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SUPERIOR COURT OF WASHINGTON
FOR SNOHOMISH COUNTY

VERIZON NORTHWEST INC.,

Petitioner,

vs.

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Respondent.

No. 03-2-10227-8

PETITION FOR REVIEW

Verizon Northwest Inc. ("Verizon"), pursuant to RCW 34.05.570(3), petitions this court to review and vacate an Order¹ of the Washington Utilities and Transportation Commission ("WUTC" or "Commission") requiring Verizon to reduce its rates on October 1, 2003 by \$32 million. The WUTC ordered this reduction even though Verizon was earning less than a 3% rate of return, the rate reduction will reduce its earnings to almost zero, and the WUTC previously determined that it would be reasonable for Verizon to earn 9.76%. In ordering this reduction, the Commission violated its statutory and Constitutional obligations to ensure that Verizon's rates are "sufficient."

Accompanying this Petition is Verizon's Motion for Supersedeas, which requests the court to stay the effectiveness of the Rate Reduction Order pending appeal.

¹ *AT&T Communications of the Pacific Northwest v. Verizon Northwest Inc.*, Docket No. UT-020406, Eleventh Supplemental Order (W.U.T.C., Aug. 12, 2003) ("Rate Reduction Order"). A copy of this order is attached as Exhibit A.

PETITION FOR REVIEW -- 1

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I. BACKGROUND

A. Access Charges

The rates the WUTC ordered Verizon to reduce are access charges Verizon collects from long distance companies for the use of Verizon's telephone network to complete long distance calls. When a Verizon customer in Redmond uses AT&T Communications of the Northwest, Inc. ("AT&T") to make a long distance call to a Verizon customer in Everett, the call is carried by Verizon's network from the customer's home to AT&T's network. AT&T then carries the call between Redmond and Everett where it transfers the call to Verizon's network to carry to the Verizon customer in Everett. The fee AT&T pays Verizon for carrying the call from Verizon's customer in Redmond to AT&T is referred to as an "originating access charge." The fee AT&T pays Verizon for carrying the call from AT&T to Verizon's customer in Everett is referred to as a "terminating access charge."

B. The Commission Regulates Verizon's Access Charges

The rates Verizon charges for its telephone services provided within Washington, including its access charges collected from long distance companies like AT&T, are regulated by the WUTC. Those rates, including access charges, must be set by the WUTC to be "fair, just, reasonable, and sufficient."² As explained by the WUTC,

[Verizon's] rates are regulated by the Commission and must be fair, just, reasonable, and sufficient. A decrease in access charges will result in either a decrease in [its] overall profits (which must remain "sufficient") or an offsetting increase in other rates, or some combination of the two.³

In short, the WUTC has recognized that its regulation of Verizon's access charges is subject to the governing legal standards for rate setting in Washington.

² RCW 80.36.080; see also Docket No. UT-970325, *General Order R-450* at 4.

³ *General Order R-450* at 4.

1 **C. The WUTC's Access Charge Rule**

2 The WUTC adopted a rule for setting access charges in WAC 480-120-540. The
3 Washington Supreme Court recently upheld this rule in *WITA v. WUTC*.⁴

4 When the WUTC adopted this rule, it recognized the importance of revenue neutrality
5 when access charges are changed. For example, the rule permits revenue-neutral increases to
6 originating access charges to offset any reductions in terminating charges.⁵

7 In addressing the revenue-neutral aspect of the rule, the Commission explained that the
8 ability of carriers to keep this revenue will be “a function of customer demand” rather than
9 prescriptive regulation.⁶ In making this determination, the Commission expressly rejected the
10 proposals of AT&T and other long distance companies to reduce all access charges to alleged
11 “cost-based” levels, again recognizing that access charges relate directly to overall profits, which
12 must be sufficient.⁷

13 **D. Verizon's Current Access Charges**

14 In 1999, the WUTC approved access charges and other rates for Verizon that it held were
15 “just reasonable and compensatory” and that produced sufficient revenues under Washington
16 law.⁸ Verizon’s current rates fully comply with that order. Verizon’s access charges also fully
17 comply with the WUTC's access charge rule.⁹

18 **E. AT&T's Complaint**

19 In April 2002, AT&T filed a complaint seeking to reduce Verizon’s access charges to
20 alleged “cost-based” rates. Verizon explained that its access charges cannot be reduced in a
21 complaint case because, among other reasons, its access charges complied with the Commission’s
22 access charge rule, and AT&T’s complaint was nothing more than a collateral attack on that rule.

