regulated. US West and AT&T are the only companies that have elected to participate in this regulatory plan.<sup>3</sup> The other interexchange carriers were already, in effect, operating under deregulation with respect to rates prior to enactment of this legislation.

**Method of Regulation.** The Idaho Public Utilities Commission has regulatory authority for the rates of basic local exchange services. The term "basic local exchange service" is defined as "the provision of access lines to residential and small business customers with the associated transmission of two-way interactive switched voice communication within a local exchange area." Local rates in effect have been frozen since enactment of this legislation. All telephone companies which provide intraLATA toll service, WATS service, or access to their local exchange network must file tariffs with the Idaho Public Utilities Commission. For other services, except local exchange services, there is no requirement for a company to file tariffs. The Commission requires providers of intraLATA toll services to average their rates for such service.

The 1988 law directed the Idaho Public Utilities Commission to develop a plan to allocate costs between regulated and (for rates) deregulated services. To date, such plan only pertains to US West. Under a plan approved by the Commission in 1989, US West and its ratepayers share increased or decreased revenues per access line based on the proportion of revenues collected from deregulated (approximately 60 percent) and regulated (approximately 40 percent) services. The revenue sharing plan uses 1987 revenue data to determine the "base year" average revenue per access line. If sharing year per-line revenue exceeds the revenue for the base year, a portion of the growth is attributed to regulated services. However, if the sharing year per-line revenue is less than the base year amount, regulated services are assigned a portion of the deficit. The ratio used to assign growth or deficit revenue is identical to the actual revenues generated by the regulated and deregulated services for the year to which the calculations apply. The sharing plan is not affected by an increase or a decrease in expenses except for changes mandated by the Federal Communications Commission, income tax changes, and a previously approved expense treatment for an upgrade program. Since the enactment of this law, the Commission has ordered several changes to the revenue sharing plan.

**Regulatory Oversight.** In addition to determining the method of allocating costs between regulated and (for rates) deregulated services and to making periodic adjustments, the Commission retains authority to investigate subscriber complaints on quality and availability of all services, intercompany disputes, and other administrative matters and to order remedies to resolve such disputes. The Commission also has access to utility records for all revenues to enforce the prohibition against subsidization by regulated telecommunications services of other telecommunications services. Finally, the Commission is authorized to review the revenue-sharing plan pertaining to US West and make necessary adjustments.

**Cross-Subsidization.** As in North Dakota, telephone companies in Idaho are prohibited from subsidizing their deregulated services with revenues from their regulated service.

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<sup>3</sup>According to Idaho Commission staff, the law is unclear as to whether telephone companies participating in this regulatory scheme would have to surrender their certificates of public convenience for basic local exchange service, particularly if customers have five lines or less, although it appears that they would not have to. According to Idaho Commission staff, it is particularly unclear whether the law allows for local exchange competition.

<sup>3</sup>Apparently, US West has not chosen to participate in this scheme for all LATAs in the state.

### III. Nebraska

**Law Enacted.** 1986; amended 1991.

**Companies Affected.** All telecommunications companies subject to regulation by the Nebraska Public Service Commission were removed from rate regulation; only the rates of basic local exchange services are subject to regulation.

**Method of Regulation.** Local rates are limited to a 10 percent increase within a consecutive 12-month period without Commission approval. Rates for other telecommunications services must be filed with the Commission and take effect after ten-days' notice. Interexchange carriers are required to average their toll rates on a statewide basis. (This requirement was scheduled to terminate on August 31, 1991, but was made permanent in the 1991 law.)

**Regulatory Oversight.** The Commission may review basic local exchange service on its own motion if rates increase in excess of 10 percent each year. Ratepayers may also initiate a Commission review of basic local exchange rates if a specified number of subscribers affected by a rate increase sign a petition. As a result of the 1991 law, the Commission may review windfall profits of local exchange carriers due to tax law changes. The Commission also retains authority to investigate complaints concerning quality of service, subscriber deposits, and service disconnection. Finally, the Commission is required to report annually to the Legislature on the quality of telecommunications service, the availability of diverse and affordable services to all Nebraskans, and the level of rates of local exchange companies and interexchange carriers.

