

0001

1 BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION

2 COMMISSION

3 WASHINGTON UTILITIES AND)
 4 TRANSPORTATION COMMISSION,)
 5 Complainant,) DOCKET NO. UT-061777
 6 vs.) Volume I
 7) Pages 1 - 30
 8 VERIZON NORTHWEST, INC.,)
 9 Respondent.)

10 A prehearing conference in the above matter
 11 was held on May 7, 2008, at 1:33 p.m., at 1300 South
 12 Evergreen Park Drive Southwest, Olympia, Washington,
 13 before Administrative Law Judge ANN E. RENDAHL.

14 The parties were present as follows:

15 WASHINGTON UTILITIES AND TRANSPORTATION
 16 COMMISSION, by GREGORY J. TRAUTMAN, Assistant Attorney
 17 General, 1400 South Evergreen Park Drive Southwest,
 Post Office Box 40128, Olympia, Washington 98504;
 telephone, (360) 664-1187.

18 VERIZON NORTHWEST, INC., by GREGORY M.
 19 ROMANO, General Counsel, Northwest Region, 1800 41st
 Street, WA 0105GC, Everett, Washington 98201;
 telephone, (425) 261-5460.

20 DEPARTMENT OF DEFENSE, FEDERAL EXECUTIVE
 21 AGENCIES, by STEPHEN S. MELNIKOFF, Principal
 22 Telecommunications Trial Counsel, Regulatory Law
 Office, U.S. Army Litigation Center, 901 North Stuart
 23 Street, Suite 700, Arlington, Virginia, 22203-1837;
 telephone, (703) 696-1643.

24 Kathryn T. Wilson, CCR

25 Court Reporter

0002

1 WEBTEC, by ARTHUR A. BUTLER (via bridge
2 line), Attorney at Law, Ater Wynne, 601 Union Street,
3 Suite 1001, Seattle, Washington 98101; telephone,
4 (206) 623-4711.

5 PUBLIC COUNSEL, by SIMON J. FFITCH, Assistant
6 Attorney General, 800 Fifth Avenue, Suite 2000,
7 Seattle, Washington 98104; telephone, (206) 389-2055.

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0003

1

2

INDEX OF EXHIBITS

3

4

EXHIBIT:

MARKED:

OFFERED:

ADMITTED:

5

6

1

7

9

9

7

2 - 9

8

9

9

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

0004

1 P R O C E E D I N G S

2 JUDGE RENDAHL: Let's be on the record. Good
3 afternoon. I'm Ann Rendahl, the administrative law
4 judge presiding over this proceeding. We are here
5 before the Washington Utilities and Transportation
6 Commission this Wednesday, May 7th, 2008, for a hearing
7 concerning a settlement agreement filed in Docket
8 UT-061777, which is captioned here at the Commission,
9 Staff investigation regarding agreements for directory
10 services between Verizon Northwest, Inc., and Idearc
11 Media Corporation, formally Verizon Information
12 Services, Inc.

13 So we are here this afternoon to hear
14 testimony from the parties concerning the settlement
15 and to allow the Commission to inquire about the terms
16 of the settlement to determine if the settlement meets
17 the requirements for approving a settlement; namely,
18 that the settlement is lawful, that it's supported by
19 the evidence, and that it's in the public interest.

20 On April 14th, the parties to the settlement
21 filed an agreement with the Commission, and after
22 conferring with all the parties by teleconference, the
23 parties agreed to today's date for a hearing. On April
24 22nd, the Commission issued a notice of the hearing.
25 On May 1st, the parties filed with the Commission a

0005

1 narrative statement that supports the settlement
2 agreement, so that's the background to where we are
3 today. I guess it all started on November 21st, 2006,
4 when Verizon filed a number of agreements concerning
5 the spin-off of the directory business to Idearc.

6 So let's take appearances and then we will
7 start in with witnesses' statements and witnesses and
8 exhibits and all of that good stuff. So before we go
9 any farther and because we haven't taken appearances in
10 this docket, that means you have to give all that fun
11 information, name, who you represent, address,
12 telephone number, fax -- don't know why we do that
13 anymore -- and e-mail address, so starting with
14 Verizon.