23 ⁴ 148 Wn.2d 887, 64 P.3d 606 (2003).

24 ⁵ *General Order R-450* at 12-13.

25 ⁶ *Id.*

26 ⁷ *Id.* at 18.

⁸ *In the Matter of the Application of GTE Corp. and Bell Atlantic Corp.*, Docket Nos. UT-981367, et al., Fourth
Supplemental Order Approving and Adopting Settlement Agreement (W.U.T.C., Dec. 1999) (“Merger Order”).

⁹ Rate Reduction Order at 12.

1 Verizon also explained that its access charges could not be reduced in a vacuum. It explained that
2 these charges generate a significant part of Verizon's overall revenues, and that the Commission
3 could not, by law, reduce them because Verizon's resulting revenues would not be sufficient
4 without an offsetting increase in other rates.¹⁰

5 **F. The WUTC's Rate Reduction Order**

6 On August 12, 2003, the WUTC issued its Rate Reduction Order requiring Verizon to
7 reduce its access charges by \$32 million. The WUTC concluded that Verizon's access charges
8 are "discriminatory," "unduly preferential," and "cause unreasonable competitive disadvantage."¹¹
9 It reached this conclusion even though it expressly found that Verizon's access charges comply
10 with the WUTC's access charge rule that, in the WUTC's own words, is "pro-competitive,"
11 "competitively neutral," and supports "emerging competition without favoring any class of
12 participants."¹²

13 The Rate Reduction Order refused even to consider whether Verizon's resulting revenues
14 would be legally "sufficient." It stated that "the status of the company's earnings is not
15 relevant."¹³ The Rate Reduction Order failed to explain why Verizon's overall revenues are not
16 relevant in examining its access charges, when it expressly stated that the access charge reductions
17 ordered by the WUTC "will cause a considerable reduction in Verizon's revenues."¹⁴

18 **G. Impact on Verizon of the Rate Reduction Order**

19 The affidavit of Nancy Heuring, Director-Regulatory Accounting for Verizon Services
20 Organization, which is attached to Verizon's Motion for Supersedeas, explains the impact on
21 Verizon of the \$32 million rate reduction required by the WUTC. In short, this access charge
22 decrease amounts to a reduction of 8.5% of Verizon's \$378 million in revenue collected from
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24 ¹⁰ The complete procedural history of this case is summarized in Appendix A to the Rate Reduction Order.

25 ¹¹ Rate Reduction Order at 17, para. 45.

26 ¹² *General Order R-450* at 1, 8, and 11.

¹³ *Id.* at 42, para. 140.

¹⁴ *Id.* at 43, para. 144.

1 services subject to the WUTC's jurisdiction in 2002.¹⁵ Verizon's earnings from these services in
2 2002 were only 2.42%, and this access charge reduction would reduce its earnings to 0.28%; by
3 contrast, its rate of earnings authorized by the WUTC is 9.76%.¹⁶

4 Moreover, to put the magnitude of this revenue reduction in further context, a \$32 million
5 rate reduction would be equal to 24% of the capital investment Verizon made in services subject
6 to the WUTC's jurisdiction in 2002, 41.5% of the amount Verizon spent in 2002 to maintain and
7 repair the network it used to provide those services, and 3.5 months of payroll expense in 2002
8 for Verizon's employees in Washington.¹⁷

9 **H. Verizon's Compliance Filing**

10 As required by the Rate Reduction Order, Verizon filed tariffs implementing the reduced
11 rates on August 22, 2003. Verizon did so under protest. The reduced rates are scheduled to take
12 effect October 1, 2003.¹⁸

13 The Rate Reduction Order does not allow Verizon to increase other rates to offset the
14 access charge reductions. Thus, Verizon will begin losing revenue the very first day the reduced
15 rates take effect. This appeal of the Rate Reduction Order and the accompanying Motion for
16 Supersedeas followed.