**Cross-Subsidization.** There appears to be no specific prohibition in the statute against the subsidization of deregulated telecommunications services with revenue from regulated local services.

### IV. Michigan

**Law Enacted.** 1991; sunsets 1996.

**Companies Affected.** The regulatory scheme posited in the law affects certain services of local exchange companies. Entire companies are no longer regulated under this law.

**Method of Regulation.** Basic local exchange rates were frozen for two years (1992 and 1993) for all local carriers serving more than 15,000 access lines. There is a provision for very limited automatic alterations to the local exchange rate without Commission review. However, the Commission is required to hold a hearing on all other alterations in basic local exchange rates. The law affords residential subscribers the option of choosing flat rate basic exchange service, rates based on time duration of service usage or the distance between the points of service origin and termination, rates determined by service usage, or a combination thereof. Regulation of access rates is continued and access rates are capped at interstate rates for identical interstate services unless otherwise ordered by the Commission. Rates for business and residential intraLATA toll service are capped at levels effective on December 31, 1991, and are not, except under specific circumstances, subject to Commission regulation. As in Nebraska and Idaho, toll rates are averaged. Providers of toll service must implement discount plans for calling to exchanges within 20 miles of a customer's home exchange. Public and private educational institutions may own and operate telecommunications systems for educational purposes without being subject to regulation. Rates for interactive video and data services provided to educational institutions shall be subject to an open bid process.

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**Regulatory Oversight.** In addition to setting rates for regulated services as addressed above, the Commission is authorized to adopt policies and issue orders to exercise regulatory flexibility after making the determination that a competitive market for a regulated service exists in the state. The Commission also is authorized to deregulate a service if the Commission finds, after investigation and a hearing, that sufficient competition exists to protect the public interest. Furthermore, the law authorizes the Commission, upon complaint and after a hearing, to regulate new telecommunications services (which became available after the law took effect) that are considered adverse to the public health, safety, or general welfare, or quality of service. Other Commission regulatory responsibilities include: the establishment of a program to monitor the level of telecommunications subscriber connection within each exchange in the state; the establishment of standards for the quality of each telecommunications service; the investigation of complaints related to the quality, general availability, conditions, deposit requirements, or disconnection of a regulated service with authority to order changes; and determination of the conditions under which a provider of basic local exchange service may discontinue service. The Commission also was required to file a report to the Governor and Legislature on or before January 1, 1994. I received a copy of sections of the report from the Commission, including observations based on the Commission's experience with the law over an 18-months' period.

**Cross-Subsidization.** Basic local exchange rates or access rates may not subsidize or offset the costs of other products or services offered by a provider or an affiliate of the provider. To ensure that cross-subsidization does not occur, the Commission is authorized to review the books and accounts of the provider or an affiliate of the provider. However, according to a 1994 report by the Commission, "Commission access to information related to interexchange carriers beyond filed tariffs for regulated and unregulated services is virtually nonexistent. In some cases, the interexchange tariffs reflect only what they choose to file rather than what is required by Act 179."

## **PART II -- Preliminary Policy Implications**

The four laws addressed above vary considerably in their approach to accelerating the movement toward the decontrol and deregulation of telecommunications service. Several very preliminary observations may be in order.

1. Although the provisions of each law under consideration vary significantly, each law is much more detailed than S.B. 591.
2. In none of the laws are local exchange services deregulated. The determination of basic local service rates varies considerably: tied to an inflation factor in North Dakota; subject to an allocation formula in Idaho; may increase annually up to 10 percent subject to protest petition in Nebraska; and currently subject to Commission order except for limited automatic rate alterations under specified conditions in Michigan.
3. In all states, there is some regulation of services other than local exchange service to the extent that:
  - a. the regulatory commission has some capacity to investigate ratepayer complaints although the scope of that capacity and authority to seek remedies may vary; and