15 MR. ROMANO: Yes. Thank you, Your Honor.
16 It's Gregory M. Romano, and I'm general counsel of
17 Verizon Northwest. My business address is 1800 41st
18 Street, Everett, Washington, 98201; phone number,
19 (425) 261-5460; fax, (425) 261-5262, and e-mail
20 address, gregory.m.romano@verizon.com.

21 JUDGE RENDAHL: Appearing with you?

22 MR. ROMANO: Appearing with me is Paul
23 Vasington who is a former chairman of the Massachusetts
24 Department of Telecommunications and Energy and
25 currently state public policy director for Verizon. He

0006

1 will provide his information.

2 JUDGE RENDAHL: If you are a witness, then we
3 will address that later, so unless you are stating an
4 appearance as an attorney, we don't need to talk to you
5 now yet. For Staff?

6 MR. TRAUTMAN: Thank you. Gregory J.
7 Trautman, assistant attorney general for Commission
8 staff. My address is 1400 South Evergreen Park Drive
9 Southwest, Post Office Box 40128, Olympia, Washington,
10 98504. My telephone number is area code (360)
11 664-1187. My fax number is area code (360) 586-5522,
12 and my e-mail address is gtrautma@wutc.wa.gov.

13 JUDGE RENDAHL: Thank you, and for Public
14 Counsel.

15 MR. FFITCH: Simon ffitich, assistant attorney
16 general, Public Counsel section, 800 Fifth Avenue,
17 Suite 2000, Seattle, Washington, 98104-3188; phone,
18 (206) 389-2055; fax, (206) 464-6451; e-mail,
19 simonf@atg.wa.gov.

20 JUDGE RENDAHL: Thank you, and for the
21 Department of Defense and other agencies?

22 MR. MELNIKOFF: My name is Steven S.
23 Melnikoff. I represent the Department of Defense and
24 all other federal executive agencies. My business
25 address is the regulatory law office of the United

0007

1 States Army Litigation Center, 901 North Stuart Street,
2 Suite 700, Arlington, Virginia, 22203-1837. Telephone
3 number is (703) 696-1643. Fax number is
4 (703) 696-2960, and my e-mail address is
5 stephen.melnikoff@hqda.army.mil.

6 JUDGE RENDAHL: For WeBTEC on the bridge
7 line?

8 MR. BUTLER: This is Arthur A. Butler from
9 the law firm Ater Wynne, LLP. I'm appearing on behalf
10 of WeBTEC. My address is 601 Union Street, Suite 1501,
11 Seattle, Washington, 98101-2301; telephone number,
12 (206) 623-4711; fax, (206) 467-8406, and e-mail is
13 aab@aterwynne.com.

14 JUDGE RENDAHL: Thank you very much. Is
15 there anyone else on the bridge line who wishes to make
16 an appearance at this time? Hearing nothing, let's go
17 forward with the next phase of the proceeding. I think
18 first we should talk about and get on the record the
19 exhibits in this matter. We haven't had a prehearing
20 in this case. We've just jumped right into the
21 hearing.

22 Based on our off-the-record conversations
23 before the hearing, I would mark the settlement
24 agreement that was filed in this case on April 14th as
25 Exhibit 1; the narrative supporting settlement

0008

1 agreement that was filed on May 1st as Exhibit 2. Is
2 there any appropriate order for the agreements?

3 MR. ROMANO: No, no order is necessary.

4 JUDGE RENDAHL: Then I'll just follow the
5 order that's in my book, however that came to be. I'll
6 mark as Exhibit 3 the billing services agreement
7 between Idearc Media Corporation and Verizon Services
8 Corporation; as Exhibit 4, the branding agreement
9 between Verizon Licensing Company and Idearc Media
10 Corporation that's dated November 17, 2006; as
11 Exhibit 5, a distribution agreement between Verizon
12 Communications, Incorporated, and Idearc, Incorporated,
13 dated November 13th, 2006.

