

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

**Telecommunications Division
Market Structure Branch**

**RESOLUTION T-16599
December 11, 2001**

RESOLUTION

RESOLUTION T-16599. VERIZON CALIFORNIA INCORPORATED (U-1002-C). REQUEST FOR APPROVAL OF PRICE CAP MECHANISM, IN COMPLIANCE WITH DECISION 89-10-031 AND DECISION 94-09-065, AND CORRESPONDING ADJUSTMENTS TO SURCHARGES WHICH WILL BE EFFECTIVE ON JANUARY 1, 2002.

BY ADVICE LETTER NO. 9888 FILED ON SEPTEMBER 28, 2001.

SUMMARY

This Resolution authorizes Verizon California, Inc. (Verizon) to decrease its annual revenue by \$13,000,000 effective January 1, 2002. The adopted revenue adjustments and surcharge changes are shown in Appendices A and B attached to this resolution.

Verizon requested an annual revenue decrease of \$13,000,000 due to the impacts of a one-time LE factor adjustment for Local Competition Implementation Cost Recovery and a compliance adjustment for the GTEC/Bell Atlantic Merger Revenue Reduction.

BACKGROUND

New Regulatory Framework

In Decision (D.) 89-10-031 the Commission adopted an incentive-based regulatory framework (called the new regulatory framework or "NRF") for Pacific and GTE California Incorporated (GTEC), which is now know as Verizon California Incorporated. The decision stated:

This new regulatory framework is centered on price indexing mechanisms with sharing of excess earnings above a benchmark rate of return level.

Following a startup revenue adjustment (given in D.89-12-048), ...prices for the utilities' basic monopoly services and rate caps for flexibly priced services will be indexed annually according to the Gross national Product Price Index (GNP-PI) inflation index reduced by a productivity adjustment of 4.5%.

The indexing formula also allows for rate adjustments for a limited category of exogenous factors whose effects will not be reflected in the economy-wide GNP-PI. While all such costs cannot be foreseen completely, we recognize that the following factors (called Z-factors): changes in federal and state tax laws to the extent they affect the local exchange carriers disproportionately, mandated jurisdictional separations changes, and changes to intraLATA toll pooling arrangements or accounting procedures adopted by this Commission.

However, the Commission did not authorize Z-factor treatment for all unforeseen or exogenous factors. In D.89-10-031, the Commission stated that:

...Normal costs of doing business (including costs of complying with existing regulatory requirements) or general economic conditions would be excluded as Z-factor items.

In D.93-09-038, the Commission ordered GTEC to replace the GNP-PI with the Gross Domestic Product Price Index (GDP-PI) commencing with GTEC's 1994 price cap filing. In addition, the Commission adopted a productivity factor of 4.6% for GTEC's 1995 price cap filing.

In D.94-09-065, the Commission authorized Pacific and GTEC to implement the 1995 price cap rate adjustments through the billing surcharge/surcredit mechanism.

In 1995, the Commission issued D.95-12-052 regarding the second triennial New Regulatory Framework review. In Ordering Paragraph No. 4 of that decision, the Commission suspended the application of the GDP-PI minus productivity factor formula used in price cap regulation of Pacific and GTEC until further order of this Commission or until a final decision is issued in the next triennial review.

In October 1998, the Commission issued D.98-10-026 regarding the third triennial review of the NRF. The order continues the suspension of the GDP-PI minus

productivity factor formula, suspends for the first time the sharing mechanism, permanently eliminates the depreciation review, replaces Z-factors with limited exogenous (LE) factors, and effectively imposes a cap on residential services by keeping price caps generally.

The order also specifies that, in the future, LE cost recovery is confined to recovery for cost increase or decreases resulting from (1) items mandated by the Commission and (2) changes in total intrastate recovery resulting from changes between federal and state jurisdiction. Recovery of Commission mandated cost changes must be authorized in the underlying Commission Decision.

Verizon's Price Cap Filing

On September 28, 2001 Verizon California Inc. filed Advice Letter No. 9888 requesting billing surcredit changes to be effective January 1, 2002 in order to implement the certain one-time revenue adjustments for 2002.

Verizon California Inc.'s filing requests the following revenue adjustments.

1. Local Competition Implementation Costs

Per D 01-09-063, Verizon California Inc. is authorized to recover its implementation costs for Local Competition of \$12.0 million over a 2-year period.

2. GTE-Bell Atlantic Merger Compliance Adjustment

Per D.00-03-021, the former GTE California Inc. which is now known as Verizon California Inc. must include an annual rate reduction of \$19.0 million per year for five years beginning with the first NRF price cap filing made after consummation of its merger with Bell Atlantic.

3. Recovery of NRF Financial Audit Expenses (Deferral until 2003 Price Cap)

Resolution T-16480 authorized deferral until the 2002 Price Cap for recovery of NRF Financial Audit Expenses. Due to ongoing audit work, Verizon continues to receive, and pay, invoices from the Commission's external audit consultants. Therefore, Verizon requests deferral until the 2003 Price Cap to recover its known and quantifiable expenses.

Verizon California requests a total revenue reduction of \$13.0 million to become effective on January 1, 2002, that reflects the local competition implementation costs ordered in D.01-09-063 and the GTE-Bell Atlantic merger compliance adjustments ordered in D.00-03-021. Verizon used an annualized billing base of \$2,110,323,000 for calculating the surcredit effective January 1, 2002.

NOTICE/PROTESTS

Verizon California Inc. stated that a copy of the advice letter, and related tariff sheets were mailed to all interested utilities and/or parties. Notice of Advice Letter No. 9888 was published in the Commission Daily Calendar on October 10, 2001.

No protests were filed.