- b. the commissions are authorized to monitor activities under these regulatory schemes.
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- 4. It appears that all four laws provide varying degrees of rate flexibility for local exchange carriers and providers of intraLATA toll service.
  - 5. Although at least three of the laws expressly prohibit the subsidization of nonregulated services by local exchange services, it appears that only Idaho's law allows its regulatory commission access to a company's records of total revenues to both ensure that cross-subsidization does not occur and address such cross-subsidization. Whereas the Nebraska Commission has access to the company's records on total revenues, its authority is relegated only to review.
  - 6. There was no attempt made to obtain and analyze information in a systematic manner as to the degree of real competition that existed at the time these laws were enacted and the effect these laws have had on emerging technologies. However, this appears to be an issue that warrants further examination. An analysis of the existence of real competition might include, but not be limited to, such factors as: legislative and regulatory (federal law, state law, court decisions, state public utility commission orders, and Federal Communication Commission regulations) barriers; technologies; customer demographics (needs of customers, population density, and concentration of big customers).
  - 7. There have been questions about clarity in the laws reviewed in this memorandum. For example, according to Larry Garnatz, a spokesperson for US West in North Dakota, a lack of clarity in the statutes caused considerable contention for three years until the law was changed in 1993. The single item causing the greatest amount of contention was the formula for the essential telecommunications price factor which was subject to conflicting interpretations until the law was amended. In another example, the report by the Michigan Commission also raised a definitional issue about the meaning of "appropriate related costs," as that term refers in law to the costs educational institutions should be pay for telecommunications services. Time constraints prevented me from analyzing the issue of statutory clarity in any depth.

### III. SELECTED FEATURES OF ALTERNATIVE TELECOMMUNICATIONS REGULATION

STATE	AGREED TO UPGRADES	CPI ADJUSTED /AMOUNT	RATE OF RETURN RANGE	FREEZE ON BASIC	SERVICE STANDARDS	PRODUCTIVITY ADJUSTOR /AMOUNT	SHARING LEVELS RATEPAYER: COMPANY (R/P:CO)	TRIALS /LENGTH	ANY DETARIFFING, DEREGULATION, RATE FLEXIBILITY	COMMENTS
AL	N/A	N/A	11.65 - 12.30%ROC	Yes	Yes	No	Yes—above 12.3% ROC up to 50% sharing	Yes until 1/1/94	N/A	Local rate freeze only for low use measured service.
AK	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A		
AZ	N/A	N/A	13.75% No range	N/A	N/A	N/A	N/A	N/A	Law allows deregulation of non-essential services. Mobil, rural radio	
AR	N/A	N/A	Yes. Until 12/31/89	N/A	N/A	N/A	N/A	Yes. Expired 1/1/90	No	
CA	Yes	GNPPI	11.5-16.5%	No	Yes Monitoring	Yes 4.5%	Yes 13-16.5% = 50:50 > 16.5% = 100% TO R/P		Categ. II services allowed downward pricing flexibility. Categ. III allowed maximum pricing flexibility.	Reviewing new regulatory framework.
CO	N/A	N/A	N/A	N/A	Yes Monitoring	N/A	Yes above 13.5%	Yes. Through 1997	Fully competitive - deregulated. Emerging competitive - rate flexibility	
CT	No	No	11.26-13.05%	No	Yes	No	11.26-13.05% = 50/50 > 13.05% = 100% to R/P	No	N/A	Modernization agreement not tied to incentive portion of docket.
DE	N/A	N/A	12% equity	N/A	N/A	N/A	N/A	N/A	For competitive or discretionary services	

