D.P.U. 94-50

Petition of New England Telephone and Telegraph Company d/b/a NYNEX for an Alternative Regulatory Plan for the Company's Massachusetts intrastate telecommunications services.

APPEARANCES: A. Eric Rosen, Esq.
Bruce P. Beausejour, Esq.
Barbara Anne Sousa, Esq.
185 Franklin Street, Room 1403
Boston, Massachusetts 02107-1585

-and-

Robert J. Keegan, Esq.
Robert N. Werlin, Esq.
Ellen W. Schmidt, Esq.
Keohane & Keegan
21 Custom House Street
Boston, Massachusetts 02110

-and-

James K. Brown, Esq.
Foley, Hoag and Eliot
One Post Office Square
Boston, Massachusetts 02109
FOR: NEW ENGLAND TELEPHONE & TELEGRAPH COMPANY D/B/A NYNEX
Petitioner

L. Scott Harshbarger, Attorney General
By: George B. Dean
Edward G. Bohlen
Daniel Mitchell
Viveca Tung Kwan
William McAvoy
Joseph W. Rogers
Kevin McNeely
James Stetson
Assistant Attorneys General
131 Tremont Street, 3rd Floor
Boston, Massachusetts 02111
Intervenor

Jeffrey F. Jones, Esq.
Jay E. Gruber, Esq.
Palmer & Dodge
One Beacon Street
Boston, Massachusetts 02108

-and-

George Finkelstein, Esq.
Eleanor Olarsch, Esq.
32 Avenue of the Americas, Room 2700
New York, New York 10013
FOR: AT&T COMMUNICATIONS OF NEW ENGLAND, INC.
Intervenor

Robert Glass, Esq.
Glass, Seigle & Liston
75 Federal Street
Boston, Massachusetts 02110

-and-

Richard C. Fipphen, Esq.

Carl D. Giesy, Esq.
One International Drive
Rye Brook, New York 10573
FOR: MCI TELECOMMUNICATIONS CORPORATION
Intervenor

Alan D. Mandl, Esq.
Rubin and Rudman
50 Rowes Wharf
Boston, Massachusetts 02110

FOR: NEW ENGLAND CABLE TELEVISION ASSOCIATION, INC.
Intervenor

Andrew D. Lipman, Esq.
Russell M. Blau, Esq.
Dana Frix, Esq.
Swidler & Berlin, Chartered
3000 K Street, N.W.
Washington, D.C. 20007
FOR: MFS COMMUNICATIONS COMPANY, INC.
Intervenor

Teresa Marrero, Esq.
Teleport Communications Group, Inc.
Regulatory Affairs
One Teleport Drive
Staten Island, New York 10311
FOR: TELEPORT COMMUNICATIONS - BOSTON
Intervenor

Cathy Thurston, Esq.
1850 M Street, N.W.
11th Floor
Washington, D.C. 20036
FOR: SPRINT COMMUNICATIONS COMPANY, L.P.
Intervenor

Richard J. Quist, Jr.
Southwestern Bell Mobile Systems, Inc. d/b/a Cellular One
Westwood Executive Center
100 Lowder Brook Drive
Westwood, Massachusetts 02090

- and -

Robert L. Dewees, Jr., Esq.
Peabody & Brown
101 Federal Street
Boston, Massachusetts 02110
FOR: SOUTHWESTERN BELL MOBILE SYSTEMS, INC. D/B/A CELLULAR ONE
Intervenor

Mark R. Perkell
General Counsel
29 Church Street
P.O. Box 967

Burlington, Vermont 05402
FOR: RCI LONG DISTANCE NEW ENGLAND, INC.
D/B/A LONG DISTANCE NORTH
Intervenor

Andrew D. Lipman, Esq.
Dana Frix, Esq.
Swidler & Berlin, Chartered
3000 K Street, N.W.
Washington, D.C. 20007

-and-

Francis D.R. Coleman
Corporate Counsel
39 State Street
Rochester, New York 14614
FOR: ACC CORPORATION
Intervenor

Paul C. Besozzi, Esq.
Besozzi, Gavin & Craven
1901 L Street, N.W.
Suite 200
Washington, D.C. 20036
FOR: THE NEW ENGLAND PUBLIC COMMUNICATIONS COUNCIL, INC.
Intervenor

Cecil O. Simpson, Jr., Esq.
Office of the Judge Advocate General
Department of the Army
Litigation Center
901 North Stuart Street, Room 400
Arlington, Virginia 22203-1837
FOR: DEPARTMENT OF DEFENSE AND ALL OTHER FEDERAL EXECUTIVE AGENCIES
Intervenor

Frank Burns
Director of Voice Communications
Commonwealth of Massachusetts
Office of Management Information Systems
Bureau of Communications Technology
One Ashburton Place, Room 811
Boston, Massachusetts 02108-1518
Intervenor

David A. Tibbetts
General Counsel
One Ashburton Place, Room 2101
Boston, Massachusetts 02108
FOR: COMMONWEALTH OF MASSACHUSETTS EXECUTIVE OFFICE OF ECONOMIC AFFAIRS

Intervenor

Honorable Daniel E. Bosley
Representative
Commonwealth of Massachusetts
House of Representatives
State House, Room 43
Boston, Massachusetts 02133
Intervenor

Honorable Christopher J. Hodgkins
Representative
Commonwealth of Massachusetts
House of Representatives
State House, Room 34
Boston, Massachusetts 02133
Intervenor

Thomas P. O'Neill, Esq.
One Beacon Street
Boston, Massachusetts 02108
FOR: BOSTON GAS COMPANY
Limited Participant

John Cope-Flanagan, Esq.
COM/Energy Services Company
One Main Street
P.O. Box 9150
Cambridge, Massachusetts 02142-9150
FOR: CAMBRIDGE ELECTRIC LIGHT COMPANY,
COMMONWEALTH ELECTRIC COMPANY, AND
COMMONWEALTH GAS COMPANY
Limited Participants

Stephen Ostrach, Esq.
150 Lincoln Street
Boston, Massachusetts 02111
FOR: NEW ENGLAND LEGAL FOUNDATION
Limited Participant

Raymond W. LaBarge
Chairman
Board of Hampshire County Commissioners
County Commissioners' Office
Hampshire County Court House
99 Main Street, Room 232
Northampton, Massachusetts 01060
Limited Participant

George C. Jordan, III
The Gate House at Ventfort Hall

Lenox, Massachusetts 01240-2709
Limited Participant

Mitchell Ziegler
5 Daniel Court
Hyde Park, Massachusetts 02136
Limited Participant

Mark Brown
22 Haverhill Street
Andover, Massachusetts 01810
Limited Participant

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INTERLOCUTORY ORDER ON MOTION TO DISMISS
OF THE NEW ENGLAND CABLE TELEVISION ASSOCIATION, INC.