17 **II. INFORMATION REQUIRED BY RCW 34.05.546**

18 1. Name and address of petitioner

19 Verizon Northwest Inc.
20 1800 - 41st Street
21 P.O. Box 1003
22 Everett, WA 98206
23
24

25 ¹⁵ Heuring Affidavit at para. 7.

26 ¹⁶ *Id.* at para. 9.

¹⁷ *Id.* at para. 8.

¹⁸ Rate Reduction Order at 43, para. 146.

1 2. Name and address of petitioner's attorney

2 Judith A. Endejan
3 Graham & Dunn
4 Pier 70
5 2801 Alaskan Way, Suite 300
6 Seattle, Washington 98121-1128
7 (206) 624-8300

8 3. Name and address of agency whose action is at issue

9 Washington Utilities and Transportation Commission
10 1300 South Evergreen Park Drive SW
11 P.O. Box 47250
12 Olympia, WA 98504-7250

13 4. Identification of agency action at issue

14 Eleventh Supplemental Order, *AT&T Communications of the Pacific Northwest, Inc. v.*
15 *Verizon Northwest Inc.*, Docket No. UT-020406 ("Rate Reduction Order").¹⁹

16 5. Identification of persons who were parties in the adjudicative proceeding

17 In addition to Verizon the other parties to the proceeding were Complainant AT&T and
18 the following Intervenor: Staff of the Washington Utilities and Transportation Commission;
19 Public Counsel from the Attorney General's Office; Worldcom; the Washington Electronic
20 Business and Telecommunications Coalition; and the Citizen's Utilities Alliance of Washington,
21 Spokane Neighborhood Action Programs.

22 6. Facts that demonstrate petitioner is entitled to obtain judicial review

23 a. *Verizon's Petition satisfies all requirements of the APA*

24 The Rate Reduction Order was issued August 12, 2003, and Verizon's Petition is timely
25 filed and complies with the requirements of the Washington Administrative Procedures Act, RCW
26 Ch. 34.05. Verizon owns property in Snohomish County, which is also its principal place of
27 business. Therefore venue is appropriate under RCW 34.05.514(1). This Petition contains all

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¹⁹ The Rate Reduction Order is a culmination of earlier orders in the docket below, including the Second Supplemental Order (denying Verizon's motion to dismiss), and the Fifth and Seventh Supplemental Orders (striking Verizon testimony and denying Verizon's motion to compel). Verizon appeals the WUTC's findings adverse to Verizon in all of these orders, which are attached as Exhibits B, C and D.

1 that is required by RCW 34.05.546. Finally, as discussed above, relief is warranted because the
2 Rate Reduction Order has substantially prejudiced Verizon. Therefore, Verizon is entitled to
3 obtain judicial review under RCW 34.05.570(3).

4 *b. The Rate Reduction Order is unlawful*

5 The Rate Reduction Order requires Verizon to revise its access charges effective
6 October 1, 2003, and acknowledges that these changes will reduce Verizon's revenues by
7 approximately \$32 million per year. The Rate Reduction Order is unlawful for many reasons,
8 including (1) it establishes unjust, unreasonable, and confiscatory rates in violation of law, (2) it
9 erroneously interprets and applies Washington statutes and the Commission's rules, and (3) it is
10 not supported by substantial evidence. Given this, Verizon is entitled to judicial review.