N/A = Not applicable

Attachment 2-1  
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STATE	AGREED TO UPGRADES	CPI ADJUSTED /AMOUNT	RATE OF RETURN RANGE	FREEZE ON BASIC	SERVICE STANDARDS	PRODUCTIVITY ADJUSTOR /AMOUNT	SHARING LEVELS RATEPAYER COMPANY (R/P:CO)	TRIALS /LENGTH	ANY DETARIFFING, DEREGULATION, RATE FLEXIBILITY	COMMENTS
DC	N/A	N/A	11.5-13.5%	Yes	N/A	N/A	12.5-13.5% ROI = 100% to Co > 13.5% = 50:50	Yes 3 years	Criteria adopted for pricing flexibility.	
FL	N/A	N/A	11.5-16%	Not determinable	N/A	N/A	14-16% ROI = 60% R/P:40% Co 16% ROI = 100% to R/P	Extended to 12/31/92		
GA	No	N/A	12-16%	Not determinable	No sharing by Co. of earnings > 14% if trouble reports > 5/100 lines	Yes 7%	14% = 50:50 16% = 100% to R/P	Yes 2 years	No	Sharing between 14-16% predicated on Co. meeting productivity and service goals. Sliding scale of sharing if productivity = 5-7%
HI	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
ID	Yes	No	N/A	Effectively	N/A	N/A	Based on revenue	Beyond 1991	Yes - all services except basic local services	Sharing based on revenue not profits
IL	N/A	N/A			N/A	N/A		N/A	N/A	Decision on incentive regulation pending
IN	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Detariffing flexibility for small companies. Rate flexibility for large LECs only for customer-specific service offerings.	
IA	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Deregulated many services subject to competition.	

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STATE	AGREED TO UPGRADES	CPI ADJUSTED /AMOUNT	RATE OF RETURN RANGE	FREEZE ON BASIC	SERVICE STANDARDS	PRODUCTIVITY ADJUSTOR /AMOUNT	SHARING LEVELS RATEPAYER: COMPANY (R/P:CO)	TRIALS /LENGTH	ANY DETARIFFING, DEREGULATION, RATE FLEXIBILITY	COMMENTS
KS	Yes	N/A	13.25%ROE	5 years	No	No	No	5 years	Flexible pricing on certain non-basic services	
KY	No	No	10.99-11.61% ROC ROE 12.5-13.5%	Until 1994	No	N/A	11.61-13.11%ROC = 50:50 > 13.11 = 75%R/P:25%Co 9.49-10.99% = 50:50 split of increase <9.49% = 25%R/P:75%Co	Ends May 1994	No	
LA	Yes	No	11.75-12.75% ROE	No	Yes	No	Yes: several levels	Yes 3 years	No	Sharing by Co. predicated on meeting certain service levels.
ME	Yes	No	N/A	Yes	No	N/A	N/A	2 years with extension concluded	Yes - allow service trials with expedited approval.	Considering other alternative regulatory schemes.
MD	N/A	N/A	13.6-15.6% ROE	Yes, 2 years	No	N/A	13.6-15.6% = 50:50 > 15.6% = 100% to R/P	2 years	Yes - for competitive services.	
MA	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	AT&T	
MI	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Yes - most services except basic exchange and access.	New legislation effective 1/1/92 made obsolete prior incentive plan
MN	Yes	N/A	13.25%ROE	Limited	Yes	No	13.5-18.5%ROE = 50:50 > 18.5% = 100% to R/P <10% = Co. can file rate case	2 years with extension	For competitive and emerging competitive services.	Limits rate changes for non-competitive services to "miscellaneous tariff filings."

STATE	AGREED TO UPGRADES	CPI ADJUSTED /AMOUNT	RATE OF RETURN RANGE	FREEZE ON BASIC	SERVICE STANDARDS	PRODUCTIVITY ADJUSTOR /AMOUNT	SHARING LEVELS RATEPAYER: COMPANY (R/P:CO)	TRIALS /LENGTH	ANY DETARIFFING, DEREGULATION, RATE FLEXIBILITY	COMMENTS
MS	No	No	10.74-11.74 ROE	No	No	N/A	> 11.74% = 50:50 < 10.74% = Co can increase 50% needed to reach 10.74%	3 years	No	
MO	Yes	No	12.62-14.1% ROE	3 years	Yes	No	12.62-14.1% = 100% to Co 14.1-14.5% ROE = 60% R/P:40% Co 14.5-17.25% ROE = 50:50 > 17.25% = 100% to R/P	3 years	Not determinable	Considering extension
MT	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	For competitive services on service-by-service basis.	
NE	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	All services except basic are detariffed	
NV	No	N/A	Up to 13% ROE	5 years	Yes	N/A	Sharing when ROE > 13%	No	Rate flexibility for some services, detariffing for others	
NH	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Commission established collaborative process to consider incentive regulation.
NJ	No	Yes		6 years	Yes	Yes	13.7% threshold	6 years	Earnings flexibility for competitive services	
NM	Yes	No	13.75% ROE	3 years	No	N/A	> 13.75% ROE = 55% R/P:45% Co > 20% ROE = 100% to R/P	3 years with extension	Price flexibility for non-basic services.	Company to invest in state-of-the-art communication system for NM colleges.

