

MEMORANDUM

TO: Chairman Richard L. Mathias
Commissioner Terry Harvill
Commissioner Edward Hurley
Commissioner Ruth K. Kretschmer
Commissioner Mary Frances Squires

FROM: Eve Moran and Phillip A. Casey, Hearing
Examiners

DATE: May 23, 2001

SUBJECT: Illinois Bell Telephone Company

Application for review of alternative regulation plan.

Illinois Bell Telephone Company

Petition to rebalance Illinois Bell Telephone Company's
carrier access and network access line rates.

Citizens Utility Board and The People of the State of Illinois
-vs-
Illinois Bell Telephone Company

Verified Complaint for a reduction in Illinois Bell Telephone
Company's rates and other relief.

RE: 98-0252/98-0335/00-0764 Consol. Hearing Examiners
Proposed Order.

DISCUSSION

Here is a brief summary of the HEPO for this consolidated proceeding.

1. On the basis of a comprehensive and thorough review of the 10 items that the Commission set out in the original Alt Reg Order, and which includes the statutory requirements and goals under Section 13-506.1, we submit that the Plan has worked reasonably well and should be continued, albeit with certain modifications to correct its failings. (See, Parts II and III of the HEPO). In other words, on the whole of the record

evidence, having the Company go back to rate of return regulation is neither required nor desirable.

2. Having considered the merits of a number of proposed modifications to the Price Cap Index formula we have adopted the following: a) in most aspects, the formula itself shall remain the same; b) on a going forward basis, a chain weighted Gross Domestic Product Price Index shall be used as the Inflation measure, rather than the older fixed weight version; c) the X factor within the formula will be 4.3%. This amount includes a 1% consumer dividend; d) the Z factor, or exogenous events, shall continue except that there is no express prohibition for giving such treatment to Commission mandated events;

Other issues concerning the PCI are also addressed within the HEPO. A proposal to give AI additional pricing flexibility was rejected. A proposal to re-initialize rates specifically within the four baskets themselves was rejected. A proposal to add an earnings sharing component to the PCI was rejected. A proposal to add a penalty structure for premature service reclassifications or require certain refunds was rejected. On a going forward basis, the monitoring and reporting requirements imposed upon AI are continued. Both service quality and merger related savings are to be addressed by the Commission on an individual basis and outside the scope of the PCI. See Part V.

3. Rate Re-Balancing - is discussed in Part IV of the HEPO. Ultimately we conclude that AI has not carried its burden and its proposal to re-balance certain residential rates was rejected. The model, Loop Facility Analysis Model or "LFAM", relied upon by AI to justify re-balancing fails to comply with the Commission's Cost of Service Rule, Part 791 requirements. Further the model seemed to produce unbelievable results.
4. Reinitialization of rates as proposed, and as underlines the CUB/AG complaint, is rejected. See Part VI.
5. The maintenance of service quality - going forward is discussed separately in Part VII of the HEPO. Here we adopt a number of performance measures and set benchmarks individually for each measure. As importantly, we discuss changes to the incentive structure of the existing Plan and detail a new incentive scheme that would have

meaningful customer credits be assigned to those most aggrieved by the Company's non-performance of its service obligations. In the end of this part, we turn our attention to other service quality proposals (e.g., reporting, investment, etc.) and offer reasonable conclusions to these matters.

In sum, the HEPO:

- a. continues the Plan with modifications under Docket 98-0252;
- b. denies AI's its requested rate re-balancing relief in Docket 98-0335; and,
- c. denies the CUB/AG rate complaint in Docket 00-0764.

PAC/EM:jt