

FINAL REPORT

REGULATION OF TELEPHONE UTILITIES STUDY COMMITTEE

January 1993

AUTHORIZATION AND APPOINTMENT

The Regulation of Telephone Utilities Study Committee was created by the Legislative Council for the 1992 Legislative Interim. The Study Committee was charged to review Iowa's current laws and rules regulating telephone utilities to determine if any changes are necessary to allow for greater efficiency by utilities while guaranteeing quality service and reasonable rates for consumers.

Members serving on the Study Committee included:

Senator Mike Gronstal, Co-chairperson
Representative Bill Brand, Co-chairperson
Senator Donald Doyle
Senator Jim Kersten
Senator Bill Palmer
Senator Sheldon Rittmer
Representative Jack Holveck
Representative Joe Kremer
Representative David Osterberg
Representative Greg Spenner

COMMITTEE PROCEEDINGS

The Study Committee was granted two meeting days to conduct its study and held the meetings on November 24, 1992, and December 15, 1992. A number of individuals testified before the Study Committee and a summary of their testimony is provided in this report. A list of all materials received by the Study Committee is attached to this report. Copies of these materials are maintained on file with the Legislative Service Bureau.

MEETING - November 24, 1992

The first meeting of the Study Committee was held on November 24, 1992, in Hearing Room 1, 1st Floor of the Lucas State Office Building. Presentations were made concerning alternative forms of telephone utility regulation.

Mr. Dennis Nagel, Chairperson of the Iowa Utilities Board, provided background information on the current regulatory structure in Iowa and various alternative forms of regulation, and testified that as a result of changes in the telecommunications industry, regulatory reforms are needed.

Mr. James Maret, Consumer Advocate, stated his opposition to any alternative regulatory plan, testifying that such regulation will not promote efficiency, is not necessary or desirable to modernize the current telecommunications network, will not assist in promoting competition, and will lead to higher rates for consumers.

Mr. Ronald Binz, Director of the Colorado Office of Consumer Counsel Committee and former President of the National Association of State Utility Consumer Advocates, stated that while he is not totally opposed to alternative forms of regulation, certain consumer protections must be included in any proposal. He opined that he does not see the need in Iowa to move toward incentive regulation. (A brief explanation of the term "incentive regulation" is provided in the recommendation portion of this report.)

Mr. Robert Holz, an attorney with the Davis, Hockenberg, Wine, Brown, Koehn, & Shors law firm, testified on behalf of the Iowa Telephone Association that traditional rate-of-return regulation should be abandoned and that the state should implement alternative regulation.

MEETING - December 15, 1992

The second and final meeting of the Study Committee was held on December 15, 1992, in Committee Room 116 of the Statehouse. Additional presentations were made, followed by Study Committee discussion and recommendations.

Mr. William Smith, Utilities Division, presented a summarization of the final report prepared by Arthur D. Little, Inc. entitled "Study of the Role of the Telecommunications Industry in Iowa's Economic Development". The report had previously been presented to the Iowa Utilities Board and the Department of Economic Development.

Mr. David Conn, Consumer Advocate Division, expressed his concern regarding the conclusions of the Arthur D. Little study. He expressed the opinion that the recommendation for the implementation of incentive regulation is inconsistent with

the findings of the study and that there is no linkage between incentive regulation and technology deployment. He concluded by indicating that if incentive regulation is to be implemented, it should be targeted toward the particular goal which is intended to be achieved.

Mr. Lyle Williamson, MCI Corporation, noted that state law and the policies of the Utilities Board have generally been positive for the telecommunications industry. He noted that MCI is interested in seeing technological upgrades in the local exchange networks, and would support incentive regulation to the extent this would be accomplished. He noted, however, that competitive markets should be promoted wherever possible, and proprietors of the local exchange networks should not be allowed to discriminate against other providers in favor of their own competitive services.

Ms. Elizabeth Powell, American Association of Retired Persons, expressed concern regarding the possibility that any alternative form of regulation might be considered. She indicated that in one way or another, any alternative form of regulation undermines the primary features of rate-of-return regulation which include a fair rate of return for investors and fair rates for consumers.