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STATE	AGREED TO UPGRADES	CPI ADJUSTED /AMOUNT	RATE OF RETURN RANGE	FREEZE ON BASIC	SERVICE STANDARDS	PRODUCTIVITY ADJUSTOR /AMOUNT	SHARING LEVELS RATEPAYER: COMPANY (R/P:CO)	TRIALS /LENGTH	ANY DETARIFFING, DEREGULATION, RATE FLEXIBILITY	COMMENTS
NY	No		11.7%ROE	No	Yes		Yes	2 years - Rochester; 1 year - NYT	AT&T	
NC	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
ND	Yes		N/A	No	No		No	No	Yes - non-essential services detariffed	Essential services increased by "price factor" which equals cost index less 1/2 of productivity incentive adjustment.
OH	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Streamlined regulation for competitive services, including flexible pricing & automatic tariff approval	Ohio Bell proposal pending
OK	Yes	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
OR	No	GNP-P1	13.53% ROE	No	Yes	Yes, 4%	50:50	5 years	Pricing flexibility allowed for fully competitive services	Yellow Pages advertising revenue included in 50:50 revenue sharing. Plan can be terminated if quality of service standards not met.
PA	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	Pricing flexibility for competitively bid contracts and some competitive services	
RI	Yes	Yes	12.25-15.75% return on equity	Yes	No	N/A	13.25-14.75% R(O)E = 50:50 > 15.75% = 100% to R/P	2 years, extended and modified	Not determinable	

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**Southwestern Bell's Responses to Questions  
from Don Low's Testimony Regarding Senate Bill 591**

1. Mr. Low states that TeleKansas has been a good experiment, but that it should not be continued because "total earnings flexibility is unwarranted." He further states that the commission staff believes a "sharing" mechanism would be more appropriate.

Response: We take great exception to Mr. Low's conclusion. "Sharing" is rate of return regulation (which was not in effect under TeleKansas I). It allows the commission to set a rate of return and requires, in essence, an annual "rate case" to determine whether the company reached or exceeded a certain return level. It is rate of return regulation at its worst.

Southwestern Bell's most recent experience with such a plan has been in Missouri where, after all of this complicated procedure, only about \$20.00 per customer in rate reductions was "shared" over a three year period. This is compared to the \$760.00 investment per customer under TeleKansas.

Under sharing, a company like Southwestern Bell has little or no opportunity -- or incentive -- to achieve what the company has in Kansas. Under SB 591, customers have a great deal to gain, and nothing to lose.

2. Mr. Low states that SB 591 is "bad legislation" because it is contrary to "accepted public policy." This policy is that "regulation is a substitute for competition," and the amount of regulation should compare to the degree of competition.

Response: SB 591 is good legislation that recognizes major changes in telecommunications today. What may have been "accepted public policy" twenty years ago -- or even five years go -- is not necessarily what public policy is or ought to be today.

There is great emerging competition in telecommunications today and this cannot be ignored. Simply look at long distance service (over 70 providers in Kansas), PBX providers, CATV making moves to provide local telephone services, competitive coin phone operations, competition for 800/WATS, private line, resellers, cellular service, inside telephone wiring, etc. These services are present today or rapidly developing. And this is good. But it requires that we recognize the need for a new public policy.

What SB 591 proposes is a reduction in regulation to 2/15/94  
*Commerce*

*Attachment 2-1*



match the increase in competition. It simply says, "Let's reduce (government) regulation to correspond with increases in (private enterprise) competition."