DISCUSSION

Local Competition Implementation Costs

In D.01-09-063 (OP 2), Verizon was authorized to include an implementation cost surcharge in its Annual Price Cap filing beginning January 1, 2002 to recover \$6 million per year for a two-year period, for a total of \$12 million, to be applied to exchange, toll, and access services pursuant to schedule CA. PUC No. 38-Billing Surcharges of Verizon's tariffs. Verizon's request for recovery of \$6 million in local competition implementation costs complies with D.01-09-063.

GTE-Bell Atlantic Merger Compliance

In D.00-03-021 (OP 1.b), Verizon (formerly GTE California Inc.) was directed as follows.

"GTE California, or its successor, shall reduce its annual revenues by \$19.0 million per year for five years. GTE California, or its successor, shall include this revenue reduction in the first October 1 new regulatory framework price cap advice letter filing made after consummation of the merger. GTE California, or its successor, shall include this revenue adjustment in each October 1 price cap advice letter filing for a total of five years. Each price cap advice letter shall specify, among other things, the billing base for the purpose of this surcredit. The billing base shall include local, toll and access revenues, with the billing base incorporating the amount of both the CHCF-B and the annual total revenues from residential exchange service access charges. The billing base shall be updated with each price cap advice letter".

Verizon California Inc.'s price cap filing complies with the order in D.00-03-021. It reflects the \$19.0 million revenue reduction ordered in the decision. The filing also identified the billing base used for the merger surcredit for the 2002 price cap filing. The billing base includes local, toll and access revenues.

Recovery of NRF Financial Audit Fee

The issue of cost recovery related to the NRF audit was discussed in D.96-05-036. This decision did not guarantee recovery of audit related expenses, deferring such judgment until a request for recovery was submitted and given due consideration. Verizon, in its 2000 price cap filing, requested LE factor recovery for NRF financial audit expenses. In Resolution T-16376, this Commission determined that Verizon does have authorization for LE factor treatment of the NRF financial audit expenses under the current procedures, and declined to authorize recovery of costs associated with the NRF audit prior to incurrence of the costs. Verizon was allowed to seek recovery of costs associated with the NRF audit when actual costs are incurred. Verizon was also asked to include the nine-criteria Z-factor analysis with its request for recovery.

Since the proceeding addressing the NRF audit is in progress, actual costs will not be known until after the conclusion of hearings in the proceeding. Verizon requests deferral of its filing for recovery of the known and quantifiable expenses until the 2003 Price Cap. Verizon has also included the nine-criteria Z-factor analysis as instructed in Resolution T-16376. Consistent with treatment in Resolution T-16376 for the audit costs, we believe it is appropriate for Verizon to defer a request for recovery of NRF audit costs until total actual audit costs are known. At the time of its filing, Verizon shall include the nine-criteria Z-factor analysis, updated as necessary to reflect any Commission orders in the proceeding addressing the NRF audit.

This is an uncontested matter in which the resolution grants the relief requested. Accordingly, pursuant to PU Code Section 311 (g) (2), the otherwise applicable 30-day period for public review and comment is being waived.

FINDINGS

1. Verizon filed Advice Letter No. 9888 on September 28, 2001 to implement Verizon's 2001 price cap mechanism and certain one-time adjustments. Verizon requested adjustments for local implementation costs, the GTE-Bell Atlantic merger and deferral of the NRF Financial audit fee.
2. The local competition implementation costs requested by Verizon in compliance with D.01-09-063 should be adopted.
3. The Bell-Atlantic merger savings refund identified by Verizon is in compliance with D.00-03-021, and should be adopted.
4. Verizon's request to defer recovery of the NRF Audit expenses should be granted.

5. A total price cap mechanism decrease \$13.0 million, effective January 1, 2002, is justified.

THEREFORE, IT IS ORDERED that:

1. Verizon California, Inc. shall reduce its annual revenue by \$13.0 million as a result of its 2002 annual Price Cap Adjustment filing in Advice Letter No. 9888.
2. Verizon California, Inc. shall defer recovery of NRF Audit expenses until total expenses are known and quantifiable. At the time recovery of NRF Audit expenses is requested, the request shall include an updated nine-criteria Z-factor analysis.
3. The revisions to Verizon California, Inc's price floors filed in Advice Letter No. 9888 are adopted, and shall be implemented on January 1, 2002. In instances where the price floor exceeds the established price cap, Verizon shall file an application to amend the rates for those services, consistent with the provisions of D.95-05-047.

This Resolution is effective today.

I hereby certify that the Public Utilities Commission adopted this Resolution at its regular meeting on December 11, 2001. The following Commissioners approved it:

/s/ WESLEY M. FRANKLIN

WESLEY M. FRANKLIN
Executive Director

LORETTA M. LYNCH
President
HENRY M. DUQUE
RICHARD A. BILAS
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners

APPENDIX A
 Resolution T-16599

Verizon California, Inc.
 2002 Price Cap Filing
 \$ (in Millions)

	Verizon Proposed Revenue Impacts	Adopted Impacts
Ongoing Adjustments		
GTE-Bell Atlantic Merger Compliance	\$ (19.0)	\$ (19.0)
Local Competition Recovery Costs	\$ 6.0	\$ 6.0
One-time LE-factors		
NRF Audit Fee	\$ deferred	\$ deferred
Total	\$ (13.0)	\$ (13.0)

APPENDIX B
Resolution T-16599

Verizon California, Inc.
2002 Price Cap Filing
(Adjustments by %)

	Verizon Proposed Surcredit	Adopted Surcredit
Access	(3.71%)	(3.71%)
Local	(0.72%)	(0.72%)
Toll	(2.90%)	(2.90%)