11 The following additional facts support Verizon's request for judicial review:

12 (i) Verizon is a public utility that provides telecommunications services in Washington. Its
13 rates, including its access charges, are set by the Commission. The Commission is "charged by
14 law with the setting of just, reasonable, and sufficient public utility rates," which means that the
15 utility must be allowed to charge rates that "will yield to the utility its aggregate allowed revenue
16 requirement."²⁰

17 (ii) In general, a utility's annual revenue requirement must be sufficient to cover (a) the
18 utility's annual operating expenses, (b) the annual cost of the utility's network, and (c) a
19 reasonable rate of return on the utility's investment, i.e., a reasonable profit.²¹ The Commission is
20 responsible for setting the utility's revenue requirement and for establishing rates that afford the
21 utility an opportunity to earn this revenue requirement.²²

22 (iii) The Commission last examined Verizon's revenue requirement in December 1999,
23 when it entered its order approving the Bell Atlantic-GTE merger (the "Merger Order").²³ In the

24 _____
²⁰ *POWER v. WUTC*, 104 Wn.2d 798, 711 P.2d 319, 324-26 (1985); *see also* RCW 80.36.080.

25 ²¹ *Id.*

26 ²² *Id.*

²³ The merger resulted in the creation of Verizon Corporation. Prior to the merger, Verizon Northwest operated under the name GTE Northwest.

1 Merger Order, the Commission approved a settlement that reduced Verizon's revenues and re-set
2 Verizon's access charges. The Commission specifically found that the adjustments to Verizon's
3 revenue "produce fair, just, and compensatory rates and charges" for all Verizon services.²⁴

4 (iv) The Commission refused to consider Verizon's overall earnings and revenue
5 requirement in the proceeding below. Also, the Commission struck much of Verizon's surrebuttal
6 testimony, including testimony on Verizon's overall earnings, over Verizon's objections.²⁵

7 (v) Verizon's current access charges comply with the Merger Order.

8 (vi) Verizon's current access charges also comply with the Commission's access charge
9 rule, 480-120-540. That rule, which was affirmed earlier this year by the Washington Supreme
10 Court, sets forth a specific rate methodology for calculating terminating access charges, and
11 permits revenue-neutral increases to originating access charges to offset any reductions in
12 terminating charges. The stated purpose of the rule, in the Commission's words, is to "conform
13 Washington's telecommunications access charge system with state and federal laws encouraging
14 competition." In adopting the rule, the Commission explained that it is "consistent with the public
15 interest (including economic theory, law, and public policy)" and ensures that "no company is
16 unfairly prejudiced."²⁶

17 (vii) The Commission denied Verizon's request that AT&T be required to prove its claims
18 that Verizon was engaging in an unlawful price squeeze and harming AT&T. When Verizon
19 asked AT&T in discovery requests to provide all the data to support these claims and to quantify
20 precisely how much, if at all, AT&T's current prices would decrease if Verizon's access charges
21 were reduced, AT&T refused to respond. Although an administrative law judge ordered AT&T
22 to provide this information, the Commission reversed, holding that it was not relevant.²⁷

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25 ²⁴ *Merger Order* at 25.

26 ²⁵ *See, e.g., Fifth, Seventh Supplemental Order and Ninth Supplemental Order.*

²⁶ *General Order R-450* at 1, 6-11.

²⁷ *Fifth Supplemental Order* at 17, para. 50.

1 Verizon will discuss these points and the other errors contained in the Rate Reduction
2 Order when it files its brief, but the preceding facts illustrate that Verizon is entitled to judicial
3 review and that the Rate Reduction Order must be vacated.

4 7. Petitioner's reasons for believing relief should be granted

5 The court should grant relief for the reasons set forth above and under the criteria set forth
6 in RCW 34.05.570(3):

7 a. *The order violates constitutional provisions on its face or as applied*

8 The access charge reductions required by the Rate Reduction Order are unjust,
9 unreasonable and confiscatory in violation of the Fifth and Fourteenth Amendments to the United
10 States Constitution and Washington Const., Art. I § 3.

11 b. *The order is outside the statutory authority or jurisdiction of the*
12 *Commission*

13 (i) The Rate Reduction Order violates RCW 80.36.080 because (1) it established charges
14 that are not "fair, just, reasonable and sufficient" and (2) it failed even to consider whether the
15 access charge reductions would result in sufficient overall revenues to Verizon.

16 (ii) The Rate Reduction Order is unlawful because it changed or ignored Commission
17 rules in a company-specific complaint proceeding.