I. INTRODUCTION

On April 14, 1994, New England Telephone and Telegraph Company d/b/a NYNEX ("NYNEX" or "Company") filed with the Department of Public Utilities ("Department") an Alternative Regulatory Plan ("Plan") [1] for NYNEX's Massachusetts intrastate operations. The Plan proposes an alternative form of regulation for NYNEX to replace the Department's existing rate-of-return regulation. The matter was docketed as D.P.U. 94-50.

On May 11, 1994, the New England Cable Television Association, Inc. ("NECTA") filed a Motion to Dismiss NYNEX's filing ("Motion"). In response to NECTA's Motion, NYNEX filed an Objection, and the Attorney General of the Commonwealth ("Attorney General") submitted Comments. NECTA filed a Reply to NYNEX's Objection. In the Department's June 14, 1994 Interlocutory Order, the Department found that one ground of NECTA's Motion was moot. See New England Telephone and Telegraph Company d/b/a NYNEX , D.P.U. 94-50, at 11 (June 14, 1994 Interlocutory Order). In addition, the Department determined in that Order that it would defer ruling on NECTA's second ground for dismissal -- that NYNEX's Plan violates state telecommunications statutes and, therefore, the Department lacks

[1] The Plan was subsequently marked as Exh. NYNEX-1.

authority to adopt the Plan -- to allow additional time for parties in this proceeding to address briefing questions issued by the Department. Id. at 12. On July 28, 1994, the Department issued a series of briefing questions addressing, among other issues raised by NECTA's Motion, the question of the Department's statutory authority to approve alternative regulation, such as price cap regulation, and the specific form of price cap regulation proposed in the Company's Plan. The Department received responses to its briefing questions from NYNEX, NECTA, the Attorney General, AT&T Communications of New England, Inc. ("AT&T"), and MCI Telecommunications Corporation, Inc. ("MCI"). In this Order, we rule on NECTA's second ground for dismissal. [2]

II. SUMMARY OF THE COMPANY'S PLAN [3]

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[2] As a general principle, the Department endeavors to respond in a timely fashion to motions by parties in its proceedings. However, the Department also must be mindful not to delay the conduct of its proceedings while considering procedural motions. See 220 C.M.R. § 1.04(5)(b). NECTA's Motion indirectly, if not directly, raised the issue of the Department's authority to depart from traditional rate-of-return regulation, an issue which to our knowledge has never been explicitly addressed in a Department Order. To respond to the complex legal questions raised by NECTA's Motion, we have had to conduct a thorough analysis.

[3] Although there are many other elements to the Company's proposed Plan, for purposes of ruling on NECTA's Motion, it is only necessary that we summarize the basic mechanics of the price cap formula. The Department will discuss the Company's Plan in much greater detail in the final Order in this case.

The Company's Alternative Regulatory Plan for NYNEX's Massachusetts intrastate operations would establish a price cap form of regulation (April 14, 1994 Killian Transmittal Letter at 2). NYNEX contends that the Plan could allow for prices for all of the Company's services, except basic local residence service, to be adjusted in the aggregate each year based on increases or decreases in inflation ("Gross Domestic Product-Price Index" or "GDP-PI"), minus a productivity factor of 2.5 percent, plus or minus exogenous changes (Killian Pre-filed Testimony at 14). [4,5,6] NYNEX must also meet quality of service commitments to increase prices in the aggregate (Plan at 13). The Company contends that the price cap formula "guarantees that, except for exogenous changes, overall prices for telephone

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[4] The Company defines an exogenous change as a change outside the Company's control and/or not properly reflected in the GDP-PI (Killian Pre-filed Testimony at 15). Mr. Killian's pre-filed testimony was subsequently marked as Exh. NYNEX-8.

[5] NYNEX asserts that the 2.5 percent productivity factor reflects the fact that long run total factor productivity in the telecommunications industry has been 2 percent greater than United States industry in general (Taylor Pre-filed Testimony at 12-21). NYNEX terms the additional 0.5 percent a "consumer dividend" designed to ensure rate stability (Killian Pre-filed Testimony at 15).

[6] The Company has stated that the Plan establishes a ceiling on the price increase permitted for each individual rate element, which for most rate elements is determined by the change in inflation (CPI) plus or minus exogenous changes (Caldwell Pre-filed Testimony at 2; Plan at 4-10). Mr. Caldwell's pre-filed testimony was subsequently marked as Exh. NYNEX-4.

service over the duration of the Plan will fall in real terms" (Killian Pre-filed Testimony at 14). NYNEX maintains that "adjusting the price index annually using a formula that accounts for inflation, productivity, and exogenous cost changes ties prices to long run industry average costs, and provides competitive market incentives to reduce costs and lower prices" (Taylor Pre-filed Testimony at 38). [7] Prices for basic local residence service would be frozen at current rates through August 2001 for all residence customers, and then could be adjusted according to the price cap formula (Killian Pre-filed Testimony at 14). The Company contends that NYNEX's ongoing compliance with the pricing rules "would establish the ongoing justness and reasonableness of its rates under the Plan" (NYNEX Response to Briefing Question No. 1, at 7). According to the Company, the operation of the Plan is governed by a series of pricing rules that would constitute the regulatory mechanism used to ensure just and reasonable rates (id.). The Company's Plan does not include an earnings sharing mechanism or an explicit earnings cap (Killian Pre-filed Testimony at 13-14). Therefore, to the extent that NYNEX can increase its productivity beyond the productivity factor, it can earn higher profits, and customers can still experience reduced prices (Taylor Pre-filed Testimony at 16).

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[7] Dr. Taylor's pre-filed testimony was subsequently marked as Exh. NYNEX-3.

NYNEX states that the Company's current rates, which were found just and reasonable in its most recent transitional rate filing proceeding, D.P.U. 93-125, are the appropriate starting rates for the Plan (Killian Pre-filed Testimony at 22). The Plan also includes a provision for challenging Company tariff filings that are perceived as anti-competitive (Plan at 19-20). The Company asserts that the Department's authority under G.L. c. 159, § 20 would be unimpaired and the Department could investigate the Company's rates for compliance with the pricing rules (id. at 18). Under the Plan, NYNEX would no longer be subject to rate-of-return regulation (id. at 24).