14 I'll mark as Exhibit 6 an Intellectual
15 Property Agreement between Verizon Services Corporation
16 and Idearc Media Corporation, dated November 17, 2006.
17 As Exhibit 7, I'm marking a noncompetition agreement
18 between Idearc Media Corporation and Verizon
19 Communications, Incorporated, entered into on November
20 17, 2006, and marking as Exhibit 8 a publishing
21 agreement among Verizon Communications, Incorporated,
22 Verizon Services Corporation, and Idearc Media
23 Corporation that's dated November 17, 2006; as
24 Exhibit 9, a listing license agreement between Idearc
25 Media Corporation and the Verizon Telephone Operating

0009

1 Companies listed in Exhibit 1 to the agreement, and
2 this was entered into on November 17, 2006.

3 Except for Exhibit 9, which is not on yellow
4 paper and does not appear to be marked as confidential,
5 what's been marked at Exhibit 3 through 8 were all
6 submitted on yellow paper and appear to be marked as
7 confidential; is that correct?

8 MR. ROMANO: Correct.

9 JUDGE RENDAHL: Are there any objections to
10 admitting into the record what I've marked as
11 Exhibits 1 through 9?

12 MR. TRAUTMAN: Staff has no objection.

13 MR. ROMANO: No objection.

14 MR. MELNIKOFF: No objection.

15 MR. FFITCH: No objection.

16 JUDGE RENDAHL: Those exhibits will be
17 entered into the record, and we will refer to them
18 during the hearing, if necessary.

19 I will note that the settlement agreement,
20 there is a confidential version of the settlement
21 agreement. It has confidential information in it, so
22 that document should also be marked as confidential. I
23 do not believe I received a confidential version of the
24 narrative. Are you aware whether that is considered
25 confidential?

0010

1 MR. TRAUTMAN: No, the narrative is not.

2 JUDGE RENDAHL: So given that we have a
3 number of confidential exhibits in the record, we need
4 to be careful not to refer specifically to the
5 information that is confidential in those documents.
6 If there comes of point when we need to do that, we
7 will have to stop the hearing and close it for a
8 confidential hearing. I don't think we will need to
9 get to that point. I just wanted to get that on the
10 record.

11 So the next thing on our agenda, I believe,
12 is off the record, Mr. Trautman indicated he would make
13 an initial statement, and if the other parties wish to
14 make initial statements as well, you will have that
15 opportunity. Mr. ffitch?

16 MR. FFITCH: This is probably in excess of
17 caution, Your Honor, but you mentioned that Exhibit 1
18 is designated as confidential at the present time,
19 Exhibit 1-C, and that is correct at this time.
20 However, should the Commission approve the settlement
21 agreement, the agreement provides on a going-forward
22 basis that that exhibit would become nonconfidential at
23 that time.

24 JUDGE RENDAHL: Thank you for that
25 clarification. I think everybody would agree to that.

0011

1 MR. ROMANO: Yes.

2 MR. TRAUTMAN: Yes.

3 JUDGE RENDAHL: So for now, it will be
4 considered confidential, and if the Commission approves
5 the settlement, we will remove the confidential
6 designation from the exhibit.

7 MR. ROMANO: Your Honor, if it would make it
8 easier, we could also refile an unredacted version or
9 something after the Commission order becomes in effect,
10 if that would be helpful.

11 JUDGE RENDAHL: That would probably be the
12 best.

13 MR. TRAUTMAN: Actually, the entire agreement
14 is not confidential. It's just certain redactions.

15 JUDGE RENDAHL: Then why don't we just
16 provide that following approval, if the Commission does
17 so, then Verizon will file a clean copy,
18 nonconfidential copy of the settlement for the record.

19 MR. ROMANO: That would be fine, Your Honor.

20 JUDGE RENDAHL: So is there anything else
21 before we start in with initial statements and
22 questions; Mr. Trautman?

23 MR. TRAUTMAN: Thank you, Your Honor. As the
24 parties indicated in the narrative that was filed in
25 conjunction with the settlement agreement, Verizon

0012

1 Northwest filed several agreements on November 22nd,
2 2006, related to the spin-off of Idearc, the directory
3 publishing operation, and Staff then commenced an
4 investigation into the matter looking into the possible
5 impact of that spin-off, if any, on Verizon's
6 intrastate retail rates.