18 c. *The Commission has engaged in unlawful procedure or decision-making process*
19 *or has failed to follow a prescribed procedure*

20 The Commission engaged in unlawful procedure in that it:

21 (i) effectively repealed Commission rules, orders and policies on access charge policy and
22 imputation without following the lawful procedure for such repeal;

23 (ii) sustained a procedure that precluded Verizon from presenting evidence in defense to
24 AT&T's complaint;

25 (iii) removed AT&T's burden to prove the allegations of its complaint by relieving AT&T
26 of any requirement to show that it had been unduly prejudiced or unreasonably prejudiced or

1 placed at competitive advantage under RCW 80.36.186, and by allowing AT&T to withhold
2 evidence to this effect in discovery;

3 (iv) issued a series of confusing, inconsistent and at times conflicting orders regarding the
4 scope of the proceeding and procedure;

5 (v) established a policy for setting access charges that must be followed by other carriers
6 providing access services without notifying these non-parties and providing them with an
7 opportunity to be heard;

8 (vi) established access charges for Verizon without reasoned consideration of whether the
9 order may reasonably be expected to yield sufficient rates and to maintain Verizon's financial
10 integrity; and

11 (vii) unlawfully shifted the burden of proof on the sufficiency of Verizon's earnings and
12 revenue requirement from AT&T and other parties to Verizon.

13 *d. The agency has erroneously interpreted or applied the law*

14 The Rate Reduction Order makes the following errors of law:

15 (i) it constitutes impermissible single-issue ratemaking;

16 (ii) it violates the Commission's duty to set just, reasonable and sufficient rates under
17 RCW 80.36.080, which means that the utility must be allowed to set rates that "will yield to the
18 utility its aggregate revenue requirements";²⁸

19 (iii) it misinterprets and misapplies RCW 80.36.186 in finding that rates lawfully
20 established pursuant to Commission rule could provide an undue or unreasonable preference or
21 advantage or cause AT&T undue or unreasonable prejudice or competitive disadvantage;

22 (iv) it misinterprets the complaint statute RCW 80.04.110 to relieve a complainant of any
23 burden of proof under RCW 80.36.180 or 80.36.186;

24 (v) as applied, it discriminates against Verizon by requiring it to make access charge
25 reductions that other service providers are not required to make;

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²⁸ *POWER v. WUTC*, 104 Wn. 2d 798, 711 P.2d 319, 324-26 (1985).

1 (vi) it misinterprets the revenue benchmark formula which excludes interstate universal
2 service fund support from the interim terminating access charge (ITAC), which was created as a
3 part of the WUTC's access charge rule; and

4 (vii) it finds that Verizon's toll rates pass the Commission's imputation test but that
5 nonetheless its access charges violate RCW 80.36.186.

6 e. *The Rate Reduction Order is not supported by the evidence that is substantial*
7 *when viewed in light of the whole record before the Court*

8 The Rate Reduction Order has no evidentiary support on the following issues:

9 (i) the Commission's finding of prejudice to sustain a violation of RCW 80.36.186;

10 (ii) the Commission's adjustment to the ITAC;

11 (iii) the Commission's conclusion that Verizon's access charges must be reduced to the
12 same level as Qwest's charges; and

13 (iv) the Commission's assumption that Verizon can avoid or mitigate its losses.

14 f. *The agency has not decided all issues requiring resolution*

15 The Commission has failed to determine whether its ordered \$32 million access charges
16 reduction will yield "sufficient" rates to Verizon in contradiction of RCW 80.36.180.

17 g. *The order is inconsistent with the Commission's rules and fails to demonstrate a*
18 *rational basis for this inconsistency*

19 (i) The Rate Reduction Order finds that rates established pursuant to its access charge
20 rule, WAC 480-120-540, are nonetheless unlawful. By doing so it acts inconsistent with the rule,
21 and fails to explain how its rule is sustainable in light of the order.

22 (ii) The Rate Reduction Order finds that Verizon's toll rates satisfy state law and the
23 Commission's imputation rule, but concludes that Verizon's access charges and toll rates
24 disadvantage long distance carriers.