III. POSITIONS OF THE PARTIES [8]

A. NECTA

NECTA argues that the Department lacks authority to adopt NYNEX's filing because current statutes do not provide for the type of alternative regulation the Plan envisions (Motion to Dismiss at 5-7). NECTA contends that many elements of NYNEX's Plan would violate statutory law and approval of the Plan would exceed the Department's authority under G.L. c. 159, c. 30A, and c. 25, § 5 (NECTA Response to Briefing Questions Nos. 1, 3). Thus, NECTA contends that as a matter of law the Company's Plan

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[8] The Department relies both on the parties' pleadings concerning NECTA's Motion as well as the parties' answers to the Department's briefing questions.

must be dismissed (id.).

Although NECTA is not entirely consistent in its arguments, viewed in the aggregate NECTA appears to argue that, while the Department may have the authority under G.L. c. 159 to approve alternative regulation, the Department cannot consider NYNEX's Plan (NECTA Response to Briefing Questions Nos. 1-4; NECTA Reply at 2-3 n.1, 6 & n.3). NECTA asserts that the Plan lacks a constraint on the profits the Company could earn, thus severing the link between the Company's costs and its earnings in violation of G.L. c. 159, §§ 14 and 20 (id.).[9]

NECTA argues that the entire legislative scheme of common carrier regulation is based upon the use of common carrier costs for reviewing and determining rates (NECTA Response to Briefing Question No. 7, citing Tilton v. City of Haverhill , 311 Mass. 572 (1941)). NECTA maintains that the legislature requires a "nexus between NYNEX's revenue requirement and any maximum allowable rates," to protect customers from excessive rates (NECTA Reply at 5). NECTA purports that NYNEX's Plan is "fatally flawed" because it severs this nexus (NECTA Reply at 5; NECTA Response to Briefing Question No. 1).

Viewed another way, NECTA contends that the "express

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[9] NECTA states that under G.L. c. 159, NYNEX's rates must be determined according to cost-of-service, rate-of-return regulation (NECTA Response to Briefing Question No. 5).

language" of G.L. c. 159, §§ 14 and 20 and the overall legislative scheme of Chapter 159 create a "zone of reasonableness" standard, the upper and lower boundaries of which are a "cost-based ceiling and cost-based floor" (NECTA Response to Briefing Questions Nos. 5, 7; NECTA Reply at 2). According to NECTA, the requirement of a "cost-based ceiling" or "cost-based floor" exists in the specific language of G.L. c. 159, §§ 14 and 20, in the overall statutory scheme, and as a matter of constitutional law to prevent confiscation (NECTA Response to Briefing Question No. 7). In addition, NECTA claims that the absence of a "cost-based ceiling" in the NYNEX plan renders "superfluous or contradicts" other provisions of Chapter 159, as well as related statutes, and is contrary to longstanding tenets of statutory construction (id., citing School Comm. of Brockton v. Teachers Retirement Bd. , 393 Mass. 256 (1984)).

NECTA maintains that case law and Department precedent support its position that the reasonableness of compensation must be determined in relation to a cost-of-service measurement (NECTA Reply at 3, citing Auditor of Commonwealth v. Trustees of Boston Elevated Ry. , 312 Mass. 74, 77-78 (1942); Opinion of the Justices , 251 Mass. 569, 610-611 (1925); Boston Consolidated Gas Co., 13 P.U.R. 3d 401, 411 (1956); The Railroad Passenger Rate Case , P.U.R. 1915B 362, 369 (1915); New England Telephone and

Telegraph Company , D.P.U. 16253 (1970)). [10]

NECTA argues that because NYNEX's Plan is "completely devoid" of a nexus between the Company's revenue requirement and rates (i.e. , contains no "cost-based ceiling or floor" to prevent the Company from earning an "unlimited rate of return" or an unreasonably low rate of return), the Plan fails to satisfy Chapter 159's "just and reasonable standard" and the Section 20 requirement that rates provide "reasonable compensation for the services rendered" (NECTA Reply at 2; NECTA Response to Briefing Question No. 8).

NECTA also submits that there are other "patent deficiencies" that prevent the Department's consideration of the Plan (NECTA Response to Briefing Questions Nos. 1, 2). NECTA maintains that a cost-based cap on earnings [11] is required, among other modifications, to correct the unlawful aspects of the Plan (NECTA Response to Briefing Question No. 2).

NECTA also argues that allowing NYNEX's proposal would

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[10] In complying with this standard, NECTA argues, the Department has some latitude (i.e. , year average, year-end rate base; rate stabilization formulas, etc.) (Motion at 6; NECTA Response to Briefing Question No. 5).

[11] NECTA points to the Settlement Agreement approved by the Rhode Island Public Utilities Commission, which includes a cap on NYNEX's earnings in the price regulation component (NECTA Reply at 6). NECTA also notes that the Federal Communications Commission's ("FCC") price cap plan for AT&T, unlike the NYNEX Plan, maintains a nexus between carriers' rates, costs, and earnings (id. at 7).

violate a comprehensive statutory scheme for regulation of telecommunications carriers (NECTA Reply at 11-13, citing G.L. c. 159, §§ 26, 31, 32, 34A; c. 166, §§ 12A, 14, 22L; c. 6A, § 18D; c. 25, §§ 17, 18). NECTA argues that the underlying purpose of statutes such as G.L. c. 159, §§ 26, 31, 32, and 34A, is to facilitate the Department's scrutiny of NYNEX's costs to determine whether rates are just and reasonable (id. at 11-12). NECTA asserts approval of the NYNEX Plan would effectively "repeal" these statutes by "divorcing" them from the process of establishing rates (id. at 12). Moreover, NECTA contends, there is an underlying statutory scheme requiring a nexus between NYNEX's rates and total revenue requirement (id. at 12-13, citing G.L. c. 166, §§ 12A, 14, 22L; c. 6A, § 18D; and c. 25, §§ 17, 18).

According to NECTA, the Department is compelled, as a matter of law, to dismiss NYNEX's filing, but the Department is not precluded from addressing a price cap model or other alternative ratemaking model that is consistent with statutory requirements (NECTA Reply at 2-3, n.1). However, NECTA contends that legislation must be enacted to allow for the approval of NYNEX's Plan (Motion at 6).