3. Mr. Low says that the Bill is "inappropriate" because it is a "premature and inflexible mandate" for regulating local telephone companies.

Response: SB 591 is neither "premature" nor "inflexible". It provides for the appropriate amount of regulation at the present time, taking into account the degree of competition that is present or rapidly emerging in Kansas.

4. There's no reason for the bill to apply to all local telephone companies and, as such, it would hinder the KCC.

Response: The Bill was drafted to apply to SWBT but also not to exclude other local telephone companies. We are primarily concerned about the commitments of SWBT and the changes in regulation that the Bill addresses. It was not our intent to disadvantage other local telephone companies in the state nor to propose that they be afforded unreasonable benefits under the Bill.

5. Mr. Low says this Bill would allow SWBT to retain "unreasonable profits at the expense of monopoly ratepayers".

Response: This contention could not be further from the truth. To begin with, Southwestern Bell has not and is not planning to earn "unreasonable profits." Secondly, the services which might be perceived to be "monopoly" services are rapidly diminishing. Third, I would point out that, under SB 591, local rates would be capped indefinitely, assuring no local rate increases since 1984. As previously pointed out in Mr. Caro's letter to the committee of February 10, 1994, our costs in providing service are increasing, not decreasing.

Thus, Mr. Low's criticism is totally unfounded.

6. Mr. Low says this Bill could lead to geographic deaveraging which would disadvantage rural customers.

Response: It is not our intent under SB 591 to deaverage toll rates. One of the main purposes of this Bill is to provide advantages to rural customers.

7. Mr. Low contends this Bill will hinder competition in Kansas.

Response: This conclusion is totally unfounded. On the contrary, what this Bill will do is recognize increased competition in Kansas and provide a "level playing field" for competitive providers while providing rate stability and significant additional benefits to customers.

8. He states removal of earnings oversight and provisions of Subsection 1(b) might prevent the KCC from addressing quality of service, calling scope, and other problems.

Response: The Bill will not affect the KCC's ability to do any of those things.

9. Mr. Low says if the KCC ordered an expanded calling scope plan, under Subsection 1(b) it would have to allow offsetting increases in other rates to make up "lost revenues". This might cause independent local exchange companies to have to increase local or access rates, which he sees as a problem.

Response: Expanded calling scope type plans always involve the question of lost revenues. This, however, would not be triggered by Subsection 1(b) because it is a commission action "affecting rates".

10. Mr. Low contends that the Staff audit shows that SWBT experienced "excess earnings", based on 1992 data, and that the trend is toward greater earnings in the future. This will lead to "excess profits".

Response: This contention simply emphasizes one of the problems associated with rate of return regulation. As reported to the commission in our TeleKansas II filing on January 3, 1994, our earnings under TeleKansas I have been modest (averaged 11.8% return on equity). While there was no rate of return ceiling under TeleKansas I, if there had been, SWBT's earnings were anything but "excessive".

11. Mr. Low states that SB 591 would guarantee "excess profits" because Subsection 1(a) would prevent the commission from adjusting rates to reflect reasonable earnings.

Response: The only thing SB 591 would prevent the commission from doing is reducing SWBT's local rates while it is in compliance with its commitments under the Bill. The commission has authority to review all other rates under Subsection 1(c) and to exempt services where it finds there is competition, pursuant to Section 3. Since SWBT's local rates would be capped, and its costs of providing service are increasing, it is difficult to understand where Mr. Low thinks "unreasonable earnings" would come from.

12. He says Subsection 1(b) requires the KCC to increase rates for "non-competitive services" to offset KCC actions to introduce competition.

Response: This was certainly not our intent concerning Subsection 1(b), and we are willing to address this concern with amendatory language.

13. Subsection 1(c) makes filed rates presumptively reasonable and appears to effectively preclude KCC review.

Response: The purpose of this change in the law is to prevent the commission or its staff from unduly delaying introduction of rate changes or new services. Under the present pending order of the KCC addressing regulation of long distance companies (e.g., AT&T, MCI, Sprint) a much more expedited procedure for approval of rates and services is addressed, allowing long distance companies approval on seven days notice in many cases. Our purpose in proposing Subsection 1(c) is to place SWBT in a position comparable to the long distance companies, while also recognizing SWBT's commitment to cap local rates and spend \$138 million over five years.