Mr. Allan Thoms, Director of the Iowa Department of Economic Development, indicated the importance of telecommunications in economic development and in improving the quality of life in rural Iowa. He encouraged the Study Committee to consider implementing changes in public policy regarding regulation of the telecommunications infrastructure to permit Iowa to realize a competitive advantage.

COMMITTEE RECOMMENDATION

The Study Committee reviewed a draft proposal submitted for consideration by Co-chairperson Brand. After Study Committee discussion and amendment the following proposal was adopted:

The Regulation of Telephone Utilities Study Committee recommends that if the General Assembly considers authorizing the Utilities Board to adopt rules which establish incentive regulation for local exchange telephone utilities, certain provisions should be included. The purpose of such regulation should be to provide an incentive to participating local exchange utilities to take advantage of technological opportunities and efficiencies to improve the operating efficiency of the utilities while maintaining or improving the quality of service provided. The incentive regulation plan should include, but not be limited to, the following provisions:

1. Initial review of a participating utility's rates within twelve months prior to the date the utility begins participating. The review is to determine

whether the rates of the utility being charged at that time are just and reasonable.

2. A mechanism which provides for the sharing of any increased earnings which are the result of actual efficiencies identified by the utility over the utility's authorized rate of return established under the plan of incentive regulation with the customers of the utility as provided by rules adopted by the board. The sharing mechanism should provide that at least fifty percent of any increased earnings subject to sharing must be refunded to the utility's customers. A maximum cap should be placed on the increased earnings subject to sharing with earnings in excess of this amount being refunded entirely to the customers.
3. Minimum participation period of two years for any local exchange telephone utility electing to participate. This provision should, however, provide that the Consumer Advocate or the utility may request that the board terminate participation for the utility in the event of exceptional or unforeseeable circumstances, and that if such a request is made that the hearing shall be mandatory.
4. Periodic reports as determined necessary by the board to document that the incentive regulation plan is being properly implemented. The Consumer Advocate should have authority to investigate a utility's compliance with incentive regulation requirements and should be able to request a hearing concerning any part of the utility's report, and if such a request is made the hearing shall be mandatory.
5. A maximum time period for the authority of the board to establish and maintain a plan of incentive regulation of four to five years.
6. A study of the effectiveness of the plan of incentive regulation including a description of the plan, the number of local exchange telephone utilities participating in the plan, and an analysis of the effects of the plan. The Utilities Board shall require, as a part of the study, that each participating utility conduct an annual survey of the utility's customers concerning customer satisfaction with services offered by the utility. A report should be delivered to the General Assembly annually by January 15.
7. The local exchange utility should be required to submit a detailed plan for investment of revenues in the utility's network and facilities. The plan should also include the disposition of additional revenues retained by the utility under an incentive regulation plan.
8. The Utilities Board and the Consumer Advocate should have a strong role in assuring the quality of services provided by the local exchange utility participating under an incentive regulation plan.

REGULATION OF TELEPHONE UTILITIES STUDY COMMITTEE

Materials Received At First Meeting November 24, 1992

1. Membership list
2. Committee charge
3. Committee rules of procedure
4. First meeting agenda
5. Statement of Dennis Nagel, Chairperson, Iowa Utilities Board
6. Statement of James Maret, Consumer Advocate
7. Statement of Ronald Binz, Director, Colorado Office of Consumer Counsel Committee
8. Statement of Bob Holz, Attorney, representing the Iowa Telephone Association
9. Analysis of state regulatory schemes compiled by Mary Wybenga, U.S. West Communications Public Policy

Materials Received At Second Meeting December 15, 1992

1. Second meeting agenda
2. Statement of William Smith, Jr., Utilities Division
3. Statement of Lyle Williamson, MCI Corporation
4. Statement of Betty Powell, AARP
5. Statement of Allan Thoms, Director, Department of Economic Development
6. Letter from Iowa Telecommunications User Group
7. Resolution offered by Representative Jack Holveck
8. Recommendation offered by Representative Bill Brand