7 Since that time, Staff, along with Verizon,
8 Public Counsel, WeBTEC, and the Department of Defense,
9 have engaged in numerous discussions and conferences
10 and have conducted significant informal discovery and
11 received several documents related to this matter. As
12 the narrative indicates, the parties had different
13 positions not only on the merits but whether the
14 Commission had jurisdiction over the matter. The
15 jurisdictional issue, we would note for purposes of
16 resolving this agreement, has been resolved in
17 Paragraph 3(d)4 of the settlement, which is on Page 6,
18 which specifically says that no party will challenge
19 the agreement or the Commission's authority to adopt
20 the agreement and to hold each party to the terms of
21 the agreement or otherwise enforce the terms.

22 So therefore, if the Commission approves the
23 agreement, whatever jurisdictional challenges there
24 might have been would become moot, and if the
25 Commission were not to adopt and approve the agreement,

0013

1 then the parties as indicated in the narrative, have
2 differing positions on the Commission's jurisdiction,
3 particularly under the affiliated intrastatutes.

4 In the course of the discussions and
5 discovery between the parties, we had to look at how
6 large of an amortization figure there should be, and
7 looking at that, you would look at first of all, what
8 is the overall value of business. We had disagreements
9 on that issue, on how much should be attributable to
10 Washington rate payers, and if there were an
11 amortization period, what length of amortization it
12 should be, among other issues.

13 Following the discussions, the parties have
14 arrived at the agreement that is set forth in the
15 settlement, including the particulars that are in the
16 confidential pages of the agreement describing the
17 terms of an amortization that would be used in future
18 rate cases, AFOR filings, or financial reports that
19 would be filed by Verizon.

20 As Mr. ffitch indicated earlier, because
21 portions of the agreement were a product of
22 negotiations, they've been filed as confidential, but
23 if the Commission approves the agreement, they would
24 become public figures, and Verizon has agreed to file
25 an unredacted version of the agreement.

0014

1 The settlement is a product of compromise
2 among all the parties, and as expressed in the
3 narrative, the parties all believe that it furthers the
4 public interest for the reasons stated, and the parties
5 would request that the Commission approve the
6 agreement.

7 JUDGE RENDAHL: Thank you. Mr. Romano, do
8 you have anything to follow-up?

9 MR. ROMANO: Yes, thank you. The one thing I
10 wanted to highlight was the inclusive nature of the
11 discussions that led to the settlement. I believe
12 Mr. Trautman referred to this generally in process that
13 was used to arrive at a settlement, but the Staff and
14 Public Counsel sought for this to be an open process at
15 the outset, invited interested parties from Verizon
16 Northwest's last rate case to attend an opening
17 meeting, and the result was you had all interested
18 parties at the table, if you will, from the beginning
19 through the informal discovery process, through the
20 negotiation process, and of course it was always
21 professional, but I would say that negotiating one
22 against four is not necessarily a fun experience.

23 I think the result is that you have a
24 settlement of all interested parties, and because of
25 that, and particularly because of the language

0015

1 Mr. Trautman cited, if the Commission approves the
2 agreement in full, then the Commission does not need to
3 grapple with many threshold jurisdictional and other
4 types of issues, and because we have all parties that
5 are interested in the matter involved in the
6 settlement, I think that should go a long way to
7 showing the agreement is in the public interest and to
8 avoiding time-consuming litigation that would otherwise
9 result. Thank you.

10 JUDGE RENDAHL: Thank you. Any additional
11 follow-up on those initial statements? All right.
12 With that, let's be off the record while we convene our
13 panel.

14 (Discussion off the record.)

15 JUDGE RENDAHL: We now have a panel
16 consisting of Mr. Vasington for Verizon, Paula Strain
17 for Commission staff, Robert Spangler for the Federal
18 Agencies, and Michael Brosch, who is on the bridge
19 line, for Public Counsel, and those are the four
20 witnesses we have on the panel.

21 MR. FFITCH: I'll indicate that Mr. Brosch
22 was jointly retained by Staff and Public Counsel.

23 JUDGE RENDAHL: Thank you for that
24 clarification. So what we are going to do is I'll have
25 each one of you, starting with Mr. Vasington on the

0016

1 left and then ending with Mr. Brosch on the conference
2 bridge, stating your name, who you are representing as
3 a witness, and your address, and then after you've all
4 given that identifying information, then I'll give you
5 all the oath, and then are we starting with
6 Mr. Vasington or Ms. Strain or initial statements? So
7 we will start with Ms. Strain. So starting with
8 Mr. Vasington, state your information for the record,
9 please.

