

THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Brian J. Moline, Chair
 John Wine
 Robert E. Krehbiel

In the Matter of a General Investigation)
Into a Policy Regarding Rate Changes by) Docket No. 04- **G1MT-1080-GIT**
Rate of Return Regulated Local Exchange)
Carriers between KUSF Audits or Rate Cases.)

**ORDER OPENING DOCKET, SOLICITING COMMENTS
AND ASSESSING COST**

NOW, the above-captioned matter comes before the State Corporation Commission of the State of Kansas ("Commission") on its own motion. Having examined its files and records, and being duly advised in the premises, the Commission finds and concludes as follows:

1. In *Rural Telephone Service Co. v. Kansas Corporation Comm'n*, 31 Kan. App. 2d 760, 72 P.3d 937 (2003), the Kansas Court of Appeals held that the Commission did not have statutory authority to reduce Rural Telephone Service Co.'s ("Rural") Kansas Universal Service Fund ("KUSF") distribution in response to increased revenue from approved tariff filings. The Court reversed the Commission's October 9, 2002 Order in Docket No. 02-RRLT-875-TAR which had granted a tariff rate increase and correspondingly reduced Rural's KUSF support, but it remanded the matter to enable the Commission to determine the reasonableness of the proposed tariff changes in light of the Court's decision to disallow a contemporaneous reduction of KUSF support. On remand, after considering comments by Rural and Staff, the Commission decided, in Docket No. 02-RRLT-875-TAR, that it would allow the previously approved tariff changes to remain

in effect. However, the Commission also indicated that it would open this docket to consider Staff's proposed policy as set forth in Staff's April 28, 2004 Comments ("April 24, 2004 Comments") in that docket.

2. The basic question before the Commission is how to determine the reasonableness of proposed increases in tariffed rates for rate of return regulated local exchange carriers ("RLECs") that have undergone a KUSF audit or a rate case establishing the company's overall revenue requirements. In determining the reasonableness of rates for rate-of-return regulated companies, the Commission must evaluate not only whether the specific rates for a service are reasonable in light of costs and other considerations regarding that particular service but also whether the company's rates in aggregate result in a reasonable overall level of earnings or rate of return. If a company has been the subject of a KUSF audit or rate case, its revenue requirements have been determined and its rates or, at least, its KUSF support has been adjusted accordingly. Consequently, any increase in tariff rates might result in over-earnings by the company. At the same time, it may be desirable for specific rates for particular services to be adjusted to reflect the costs or market value of such services. Such rate increases would mean that customers of those particular services would be paying appropriate prices to the company providing the services. As a matter of policy, such a result is likely preferable to continued support from the KUSF, which is paid by all customers of telecommunications services throughout Kansas. The Court of Appeals decision does not allow for a contemporaneous offset against the company's KUSF support to prevent over-earnings. The Commission therefore needs to determine how it should address these conflicting considerations when tariff modifications that will result in rate increases are

proposed by an RLEC. The Commission seeks comments on this issue in general and specifically on Staff's proposal presented following the remand in Docket No. 02-RRLT-875-TAR.

3. The Commission has jurisdiction over the RLECs and this issue pursuant to K.S.A. 66-104, 66-1,188, 66-1,190, 66-1,191 and 66-2008.

4. In its comments, Staff expressed concern that allowing modifications that increase tariff rates between audits or rate cases could result in an unreasonable increase in a company's earnings. On the other hand, Staff recognized that limited tariff rate increases might be appropriate for RLECs if the increases are not likely to result in significant over-earnings. Staff observed that the reasonableness of tariff changes could only be judged in the context of a particular company's revenue requirement. What is reasonable for one company may not be for another, depending upon the overall contribution a particular rate makes to a company's earnings. In deciding the question of reasonableness, Staff recommended the Commission consider whether the proposed changes are revenue neutral or result in a significant increase in revenue. Staff recognized that a Commission finding regarding a company's revenue requirement becomes less valid as the test period of the audit becomes older and as a company's circumstances change. Thus, Staff stated a *de minimis* increase in revenues is unlikely to result in over-earnings. Staff's April 28, 2004 Comments, ¶¶ 5-6.