14. Mr. Low says the "freeze" on basic is "no bargain" because SWBT has no need to increase local because its earnings are so high.

Response: Our earnings are modest at best and the rates are capped, not "frozen," i.e., they can't go up but they can go down.

15. He says technological improvements, etc. will reduce the cost of providing basic service.

Response: Thus far, our costs, including the technological improvements we have made, have increased our total cost of providing service by some 20%.

16. Many states have ordered rate reductions since 1987. Why shouldn't SWBT reduce its local rates?

Response: SWBT's local rates have been the same since 1984, they are \$2.00 below the national average and they are not presently covering their costs.

17. He says modernization would be "no bargain" if the KCC doesn't have the ability to determine rates. Would this be the case?

Response: No. Rates for services under such modernization would be subject to review by the KCC.

18. Mr. Low says no competition for local service is likely for several years.

Response: We have competition today for local business services. In addition, we presently have competition from over 70 interexchange providers, and competition for WATS/800, access, private line, inside wire, directory services, operator services, coin phone services, etc. In addition, competition is imminent from CATV providers (Multimedia, TCI-Bell Atlantic), MCI's announced nationwide network, competitive access providers, and wireless service providers.

19. Mr. Low questions the use of incremental costs for controlling "predatory pricing" for noncompetitive services.

Response: Incremental costs are used as a floor under TeleKansas I; it creates a reasonable inference of the reasonableness of rates.

20. Mr. Low questions whether access charges would be fully subject to the provision of Subsection 1(c).

Response: Subsection 1(c) would apply to all services, including access, with the commission and its staff having full opportunity to review such charges.

21. Mr. Low says that the expedited procedures under Subsection 1(c) would be difficult for the KCC Staff to comply with.

Response: No more than Staff's implementation of the new procedures for long distance companies recently ordered by the KCC (written order pending).

22. Mr. Low suggests that we should wait for Congress to act before considering state legislation.

Response: Do we really want to wait for the federal government to address telecommunications policy for Kansas?



Southwestern Bell's Responses to Issues Raised  
in Material Attached to Don Low's Testimony  
Regarding Senate Bill 591

1. Does Subsection 1(a) affect the KCC's regulation over SWBT's obligation to serve or sufficiency of service?

Response: No.

2. Under Subsection 1(a), infrastructure investment -- who decides what is needed and/or where investment should be placed?

Response: SWBT, with input from various policy and customer groups. These investments would be above and beyond what are necessary to provide "sufficient/efficient" service.

3. Could SWBT's infrastructure investment in economic development be used solely for competitive infrastructure advantage over competitors?

Response: Our intent is to advance the modernization of all of Kansas, much of our program being aimed at rural Kansas. There will be competitors in some of these areas, but for the most part competitors are not "beating down the door" to serve these areas.

4. Under Subsection 1(b), if the commission takes "any action subjecting SWBT to any reduction in revenues," would this include action directly involving SWBT or does it include action concerning other companies? Does it apply only to new actions or continuing effects of prior commission actions?

Response: The intent of the language is not to use mere authorization of competition as a "triggering" action. We are willing to consider amendatory language to reflect this intent.

5. Mr. Low contends that under Subsection 1(c), there is no provision that existing rates would be reasonable.

Response: The current law provides that rates must be "reasonable, just and nondiscriminatory". SB 591 does not repeal this provision.

6. It appears that Subsection 1(c) shifts the burden to Staff to prove that a rate filing is unreasonable.

Response: Under the pending long distance company order, we understand that rates will be approved in 7 days, with no detailed review being contemplated in many cases. In any

event, Subsection 1(c) merely prevents needless suspensions of rates otherwise lawful and proper.

7. Mr. Low contends that, under Section 3, the "same or similar service" is not defined. What does this mean?

Response: It simply means a service reasonably substitutable for another in the same geographic market. "Competition" will be up to the commission to decide, and it will also determine such things as "same or similar service".