NECTA maintains that the Department's decision in AT&T, D.P.U. 91-79 (1992), approving an alternative form of regulation for AT&T, offers no support for NYNEX's position because that

decision expressly does not apply to NYNEX, and the Department was not asked to rule on the legal issues raised in NECTA's Motion (NECTA Reply at 8; NECTA Response to Briefing Question No. 11). Also, NECTA argues that the "acid test" for determining the lawfulness of NYNEX's Plan is not what was decided in D.P.U. 91-79, but what the statute permits, given that ratemaking authority is delegated by the legislature (NECTA Reply at 8-9, citing Boston Edison Co. v. City of Boston, 390 Mass. 772 (1984)). Moreover, NECTA asserts that if the Department determines that it is without authority under current statutes to approve NYNEX's Plan, such a decision would not affect the Department's Order in D.P.U. 91-79 (id.). In addition, NECTA contends that the adoption of alternative regulation plans in other jurisdictions is not controlling in this proceeding (id. at 5-6; NECTA Response to Briefing Question No. 12). Finally, NECTA asserts that NYNEX's filing must be dismissed if the Department is to establish by means of an orderly investigation the appropriate preconditions for alternative regulation (NECTA Reply at 14). [12]

B. Attorney General

Although the Attorney General supports NECTA's Motion, he

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[12] NECTA also states that NYNEX is protected from liability to its customers based upon the assumption that its rates are cost-based (NECTA Reply at 14, citing Wilkinson v. New England Tel. and Tel. Co., 327 Mass. 132, 136 (1951)).

nonetheless concedes that Chapter 159 "does not prescribe explicitly any particular mode of rate regulation" for the Department (Attorney General Response to Briefing Question No. 1, at 3, citing Weld v. Gas & Elec. Light Comm'rs , 197 Mass. 556, 558 (1908)). He states that G.L. c. 159, §§ 14 and 20 require that rates "must be just and reasonable, provide adequate compensation for the services rendered, and cannot be unjustly discriminatory, unduly preferential, or otherwise in violation of any law" (id.). However, in choosing among alternative modes of rate regulation (including price caps), the Attorney General argues that the Department must ensure that the chosen alternative complies with the standards and directives of Chapter 159 (id. at 4).[13] The Attorney General contends that the Department and the Massachusetts Supreme Judicial Court have construed the ratemaking requirements of Chapter 159 as compelling an "analysis of carrier costs and/or profits" (id. at 5 & n.6 (citations omitted)). According to the Attorney General, "`[t]he principle that rate making must be based primarily on cost factors of the utility company ...'" has been

[13] The Attorney General notes that nearly all pronouncements by the Massachusetts Supreme Judicial Court regarding the Department's discretion to employ alternative methods of regulation were within the context of appeals of Department rate decisions to employ variations to traditional cost-of-service, rate-of-return regulation (Attorney General Response to Briefing Question No. 1, at 4 n.3 (citations omitted)).

recognized by the Massachusetts Supreme Judicial Court (id. at 5, quoting Kargman v. Department of Pub. Utils. , 334 Mass. 497, 498 (1956)). The Attorney General contends that the Department's ratemaking authority under Chapter 159 was "best stated" by the Massachusetts Public Service Commission, a predecessor of the Department, in a 1915 decision concerning the appropriate rates for a railroad utility:

> Broadly speaking, rates should be so fixed so as to yield to a ... [carrier] economically and efficiently managed, revenues adequate to meet its operating expenses and fixed charges and to yield a fair return upon the capital honestly and prudently invested. Rates which are either too low or too high, judged by this standard, are unjust and unreasonable, either to the company and its stockholders or to the ... public.

(id. at 5-6, quoting Railroad Passenger Rate Case , 8d Ann.Rep. Mass. P.S.C. 3, 4 P.U.R. 1915B 362, 369 (1915) (citation omitted)). [14]

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[14] The Attorney General contends that this case was an interpretation of the ratemaking authority conferred under the 1913 "Washburn Bill," which he states was the first legislation enacted by the Massachusetts General Court to delegate ratemaking authority to the Department, and included the antecedents of G.L. c. 159, §§ 14 and 20 (Attorney General Response to Briefing Question No. 1, at 5-6, n. 5, citing St. 1913, c. 784, §§ 21 and 22; Donham v. Public Serv. Comm'n , 232 Mass. 309, 317 (1919) (Chapter 159 requires that "there shall not be an exorbitant charge for the service rendered")). The Attorney General argues that similar ratemaking statutes in other jurisdictions have been viewed by courts as giving consideration to the concept of cost and recognition that "the end of public utility regulation ... [is] the protection of consumers from exorbitant rates" (id. at 6, n.7, citing Stewart v. Utah

(continued...)

The Attorney General contends that the requirement of a nexus between carrier costs (including earnings or profits) and rates "is also supported by the predominant view of [the Department] of the purpose of utility rate regulation" (id. at 6). The Attorney General notes that the Department has determined that "prices set through the operation of sufficiently competitive markets will satisfy the `just and reasonable' standards of Chapter 159 ... [in that] competitive market prices tend to reflect marginal costs and, in contrast to monopoly prices, do not yield 'excess profits' nor sustain any price discrimination beyond that reflecting cost differences" (id. at 6-7, citing IntraLATA Competition , D.P.U. 1731, at 18, 25-26, 28-40 (1985); AT&T Communications, Inc. , D.P.U. 91-79, at 16-17, 34 (1992); Boston Edison Co. , D.P.U. 906, at 204-205 (1982), aff'd sub nom. Attorney Gen. v. Department of Pub. Utils. , 390 Mass. 208 (1983)). According to the Attorney General, it is "not possible to hypothesize any single overall benchmark other than costs" for determining just and reasonable rates under Chapter 159 (id. at 7, citing Attorney Gen. v. Department of Pub. Utils. , 390 Mass. 208, 235 (1983) ("unless there is a reasonable

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[14](...continued)
Public Serv. Comm'n , 244 Utah Adv. Rep. 11, 27 n.11 (Utah 1994) and quoting Washington Gas Light Co. v. Baker 188 F.2d 11, 15 (D.C. Cir. 1950), cert. denied , 340 U.S. 952 (1951)).

justification for significant differential in the rates of return of classes, perhaps based upon differences in usage or on public policy considerations ... continuing substantial difference in the rates of return of classes may result in `unduly or irrationally discriminatory' rates")). Thus, the Attorney General contends that the Department does not have the authority to adopt a ratemaking scheme (i.e., overall rate levels and rate structure) that "severs completely the nexus between carrier costs and lawful rates", and that to do so would require amendment to Chapter 159 (id. at 7-8) (citation omitted)). The Attorney General contends that to satisfy separation of powers requirements, Chapter 159 must be construed to include an overall benchmark, such as costs, to use in determining rates (id. at 8-9).