5. In defining what tariff changes might be considered reasonable, Staff proposed that the Commission depart from the traditional policy of not allowing increases in revenue for RLECs between rate hearings but instead allow an increase of not more than 3% to intrastate jurisdictional required revenue between audits. Staff explained that such a limited policy would generally result in an increase of less than .33% in the company's rate-of-return and, therefore, would be unlikely to result in over-earnings. Staff recommended that such changes not be allowed to become effective until at least 12

months after a Commission decision in an audit or rate case and that such a limit be placed on the cumulative total of all applications for a company's rate changes filed between rate cases or audits. Furthermore, Staff urged that a company choosing to implement tariff changes within the described parameters be required to agree, in writing, that it would not increase local rates pursuant to K.S.A. 66-2007(b) by a cumulative amount exceeding the limitation placed on increases to its required revenue. Staff's April 28, 2004 Comments, ¶ 6. Staff noted under this proposal a local exchange carrier would be allowed to increase rates for optional and non-essential services and not be limited to increases in rates for basic local service in accordance with K.S.A. 66-2007(b). Authorizing such increases between audits would allow a company to recover its revenue requirement from tariff rates for services provided to customers rather than from subsidies of these services through the KUSF as long as the tariff rates are within the boundary of reasonableness. Staff opined that adopting its proposal as a standard of reasonableness would permit limited rate increases between rate cases for RLECs that receive subsidies from the KUSF. Staff's April 28, 2004 Comments, ¶ 7.

6. The Commission requests comments on Staff's proposal. Interested parties should also submit any alternative proposals for addressing proposed tariff changes in light of the Court's decision. The Commission is especially interested in views on whether the scope of the KUSF audit proceeding should be changed to address the company's specific rates for services in some fashion.

7. All RLECs are made parties to this docket. Citizens' Utility Ratepayer Board ("CURB") is also made a party to this docket. Any other entities that want to participate actively in this docket and address the issues must file a petition to intervene no later than June 20, 2004. The service list is available on the Commission's web page for this docket. Parties that intervene in this docket are reminded that local counsel is required for all out-of-state attorneys appearing before the Commission. Kansas Supreme Court Rule 116(c) (2003 Kan. S. Ct. R. Annot. 170.)

8. The Commission finds that expenses reasonably attributable to this investigation will exceed \$100, and assesses these expenses against the rate of return regulated local exchange carriers pursuant to K.S.A. 66-1502. This assessment shall begin three days after notice of the assessment is given by service of this Order by United States mail. The rate of return regulated local exchange carriers are hereby notified that they may request a hearing on this assessment in accordance with the provisions of the Kansas Administrative Procedure Act, K.S.A. 77-501, *et seq.* Attachment 1 to this order sets out the companies that are assessed for the costs of this investigation.

IT IS, THEREFORE, BY THE COMMISSION ORDERED THAT:

- A. Interested parties should submit comments as set forth above no later than July 1, 2004, and reply comments by July 21, 2004.
- B. All rate of return regulated local exchange carriers and CURB are made parties to this docket. Other interested parties shall file petitions to intervene no later than June 20, 2004.
- C. Costs of this investigation are assessed to the rate of return regulated local exchange carriers.
- D. Any party may file a petition for reconsideration of this Order within fifteen days of the date this order is served. If service is by mail, service is complete upon mailing and three days may be added to the above time frame.
- E. The Commission retains jurisdiction over the subject matter and the parties for the purpose of entering such further order or orders as it may deem necessary and proper.

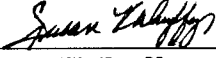
BY THE COMMISSION IT IS SO ORDERED.

Moline, Chair; Wine, Com.; Krehbiel, Com.

ORDER MAILED

Dated: JUN 04 2004

JUN 07 2004


Executive Director

Susan K. Duffy
Executive Director

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ATTACHMENT A

Blue Valley Tele-Communications, Inc.
Bluestem Telephone Company, Inc.
Cass County Telephone Company
Columbus Telephone Co. Inc.
Council Grove Telephone Company
Craw-Kan Telephone Cooperative, Inc.
Cunningham Telephone Company, Inc.
Elkhart Telephone Company, Inc.
Golden Belt Telephone Association
Gorham Telephone Company
H&B Communications, Inc.
Haviland Telephone Company, Inc.
Home Telephone Company, Inc.
J.B.N. Telephone Company, Inc.
Kan-Okla Telephone Assn., Inc.
LaHarpe Telephone Company, Inc.
Madison Telephone LLC
Mo-Kan Dial, Inc.
Moundridge Telephone Company
Mutual Telephone Company
Peoples Telecommunications, LLC
Pioneer Telephone Assn., Inc.
Rainbow Telecommunications Association, Inc.
Rural Telephone Service Company, Inc.
S&A Telephone Company, Inc.
S&T Telephone Cooperative Association, Inc.
South Central Telephone Assn., Inc.
Southern Kansas Telephone Company, Inc.
Sunflower Telephone Company, Inc.
Totah Telephone Company, Inc.
Tri-County Telephone Association, Inc.
Twin Valley Telephone, Inc.
United Telephone Assn., Inc.
Wamego Telecommunications Company, Inc.
Wheat State Telephone Company, Inc.
Wilson Telephone Company, Inc.
Zenda Telephone Company, Inc.