8. Mr. Low states that, under Section 3, it appears that only a service provided by the committing utility would be exempt, not the same or similar service provided by the other provider. Is this true?

Response: No. A service would be exempt for all providers.

9. According to Mr. Low, Subsection 1(a) provides capital expenditures in the amount of \$138 million targeted to various categories. It does not include provisions in TeleKansas II regarding 911, "TALK" and other services. Why is the Bill different than TeleKansas II?

Response: The basic tenets are the same; the Bill is less detailed. We would be willing to consider amendatory language providing greater detail for infrastructure investment.

10. Per Mr. Low, SB 591 establishes a 15 day notice for filing; TeleKansas II would continue a 20 day filing period with an advance 6 month notice of expected filings. Why the difference?

Response: We think the 15 day notice is sufficient (we proposed 14 days in TeleKansas I). Again, the Bill addresses the basic tenets of TeleKansas II.

11. Mr. Low states that TeleKansas II does not contain a provision like the one in Subsection 1(b) that requires the commission to develop a "plan" to make up for lost revenues.

Response: This is a provision similar in nature to language in TeleKansas I which provided relief to the company where there were extraordinary circumstances beyond the company's control. We believe the language in Subsection 1(b) is appropriate, although it is not SWBT's intent for Subsection 1(b) to be triggered by KCC approval of a competitor providing service in Kansas.

12. The Bill provides that carrier access charges will be established without reference to SWBT's level of earnings. TeleKansas II does not even address access charges. Why the difference?

Response: The point is, if the company makes the commitments in Subsection 1(a) it is not subject to rate of return regulation. There's no reason to make an exception in the case of access charges. The company has not said (in TeleKansas II or elsewhere) that it believes rate of return should be used to review access charges.

13. Mr. Low states that SB 591 requires exemption from regulation of any service where competition exists; TeleKansas II calls for "same regulatory treatment" where services are competitive. Why the difference?

Response: Both the Bill and TeleKansas II address the problem of SWBT being subjected to unfair regulation with regard to competitive services. The Bill simply goes a step further and provides that if the commission finds that true competition exists, regulation is no longer needed.

14. In TeleKansas I, SWBT proposed (and was ordered to make) up front revenue reductions. Why not in TeleKansas II or in the Bill?

Response: It would be highly inappropriate for the company to be required to reduce rates as a "condition" of approval of TeleKansas II or enactment of SB 591, because the company's earnings in Kansas presently are very modest by any reasonable measure. Second, the very period of time the KCC Staff looked at to come up with its suggested rate reductions was a period under TeleKansas when the company was supposed to not be under rate of return regulation.

15. Mr. Low tries to make an issue out of SWBT's attempt to reduce the number of Directory Assistance allowances while under TeleKansas I.

Response: Although 80% of the company's rates were capped or frozen under TeleKansas I, it did provide that the company could propose increases in certain limited areas. Directory Assistance was a service that fell into one of those areas and the language of TeleKansas I was ambiguous about whether SWBT could propose an increase or not. The company proposed changes, the commission reviewed it, the proposal was denied: end of story.

16. Did SWBT try to "violate" TeleKansas I, as suggested by Mr. Low, by proposing that the commission accept accounting changes regarding increased retirement benefits (FAS 106)?

Response: This is truly a "red herring". The accounting change was proposed but the company did not seek to increase any rates in connection therewith. Staff and CURB tried to distort the company's filing to suggest that rates would be affected, which they weren't.

The bottom line of this point is the company is not proposing any rate increase in TeleKansas II or SB 591 as a

result of these accounting changes.

17. Staff states in Don Low's filing, "with the exception of a few services... virtually all of SWBT's service offerings are flexibly priced today." Why do you need Subsection 1(c) of SB 591?

Response: The intent of Subsection 1(c) is to further expedite the review of rate proposals for "all other services" besides capped local. This is consistent with the thrust of the upcoming long distance company order and, as Staff seems to concede, such expedited procedures apparently aren't a problem.