10 MR. VASINGTON: My name is Paul B. Vasington.
11 I'm a director of state public policy with Verizon. My
12 business address is 185 Franklin Street, Boston,
13 Massachusetts, 02110.

14 JUDGE RENDAHL: And Ms. Strain?

15 MS. STRAIN: My name is Paula M. Strain,
16 S-t-r-a-i-n. I'm the deputy assistant director of
17 telecommunications for the staff of the Washington
18 Utilities and Transportation Commission. My address is
19 1300 South Evergreen Park Drive Southwest, Olympia,
20 Washington, 98504.

21 JUDGE RENDAHL: Mr. Spangler?

22 MR. SPANGLER: I'm Robert W. Spangler. My
23 title is senior consultant at the Washington DC-based
24 consulting firm of Snavelly, King, Majoros, O'Connor and
25 Lee. The firm's address is 1111 14th Street Northwest,

0017

1 Washington, DC, 20005. My preferred mailing address is
2 my residence, which is 17304 137th Avenue Southwest,
3 Vashon, Washington, 98070.

4 JUDGE RENDAHL: So you prefer the other
5 Washington?

6 MR. SPANGLER: I prefer information to me
7 mailed to me at Washington.

8 JUDGE RENDAHL: Mr. Brosch?

9 MR. BROSCHE: I'm Michael Brosch. I'm the
10 president of Utilitech, Inc., and I'm a consultant to
11 Public Counsel and Commission staff. My business
12 address is 740 Northwest Blue Parkway, Suite 2004,
13 Lee's Summit, Missouri, 64086.

14 JUDGE RENDAHL: Thank you very much, and
15 including you, Mr. Brosch, could you all raise your
16 right hand, please?

17

18 Whereupon,

19

THE PANEL,

20 having been first duly sworn, were called as witnesses
21 herein and examined and testified as follows:

22

23 JUDGE RENDAHL: Beginning with you,
24 Ms. Strain?

25

MS. STRAIN: Thank you, Your Honor. The

0018

1 regulatory accounting treatment of revenues from
2 directory advertising has been litigated before this
3 Commission since at least the early 1970's, and I have
4 personally been involved in litigation involving this
5 topic since 1995 on behalf of Commission staff.

6 This issue is one of many valuation and
7 pricing issues that arise from transactions between
8 regulated companies and their relate regulated
9 affiliates. The ability of an owner of an affiliated
10 group of companies can result in actions being taken
11 that shift costs to affiliates subject to
12 rate-of-return regulation and shifting profits to
13 nonregulated affiliates in the same group.

14 Since rate-of-return regulation bases rates
15 on cost and a set return on investment, and
16 nonregulated companies can charge prices without being
17 limited to a set rate of return, non arms-length
18 behavior among members of the affiliated group can
19 maximize the profits from the group as a whole.

20 With respect to cases involving directory
21 advertising through affiliates, the issue before the
22 Commission in all of the cases that have been before it
23 has been held best to identify, quantify, and record
24 the benefit imparted to the owner of a directory
25 advertising business by its association with the

0019

1 regulated incumbent telephone company. This would be
2 easy if the benefits were tangible, like building or
3 goods. In many cases, however, as in this case, the
4 benefits at issue are intangible and in some cases are
5 never quantified or recorded on the books of either the
6 directory advertising affiliate or the regulated
7 telephone company.

8 In the current case, the benefits transferred
9 were publishing rights and a commitment not to compete,
10 among other agreements that the companies made among
11 themselves. Through its parent, Verizon Communications
12 Inc., Verizon Northwest, the regulated incumbent
13 telephone company was required to enter into agreements
14 to grant these rights to Idearc for a considerable
15 number of years. In exchange for these rights and
16 commitments, Verizon Communications received cash and
17 transferred debt to Idearc. However, none of the
18 benefits of the transaction were transferred to Verizon
19 Northwest or to the regulated companies.