Finally, the Attorney General argues that an alternative scheme for regulation that amounts to a general increase in rates may be implemented only when the carrier proves that, pursuant to G.L. c. 159, §§ 14 and 20, such an increase in rates is "necessary to obtain reasonable compensation for the service rendered" (id. at 9 & n.12, citing New England Tel. and Tel. Co. v. Department of Pub. Utils., 376 Mass. 28, 32-33 (1978); New England Tel. and Tel. Co. v. Department of Pub. Utils., 373 Mass. 678, 682 (1977)).

According to the Attorney General, whether the Department

has the authority to adopt a price cap form of alternative regulation depends on

> four interrelated factors: (1) [whether] the link between carrier costs and rates [is severed]; (2) the length of time the plan will be in effect without adjustment; (3) the extent, if any, of pricing discretion afforded carriers; and (4) the provision of means by which unlawful rates that nonetheless satisfy the scheme's pricing rules can be fixed by the Department at lawful levels

(id. at 2, 12). With regard to NYNEX's specific proposal, the Attorney General asserts that the Department lacks authority to adopt NYNEX's Plan because of specific infirmities of the Plan and because the scope of the current proceeding is inadequate (id. at 18-19; see id. at 15-17, 20-23). [15] The Attorney General further avers that even if the inadequacies of the current proceeding were cured, the Department still could not adopt the Plan without the enactment of new legislation (id. at 19). The Attorney General cites the following aspects of the Plan in support of this contention: the ten-year term of the Plan; the

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[15] With respect to the scope of the current proceeding, the Attorney General maintains that because the Department has determined not to investigate rate structure in this proceeding, and because the Department's allowed examination of the Company's costs and revenues is inadequate, "it is entirely impossible for the Department to make any credible conclusions" on whether the Company's "overall rates under the ... Plan would be just and reasonable, much less whether the individual rates that could result would be just and reasonable as well as not unjustly discriminatory nor unduly preferential" (Attorney General Response to Briefing Question No. 1, at 18).

pricing discretion afforded NYNEX under the Plan; the lack of a nexus between costs and rates; the ability of NYNEX to create new customer classifications not subject to review for unjust or discriminatory rates, or undue preference; and the Plan's implicit repeal of G.L. c. 159, § 20's requirement that NYNEX bear the burden of proof with respect to a general increase in rates (id. at 19-23).

With regard to the value of D.P.U. 91-79 as precedent, the Attorney General contends that the issue of whether the Department could approve alternative regulation was never addressed in that proceeding (Attorney General Response to Briefing Question No. 11, at 2). In addition, the Attorney General argues that the particular components of the AT&T proposal approved in that proceeding are far different from the components of the NYNEX Plan (id.). The Attorney General argues that, in contrast to the NYNEX Plan, the AT&T price cap is not in violation of Chapter 159, and would not be invalidated by a determination that the NYNEX proposal is unlawful (id. at 2-3).

C. AT&T

AT&T did not initially comment on NECTA's Motion but did file responses to the Briefing Questions. AT&T argues that the Department has broad discretion under G.L. c. 159 to choose the form or forms of regulation to be applied to telecommunications companies subject to its jurisdiction and to approve alternative

forms of regulation (AT&T Response to Briefing Questions at 1, 3). AT&T states that neither the general provisions of G.L. c. 159 nor the specific provisions of §§ 14 and 20 explicitly require rate-of-return regulation or any other specific form of regulation (AT&T Response to Briefing Question No. 1, at 1). According to AT&T, the Massachusetts Supreme Judicial Court has held that the Department is not bound to apply one particular method of regulation (id., citing American Hoechest Corp. v. Department of Pub. Utils. , 379 Mass. 408, 411-12, 413 (1980)(cost of service not sole criterion for utility rate structures); Trustees of Clark Univ. v. Department of Pub. Utils., 372 Mass. 331, 336 (1977)(utility's rate need not be structured on cost-related basis)).

AT&T argues that construing G.L. c. 159 as requiring rate-of-return regulation would unduly limit the Department's ability to tailor regulation to the needs of particular industries or industry segments (id. at 2). AT&T contends that the General Court intended to establish regulatory goals for the Department and to allow the Department to determine how best to achieve those goals (id. at 2). [16] AT&T posits that if the

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[16] AT&T states that regulatory agencies are created for the purpose of developing expertise in the fields in which they regulate (AT&T Response to Briefing Questions at 2, citing Murphy v. Adm'r, Div. of Personnel Admin. , 377 Mass. 217, 220 (1979)).

General Court intended to require a single form of regulation, it would have done so explicitly in the statute (id. at 2).

AT&T contends that statutory delegation of extensive powers to regulate implicitly allows the Department to choose the method or methods of regulation (id. at 2-3, citing Attorney Gen. v. Department of Pub. Utils. , 392 Mass 262, 268 (1984)(where result of employing specific methodology in rate setting not impermissible, choice of methodology committed to agency discretion); American Hoechest Corp. v. Department of Pub. Utils. , 379 Mass. 408, 411-12, 413 (1980)(Department free to select or reject particular method as long as choice not confiscatory or otherwise illegal); Massachusetts Elec. Co. v. Department of Pub. Utils. , 376 Mass. 294, 302 (1978)(Department free to select or reject particular method as long as choice not confiscatory or otherwise illegal); New England Tel. and Tel. Co. v. Department of Pub. Utils. , 371 Mass. 67, 71 (1976)(Department not required to use method based on adjustments to historic test year); New England Tel. and Tel. Co. v. Department of Pub. Utils. , 331 Mass. 604, 616 (1954)). AT&T argues that, with respect to rates, the only limitation on the powers of the Department is the requirement that rates be just and reasonable (id. at 3, citing Donham v. Public Serv. Comm'rs , 232 Mass. 309, 325 (1919)). AT&T cites the Massachusetts Supreme Judicial Court's definition of just and reasonable rates as those which

