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Public Service Commission

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COMMISSION CLERK

-M-E-M-O-R-A-N-D-U-M-

DATE: May 19, 2005

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Competitive Markets & Enforcement (Simmons) *SAS*
Office of the General Counsel (Susan) *JS* *JK* *[Signature]*

RE: Docket No. 050294-TL – Petition for waiver of Order PSC-96-0012-FOF-TL to consolidate number of non-basic service categories by Verizon Florida Inc.

AGENDA: 05/31/05 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\CMP\WP\050294.RCM.DOC

Case Background

On April 25, 2005, Verizon Florida Inc. (Verizon or Company) filed a petition for a waiver of Order No. PSC-96-0012-FOF-TL¹ to consolidate the existing ten non-basic service categories to the same five categories approved previously for BellSouth Telecommunications Inc. (BellSouth) pursuant to a similar waiver request (Docket No. 041213-TL). Per Section 364.051, Florida Statutes, incumbent local exchange companies (ILECs) have been able to elect price regulation since January 1, 1996. Section 364.051(5)(a), Florida Statutes, limits rate increases by a price-regulated ILEC, for any non-basic service category, to 6% or 20% within a 12-month period, depending on whether or not there is another carrier providing local telecommunications service in a given exchange. The Commission established non-basic service categories in order to implement this statutory provision. The original ten non-basic service categories were established by the above referenced order, wherein the Commission approved a proposed stipulation among certain parties to Docket No. 951159-TL.

¹ Issued on January 4, 1996 in Docket No. 951159-TL, Investigation to Determine Categories of Non-Basic Services Provided by Local Exchange Companies Pursuant to Section 364.051(6), Florida Statutes.

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Discussion of Issues

Issue 1: Should the Commission grant Verizon’s Petition for Waiver of Order No. PSC-96-0012-FOF-TL and reduce the number of non-basic service categories from ten (10) to five (5)?

Recommendation: Yes. The Commission should grant Verizon’s Petition for Waiver of Order No. PSC-96-0012-FOF-TL and reduce the number of non-basic service categories from ten (10) to five (5) for Verizon. **(SIMMONS, SUSAC)**

Staff Analysis: The statutory limitation on non-basic rate increases does not apply to individual services, but rather to the average rate change (considering both increases and decreases) across all the services in a non-basic category, over a 12-month period. With each tariff filing, Verizon submits a price-out for the affected non-basic service category, showing beginning of period and proposed revenue, to demonstrate that the overall rate increase is within the statutory limit. Verizon takes the position that competition is increasingly limiting its ability to increase prices, which indicates that fewer non-basic service categories are needed.

The following chart depicts the present and Verizon’s proposed non-basic service categories:

| <u>Present</u> | <u>Verizon Proposed</u> |
|---|---|
| Residence Non-Basic Exchange Access | Residential Non-Basic Service |
| Residential Optional Services | |
| Business Non-Basic Exchange Access | Business Non-Basic Service |
| Business Optional Services | |
| Local Directory Assistance and Directory Services | Local Directory Assistance and Directory Services |
| Toll Services | Other Optional |
| Operator Services | |
| Transport Services | |
| Public and Semi-Public Telephone | |
| Miscellaneous Services | Miscellaneous Services |

Verizon proposes to migrate the revenue for each existing category to the appropriate new category, at the end of the current 12-month pricing period. According to Verizon, and staff agrees, this approach will allow the Company to transition to the new categories, while maintaining compliance with Section 364.051(5)(a), Florida Statutes.

The size and structure of the non-basic service categories can directly influence Verizon's flexibility to adjust prices and be compliant with the statute. With a larger number of services included in a non-basic service category, Verizon can increase some rates significantly if market conditions favor the Company, while lowering other rates to address competitive pressures. For this reason, staff believes that the services in a non-basic category should be subject to similar competitive and market conditions. Finally, a system of fewer, but larger, non-basic service categories inherently provides more pricing flexibility, although competitive and market conditions will dictate to what extent this flexibility is actually used.

From staff's perspective, the proposed category structure does reflect differences in the competitive pressures facing Verizon. Combining the existing Non-Basic Exchange Access and Optional Services categories for residential and business, respectively, makes sense since both types of services are provided by the end user's local telephone company. The state of competition in the local market should affect pricing of exchange access and optional local services in a similar manner. Staff also believes that Verizon's request to combine Toll Services, Operator Services, and Transport Services² is logical since these types of services are recognized as being some of the most competitive.

Staff next considers whether Verizon's rate increase history provides any indication of how Verizon might utilize additional pricing flexibility, and how customers might be affected. In reviewing Verizon's rate increase history for the various categories, staff did not discern any concerns with the proposed consolidation. For the non-basic service categories that Verizon proposes to combine, the Company has used only a limited portion of the current pricing flexibility, which indicates that the additional pricing flexibility gained through consolidating categories is unlikely to lead to higher increases in the future.

Based on the above reasoning, staff recommends that the Commission grant Verizon's Petition for Waiver of Order No. PSC-96-0012-FOF-TL and reduce the number of non-basic service categories from ten (10) to five (5) for Verizon. This action would be consistent with Order No. PSC-05-0278-CO-TL, issued in Docket No. 041213-TL, in which the Commission granted the same relief for BellSouth.

² Staff believes that the Public and Semi-Public Telephone category is no longer applicable since these retail services have been deregulated.

Docket No. 050294-TL

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Issue 2: Should this docket be closed?

Recommendation: Yes, if no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, this docket should be closed upon the issuance of a consummating order. **(SUSAC)**

Staff Analysis: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, this docket should be closed upon the issuance of a consummating order.