20 The settlement agreement before you succeeds
21 in capturing the value of the publishing rights and the
22 noncompete commitments and ensuring that those benefits
23 will be recognized for the benefit of Verizon
24 Northwest's Washington ratepayers in future proceedings
25 in which Verizon's rates are at issue. The settlement

0020

1 agreement also provides that the value will be
2 recognized and Verizon Northwest's financial filings
3 with the Commission.

4 In the long and formal review process that
5 involved all the settling parties, the Commission staff
6 identified what it believed to be the value of the
7 Idearc spin-off to Verizon Communications and then
8 quantified what portion of that value should be
9 attributed to Verizon Northwest's Washington
10 ratepayers. The amortization amount and the terms
11 agreed to in the settlement is a compromise of all the
12 parties, but the Staff believes that the settlement
13 provides substantial benefit to Verizon Northwest
14 Washington ratepayers, and it succeeds in avoiding
15 costly and protracted litigation of this issue in any
16 future rate proceeding. The Staff therefore recommends
17 that the Commission approve the settlement. Thank you.

18 JUDGE RENDAHL: Thank you. I'm going to let
19 all of you make your initial statements, and then I
20 have some questions for all of you, so go ahead with
21 your statement, Mr. Vasington.

22 MR. VASINGTON: Good afternoon, Your Honor.
23 I would just like to take a moment to briefly describe
24 the reasons that approval of this settlement is in
25 Verizon's interests and also in the public's interests.

0021

1 First Verizon's interest. Verizon operates in an
2 industry that is highly competitive and subject to
3 rapid technological change in market place uncertainty.
4 In order to respond to these business uncertainties,
5 it's imperative that we don't compound the challenges
6 that we face by adding items of regulatory uncertainty
7 to the mix.

8 Therefore, even though the settlement is
9 different from what we would advocate in a litigated
10 proceeding and different from what we would consider to
11 be an outcome consistent with the unique circumstances
12 of the case, it is more important for us to move
13 forward with an outcome that reduces uncertainty. The
14 settlement agreement provides certainty for Verizon
15 about revenue adjustments in a rate case or earnings
16 review for a set period of time, and also provides that
17 regulatory earnings reporting will include these
18 revenue adjustments.

19 Also, while Verizon is confident in its
20 litigation position, I think it's fair to say that all
21 of the other parties have similar confidence in their
22 own positions so that there would have been protracted
23 and potentially costly litigation for Verizon going
24 forward absent this settlement. Indeed, putting aside
25 legal positions that can best be described by the

0022

1 attorneys, there are a number of issues that would have
2 to be litigated even in developing a number given the
3 unprecedented nature and timing of this transaction.

4 These issues became apparent to us in the
5 negotiations and comprehensive discovery that we did
6 and number of meetings that were described earlier by
7 Mr. Trautman. All of these issues, including element
8 of subjectivity, that would require significant time
9 and attention of the parties as well as the Commission
10 to resolve. Thus, by agreeing on an overall revenue
11 adjustment figure and time period, the parties have
12 avoided presenting complicated disputes to the
13 Commission.

14 In terms of the public's interests, the
15 avoidance of litigation expense and uncertainty is also
16 in the interest of the public as well as Verizon, and
17 that benefits the Commission as well by removing an
18 issue from any contested rate or earnings proceeding
19 that would have required a significant amount of
20 litigation and Commission attention.

21 But the public interest also is served by
22 this settlement for reasons that go beyond just
23 certainty and avoidance of litigation. In Verizon's
24 opinion, the amounts represented as revenue adjustments
25 in the settlement are likely to be higher than any

0023

1 revenue adjustments that would have been included in a
2 rate proceeding over the set time period. The reason
3 for this is noted by both The Staff and Public Counsel
4 who both point out -- I'm quoting from Staff now --
5 "the risks of potentially reduced future directory
6 revenues arising from the competition being faced by
7 directory publishers," and quoting from Public Counsel,
8 "anticipated declines in future directory publishing
9 income," and to be clear, I'm quoting from the
10 narrative descriptions here.