`yield reasonable compensation for the service rendered and must be just and reasonable having relation to the service to be performed' (id. at 1, quoting Donham v. Public Serv. Comm'rs , 232 Mass. 309, 313 (1919)). AT&T also cites the Massachusetts Supreme Judicial Court's definition of reasonable compensation as that which is "`sufficient to yield a fair return on the reasonable value of the property used or invested for doing business after paying costs and carrying charges'" (id. at 2, quoting New England Tel. and Tel. Co. v. Department of Pub. Utils., 331 Mass. 604, 615 (1954)). AT&T argues that "[t]here can be little question that the legislature chose the broad language employed in G.L. c. 159 in order to ensure that the Department would have the latitude to adopt different regulatory approaches in response to changing conditions within the industries it is charged to regulate" (id. at 7). AT&T notes that while the Department has flexibility under G.L. c. 159 to develop methods for determining the reasonableness of rates, it must act within the broad constraints of G.L. c. 30A (AT&T Response to Briefing Question No. 5). [17]

AT&T contends that the Department historically has acted in a manner consistent with a broad statutory grant of discretion

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[17] AT&T states that G.L. c. 30A requires that Department decisions must be rational, non-arbitrary, non-capricious, and based on evidence in the record (AT&T Response to Briefing Question No. 5).

(AT&T Response to Briefing Question No. 1, at 3-6). AT&T cites the Department's 1984 determination that it would not impose traditional rate-of-return regulation on most interexchange carriers and the Department's determination not to impose rate-of-return regulation on resellers of telecommunications services or the mobile radio and cellular segments of the Massachusetts telecommunications market (id. at 3, citing GTE Sprint Communications Corp , D.P.U. 84-157, at 4 (1985); First Phone, Inc. , D.P.U. 1581 (1984); Cellular Resellers , D.P.U. 84-250-1, et seq. (1984)). AT&T also argues that in adopting a relaxed form of rate regulation for nondominant carriers in IntraLATA Competition , D.P.U. 1731, the Department recognized that accomplishment of the statutory mandate to ensure that regulated telecommunications carriers' rates are just and reasonable does not require the imposition of full-scale traditional rate-of-return regulation (id. at 4).[18] AT&T cites the Department's decision to approve a reduction in its regulation of AT&T's intrastate services as an example of the Department's exercise of its discretion to rely on the market rather than on rate-of-return regulation (id. at 5, citing AT&T, D.P.U. 91-79).[19] Finally, AT&T cites the Department's decision

[18] AT&T views the historical actions of the Department as regulating in proportion to the degree of competition in the market (AT&T Response to Briefing Question No. 1, at 3-4, 9).

(continued...)

in Entry Deregulation , D.P.U. 93-98 (1994), in which the Department eliminated its longstanding practice to require a certificate of public convenience and necessity as a precondition of doing business, as an example of the Department's exercise of discretion to determine the appropriate scope and degree of regulation necessary for particular segments of the telecommunications market at different points in time (id. at 5-6).

AT&T argues that G.L. c. 159, §§ 14 and 20 do not preclude the Department from considering any particular form of regulation, so long as the statutory requirements are met, and that there is nothing inherently inconsistent between a price cap form of regulation and the achievement of just and reasonable rates (id. at 6). AT&T characterizes the Department's decision in AT&T, D.P.U. 91-79 (1992), whereby the Department approved at

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[19](...continued)

[19] AT&T noted that in D.P.U. 91-79, the Department stated that its Order did not apply to NYNEX (AT&T Response to Briefing Question No. 11). AT&T stated that, in D.P.U. 91-79, it had demonstrated that nearly all of its Massachusetts intrastate services are subject to competition and that its Massachusetts intrastate business represents a small portion of its total telecommunications business (id.). AT&T presently argues that the deficiencies in NYNEX's Plan could not be compared to the AT&T proposal approved in D.P.U. 91-79 (id.). Because it is AT&T's view that the Department has the discretion to approve alternative regulation where market forces eliminate or reduce the need for regulation, AT&T argues that a determination by the Department that it lacked authority to approve NYNEX's Plan would not invalidate the result of D.P.U. 91-79 (id.).

least one form of price cap regulation, as an "appropriate exercise of the Commission's statutory authority" (id. at 7).[20]

However, AT&T argues that the Department's authority to approve the particular Plan proposed by NYNEX is less clear (id. at 7, 10). AT&T bases this assertion on its view that the Company's Plan "provides no assurances that rates will be just and reasonable" (id. at 7). AT&T argues that the Plan expressly disavows the two concepts -- rate-of-return/cost-of-service-based rates or competition -- the Department has relied on historically to ensure just and reasonable rates (id. at 8).

Also, with respect to the specific Plan put forth by NYNEX, AT&T states that NYNEX's Plan is deficient in many other respects: (1) it provides the Company with an extraordinary amount of pricing flexibility; (2) it allows the Company to impose anticompetitive price squeezes on competitors; (3) it allows NYNEX's rates to be divorced from the cost of providing services; and (4) it permits NYNEX's earnings to increase without limitation (id. at 8 (footnote omitted)). AT&T contends that in IntraLATA Competition , D.P.U. 1731, the Department determined that, in light of NYNEX's undisputed market power, NYNEX must be

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[20] The form of price cap allowed by the Department in D.P.U. 91-79 provided for a weighted-average price cap for basic message telecommunications service ("MTS") for a period of approximately one and one-half years, with reductions in access rates during that period to be automatically flowed through in reduced rates for AT&T customers. D.P.U. 91-79, at 44-45.

subject to full-scale traditional rate-of-return regulation (id. at 8-9). AT&T interprets that case as standing for the proposition that the Department would modify traditional rate-of-return regulation for a `monopoly provider of utility service' only where there has been demonstrated a `high degree of competition' (id. at 9, quoting D.P.U. 91-79, at 41).

Moreover, AT&T argues that the only standard offered by NYNEX to support its contention that rates under the Plan will satisfy statutory requirements is NYNEX's assertion that those rates have been previously determined to be just and reasonable (id. at 9). Specifically, AT&T states that NYNEX has failed to demonstrate that (1) the starting point for rates are at, or near, cost; (2) the productivity factor will capture cost changes over the term of the Plan; and (3) the pricing flexibility afforded by the Plan will not result in anticompetitive pricing for individual services (id. at 9).

AT&T lists several reasons for its assertion that NYNEX's Plan will not produce rates in compliance with governing statutes: (1) the ability to adjust individual rates under the overall price umbrella will permit predatory and monopolistic pricing; (2) NYNEX has not offered a principled reason for deviating from the transition plan to achieve cost-based rates; (3) the ten-year term is too long; (4) annual price increases virtually assured under the Plan will not reflect price changes

in the competitive market and will dissolve any existing relationship between NYNEX's costs and rates; (5) there is no cap on earnings or sharing mechanism; and (6) the productivity factor is too low (AT&T Response to Briefing Question No. 2, at 1-2).[21] AT&T asserts that to correct these problems in the Company's Plan, the Department should (1) determine and impose conditions to ensure effective competition for NYNEX's services, (2) reject the link between carrier access and toll rates, (3) subject NYNEX's earnings to a sharing mechanism, (4) reduce the term of the Plan, (5) eliminate the broad pricing flexibility afforded under the Plan, and (6) group services into price baskets based on whether they are competitive or monopoly services (id. at 1).

Finally, it is AT&T's position that annual filings under the Plan would constitute general rate increases under G.L. c. 159, § 20 because the filings will likely entail overall increases in rates with adjustments to many rates for individual services (AT&T Response to Briefing Question No. 9). AT&T states that

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[21] AT&T states that the productivity factor is based on productivity levels achieved under traditional regulation although productivity levels are generally greater in a competitive environment, and that pricing flexibility under the Plan provides an irresistible temptation for NYNEX to take advantage of its monopoly power (AT&T Response to Briefing Question No. 1, at 9). AT&T also argues that although it is difficult to determine what level of earnings would be excessive under the statute, without a cap or sharing mechanism to limit earnings, it is possible, and perhaps likely, that NYNEX's earnings will exceed the level permitted under the statute (id.).

under G.L. c. 159, § 20, the Department would be required to give notice and conduct some review of general rate filings but that it need not invoke the statutory suspension period, and may permit proposed rates to take effect on 30 days notice (id.). However, AT&T states that a petition that was not a general rate increase would not require the Department to initiate G.L. c. 159, § 20 procedures (AT&T Response to Briefing Question No. 3).

D. MCI

MCI did not comment on NECTA's Motion but did file responses to the Briefing Questions. MCI contends that the Department has broad general power over the provision of telecommunications services under G.L. c. 159, § 20 (MCI Response to Briefing Question No. 1, citing AT&T, D.P.U. 91-79 (1992)). MCI states that the Department has the statutory authority and has been granted great latitude to determine the method of regulation for telephone companies including price caps, so long as the resulting rates are just and reasonable (MCI Response to Briefing Questions Nos. 2 and 11(a), citing AT&T, D.P.U. 91-79 (1992)). According to MCI, there is no statutory requirement of a nexus between rates and a carrier's revenue requirement (MCI Response to Briefing Question No. 8).

MCI contends that the mechanics of NYNEX's Plan permit individual rate elements to increase over the life of the Plan

regardless of whether the cost of providing service is increasing or decreasing (MCI Response to Briefing Question No. 2). MCI also contends that the Plan allows NYNEX to charge wholesale customers more for access than it charges retail customers (id.). MCI further states that appropriate competitive safeguards must be implemented in NYNEX's Plan to prevent it from using its monopoly power to harm potential competitors through price squeezes, discrimination, and cross-subsidization (MCI Response to Briefing Questions Nos. 1, 4).

Finally, MCI contends that the Plan allows NYNEX to implement rates that are not just and reasonable (MCI Response to Briefing Question No. 2). MCI argues that the Department must determine if it can legally allow the level of pricing flexibility allowed in NYNEX's Plan (id.).

E. NYNEX

NYNEX argues that the Department must deny NECTA's Motion because there is no basis for dismissal of the Plan (NYNEX Objection at 11). NYNEX maintains that NECTA's contention that legislation must be enacted to authorize the filing and approval of a price cap form of regulation is wrong and is unsupported by existing case law and Department precedent (id. at 2). NYNEX asserts that the Department retains broad ratemaking authority under G.L. c. 159, §§ 14 and 20, to approve alternative regulation, including price cap regulation and, by extension,

NYNEX's Plan (NYNEX Response to Briefing Question No. 1, at 1).

NYNEX contends that G.L. c. 159 "neither implicitly nor explicitly requires one specific form of regulation" or pricing philosophy, and contrary to NECTA's assertion, the fact that NYNEX's Plan departs from traditional rate-of-return regulation does not compel its dismissal (id.). NYNEX asserts that the Department's authority is broadly defined and is limited only to ensuring that rates charged by common carriers are "just", "reasonable", and "sufficient to yield a reasonable compensation for the service rendered" (id. at 1-2, citing G.L. c. 159, §§ 14 and 20; see also Holyoke St. Ry. Co. v. Department of Pub. Utils., 198 N.E.2d 413 (1964) (G.L. c. 159, § 12 allows the Department "a wide range of discretion in appraising the public interest and in adopting reasonable policies, principles and standards for its guidance")). Therefore, NYNEX argues that the Department is not constrained to employ a specific form of regulation or pricing philosophy (i.e., rate-of-return regulation or revenue requirement investigation) to establish rates (id. at 2).

NYNEX contends that since no specific method of regulation or pricing formula is mandated by statute, "the Department has broad legal authority to implement incentive regulation, such as price cap regulation, provided that this regulatory approach can produce `just and reasonable rates'"(id., citing American

Hoechest Corp. v. Department of Pub. Utils. , 399 N.E. 2d 1, 4 (1980) (Department free to select or reject alternative form of regulation as long as its choice does not have "confiscatory effect or is not otherwise illegal").

NYNEX argues that, contrary to NECTA's claim, Chapter 159 does not incorporate an explicit "cost" component (i.e., cost-based ceiling or floor), and that, in fact, there is no method prescribed by statute for the Department to make its "reasonableness" determination (NYNEX Response to Briefing Question No. 7, at 2). Thus, NYNEX concludes that its Plan meets the "statutory standard because it establishes a process designed to result in just and reasonable rates, sufficient to yield reasonable compensation," in that it (1) caps rate levels to reduce the real price of telecommunications services consistent with productivity gains; and (2) gives NYNEX a fair and reasonable return (if productivity gains are met) (id.). According to NYNEX, the Plan's "pricing rules and other elements ... not existing rate-of-return principles, would constitute the regulatory mechanism used to ensure just and reasonable rates under G.L. c. 159, §§ 14 and 20" (NYNEX Response to Briefing Question No. 1, at 7). NYNEX asserts that its compliance with those rules would establish an ongoing justness and reasonableness of rates (id.). NYNEX also claims that the Company's current rates serve as an appropriate starting point

for the Plan as these rates were found to be just and reasonable by the Department in D.P.U. 93-125 (id. at 8, citing G.L. c. 159, § 17; NET, D.P.U. 93-125 (1994)).