11 JUDGE RENDAHL: Thank you.

12 MR. VASINGTON: Just to highlight the
13 uncertain nature of the directory publishing business,
14 it's instructive to look at what's happened to Idearc
15 in the past year. The 52-week high for Idearc common
16 stock is roughly \$38 per share, while today's price is
17 around five dollars per share. Including the revenue
18 adjustments in Verizon's reporting requirements for
19 estimating intrastate earnings also is in the public
20 interest because the earnings' reports will help to
21 assess in real time whether the revenue adjustments
22 cause Verizon's earnings to exceed its cost of capital
23 over the relevant time period.

24 Finally, I would note that in my experience
25 as a commissioner and Commission staffer, when all of

0024

1 the interested parties and their varied interests agree
2 on a settlement, that in and of itself is strong
3 evidence that the result is in the public interest.
4 Thanks for the opportunity to address the reasons why
5 this settlement should be approved, and at the
6 appropriate time, I would be happy to answer any
7 questions.

8 JUDGE RENDAHL: Thank you. Mr. Spangler, do
9 you have a statement?

10 MR. SPANGLER: Yes. The DOD and the other
11 federal agencies believe that the agreement is in their
12 own personal interest and in the public interest as was
13 explained in the narrative statement.

14 With respect to the private interests, the
15 Federal Agencies are a large customer of Verizon
16 Northwest's business telecommunications offerings.
17 They are accordingly interested that the rates for
18 those services to be just and reasonable and also that
19 the rates of other carriers who take service from
20 Verizon charge just and reasonable rates.

21 One adjustment that's often made in the
22 rate-making process, especially before this commission,
23 is to impute revenues from affiliated operations that
24 are not conducted by the telephone company, but for a
25 few regulatory reasons resulted in recognition for

1 rate-making purposes. The settlement agreement in this
2 case does, in fact, provide for a revenue imputation
3 amount that will be used over a stated period of years
4 should there be an earnings review or a rate case. The
5 result of the revenue imputation will go far in
6 ensuring that the rates paid by customers, large and
7 small, will be just and reasonable and reflect the
8 appropriate rate-making adjustments without the need to
9 engage in litigation.

10 The public interest is served by this
11 agreement also for the reasons that the other parties
12 have mentioned. DOD and the Federal Agencies was a
13 party to a previous Verizon case that was settled, and
14 just a cursory review of the record in that proceeding
15 shows that literally hundreds of pages were devoted by
16 witnesses to the issue of how directory revenues should
17 be handled. It was a strongly contested issue which
18 was not resolved because the case was settled.

19 By eliminating that issue for a stated period
20 of years, the public interest served by avoiding the
21 expense of litigation, the uncertainty that's involved,
22 and basically, this settlement will allow the parties
23 in a future proceeding, should there be one, to narrow
24 the issues to eliminate uncertainty and to allow for a
25 focus on other contested issues that will conserve both

0026

1 their time and the Commission's resources. For these
2 reasons, DOD, FEA is a signatory to the settlement and
3 strongly supports its adoption.

4 JUDGE RENDAHL: Thank you very much.

5 Mr. Brosch?

6 MR. BROSCH: Thank you. I've been editing my
7 notes as we've gone along here and have just a couple
8 of points to add.

9 First I would observe that historically,
10 directory publishing has been treated as a regulatory
11 asset in Washington with the income stream from that
12 business being credited whenever regular telephone
13 rates are established. The Idearc spin-off separates
14 the publishing business from the consolidated business
15 that contains the regulated telephone operation causing
16 it to be difficult, if not impossible, in the future to
17 effectively quantify that directory revenue credit that
18 needs to be accounted for.

19 So this spin-off event created a monetization
20 of the business that needed to be considered, and
21 through the discovery process and extensive discussions
22 among the parties, we worked through the many questions
23 and issues surrounding evaluation and allocation of
24 that business enterprise value to Washington
25 ratepayers.

0027

1 In the end, we agreed upon a settlement that
2 was structured in a manner similar to the approach and
3 outcome taken by these parties, some of these parties
4 anyway, and ultimately approved by the Commission for
5 Qwest in Docket UT-021120, and for Sprint in Docket
6 UT-051291. It is my belief that the outcome of the
7 settlement with Verizon reasonably quantifies the value
8 of the business and secures future directory benefits
9 for ratepayers, avoiding a contentious issue in future
10 periods, and for these reasons, I believe the
11 settlement should be approved.

12 JUDGE RENDAHL: Thank you very much. You all
13 have answered some of the questions I had. Just to
14 make sure it's clear on the record, the settlement in
15 Paragraph 2 identifies the settlement agreement as the
16 exclusive regulatory treatment in this state on the
17 impact of the spin-off by Verizon Communications, Inc.,
18 of its directory business.

19 So just to clarify, this settlement does not
20 have any immediate impact on ratepayers in the state of
21 Washington. It's a regulatory treatment for
22 consideration in possible future rate cases for cases
23 in which the financial status of Verizon would be
24 considered; is that correct?

25 MS. STRAIN: That is correct, Your Honor.

0028

1 MR. VASINGTON: I would just add that the one
2 immediate impact is that the earnings report will
3 immediately within months reflect the revenue
4 adjustment so that the impact of these adjustments on
5 Verizon's intrastate earnings will be reflected and
6 captured in realtime in a transparent manner.

7 JUDGE RENDAHL: How will that impact
8 consumers in this state?

9 MR. VASINGTON: If the adjustments that are
10 resulting from this settlement would cause Verizon's
11 earnings to exceed its cost of capital, which is
12 generally the measure of evaluating whether a rate case
13 is necessary, if that were to occur, it would appear in
14 these earnings reports and thus potentially trigger a
15 type of proceeding that would affect the customers'
16 rates.

17 JUDGE RENDAHL: So because I was not involved
18 in the Verizon rate case, is there a provision in the
19 Verizon settlement from the rate case triggering an
20 automatic case if the ratio of earnings to cost capital
21 exceed a certain amount? Is there an automatic
22 trigger, or is this something that Staff in its
23 discretion or the Company in its discretion could
24 choose to pursue?

25 MS. STRAIN: There is not an automatic

0029

1 trigger in the rate case settlement. There were not
2 any proceedings such as Mr. Vasington has described
3 would be initiated either by a Staff complaint or on
4 the Commission's own motion or by the Company itself.

5 JUDGE RENDAHL: Thank you. Looking at the
6 settlement in Section 3, III, D, which is the
7 obligations section, 2(a), and it's on Page 5 of the
8 confidential version that I'm looking at. I just want
9 to clarify that my understanding of this provision is
10 that no party to the settlement agreement would
11 advocate a larger annual amortized figure than the
12 amount stated in the settlement as a revenue increase
13 adjustment in future proceedings, and that this
14 limitation applies only to the issues of regulatory
15 treatment of the impact of the spin-off. It doesn't
16 refer to any other -- parties are not precluded from
17 making any other adjustments in future rate cases or
18 other issues; correct?

19 MR. ROMANO: Your Honor, just to clarify the
20 question, you mean issues other than the spin-off?

21 JUDGE RENDAHL: Correct. This does not
22 preclude parties from making proposed adjustments for
23 issues unrelated to the spin-off.

24 MR. TRAUTMAN: That's correct, Your Honor.

25 JUDGE RENDAHL: It is somewhat of a legal

0030

1 question. Just wanted to make sure that there was not
2 so much of a broad statement that it wouldn't be used
3 later to any party's detriment.

4 Having read the settlement and the narrative,
5 I think it's fairly straightforward and clear. Those
6 were my only clarifying questions relating to the
7 settlement just to get on the record the impact and the
8 scope of the settlement, so I do not have any other
9 questions for the witnesses or counsel at this time.
10 If there is anything else that we need to put in the
11 record or any other statements that you all believe
12 should be put into the record, now is the time for
13 that.

14 All right. With that, I think we have
15 concluded the hearing. I would note on the record that
16 this is Ms. Strain's last formal proceeding before the
17 Commission. Who knows whether it will be her last
18 opportunity to ever testify. One never knows, but
19 Ms. Strain is nearing retirement very quickly, and I
20 just wanted to appreciate her contributions to the
21 Commission. With that, we are adjourned. Thank you.

22 (Hearing adjourned at 2:20 p.m.)

23

24

25