NYNEX maintains that the Department and the courts, in interpreting G.L. c. 159, §§ 14 and 20, recognize no single formula or regulatory model as alone meeting constitutional and statutory requirements (id. at 2-9). NYNEX contends that the United States Supreme Court has found that state regulators are not precluded from adopting alternative ratemaking methods (id. at 3, 6 quoting Duquesne Light Co. v. Barasch , 488 U.S. 299 (1989) ("the designation of a single theory of ratemaking as a constitutional requirement would unnecessarily foreclose alternatives which could benefit both consumers and investors"); Federal Power Comm'n v. Hope Natural Gas , 320 U.S. 591, 600-601 (1944) (under statutory "just and reasonable," standard "it is the result reached and not the method employed that is controlling")). According to NYNEX, in subsequent decisions, the Supreme Court rejected the notion that just and reasonable rates must be based on the concept of cost plus a reasonable rate of return, and instead upheld the approval of incentive plans that allowed rates to increase based on non-cost factors (id. at 6).

In addition, NYNEX asserts that the Massachusetts Supreme Judicial Court has recognized the Department's "wide discretion in choosing its approach to rate regulation" (id. at 2, citing

New England Tel. and Tel. v. Department of Pub. Utils. , 371 Mass. 67, 85, 354 N.E. 2d 860, 872 (1976); New England Tel. and Tel. Co. v. Department of Pub. Utils. , 360 Mass. 443, 453, 275 N.E.2d 493, 501 (1971); New England Tel. and Tel. Co. v. Department of Pub. Utils. , 331 Mass. 604, 616, 121 N.E.2d 896, 903 (1954)). [22]

Moreover, NYNEX claims that the Department already has approved alternative ratemaking schemes for telecommunications common carriers as well as other regulated industries (NYNEX Response to Briefing Question No. 5, at 3). In the electric industry, for example, which has a similar statutory scheme to telecommunications, NYNEX contends that the Department has adopted "an alternative to cost of service, rate-of-return regulation in order to establish 'reasonable rates'" (id., citing 220 C.M.R. § 9.00; D.P.U. 86-36-C (1988); D.P.U. 86-36-E (1988)). In addition, NYNEX notes the Department's non-traditional regulatory treatment for telecommunications companies established in D.P.U. 1731, which adopted a policy of "liberating" non-dominant carriers from rate-of-return regulation (id., citing D.P.U. 1731, at 63 (1985)). Moreover, NYNEX asserts that when the Department approved AT&T's proposal for an alternative form

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[22] NYNEX asserts that the cases cited by NECTA do not "stand for the proposition that under Massachusetts' statutory scheme, traditional regulation is the only method to establish reasonableness of rates" (NYNEX Response to Briefing Question No. 5, at 1).

of price regulation in D.P.U. 91-79, it "demonstrate[d] that [it] has the necessary statutory authority to consider and grant NYNEX's Plan" (NYNEX Response to Briefing Question No. 11(a) at 1, citing D.P.U. 91-79 (1992)).

NYNEX argues that if rate-of-return regulation were a statutory requirement, then (1) the Department's regulatory framework for common carriers set forth in D.P.U. 1731 would be illegal, (2) rate-of-return regulation would be required for all carriers, and (3) more than a decade of Department decisions applying G.L. c. 159, §§ 14 and 20 would be invalidated (NYNEX Response to Briefing Question No. 1, at 5). In addition, NYNEX asserts this interpretation would undermine the Department's present regulatory policies by requiring that "[a]ll dominant and non-dominant telecommunications carriers including [pay-telephone service providers], other common carriers, and alternative operator service providers ... file rate cases in order to establish a revenue requirement to justify tariffed rates" (NYNEX Response to Briefing Question No. 6, at 1). NYNEX also concludes that a similar interpretation would apply to thousands of transportation common carriers who operate under a similar statutory scheme (id.).

Moreover, NYNEX claims that states with regulatory statutes comparable to those in Massachusetts have permitted price regulation without legislative changes (NYNEX Objection at 2 n.1,

citing R.I.P.U.C. No. 1997 (1992); N.Y.P.S.C. Case No. 28961 (1987); N.Y.P.S.C. Opinion No. 87-22 (1987); and N.Y.P.S.C. Opinion No. 87-20 (1987)). According to NYNEX, in 1987, the N.Y.P.S.C. adopted an alternative regulatory plan with a sharing mechanism for New York Telephone (NYNEX Response to Briefing Question No. 12, at 2, citing N.Y.P.S.C. Case No. 28961 (1987)). NYNEX also states that recently the N.Y.P.S.C. approved an alternative regulatory plan for AT&T, with no sharing mechanism and a 2.5 percent annual revenue increase (id., citing N.Y.P.S.C. Case No. 91-C-1323/1329 (AT&T) (1992)). According to NYNEX, the N.Y.P.S.C. also has permitted alternative forms of regulation for other utilities (id.). NYNEX contends that "[i]n none of these decisions has the N.Y.P.S.C. perceived the alternative regulatory frameworks as either conflicting or interfering with its ratemaking ability or statutory responsibilities to ensure rates charged are `adequate and in all respects just and reasonable'" (id., citing P.S.L. § 91). The Company also asserts that although some states have taken legislative action to address alternative regulation, this does not mean that, "in the absence of such legislation, the state regulatory commission lacked the legal authority to adopt such plans" (id.).

Further, NYNEX states, the Federal Communications Commission ("FCC") has interpreted the Communications Act, the federal statute similar to Chapter 159, as not requiring rate-of-return

regulation or any particular regulatory model (NYNEX Response to Briefing Question No. 12, at 3-5 citing 47 U.S.C. § 151; Report and Order (AT&T Price Cap) 4 FCC Rcd 3297 (1989); Second Report and Order (Price Cap for Local Exchange Carriers) 5 FCC Rcd 6876 (1990)). According to NYNEX, the FCC determined that under the price regulation approach, AT&T (1) is not free to earn excessive profits over its costs, (2) rates are determined prospectively by applying an adjustment formula, which captures changes in company and industry-wide costs, and (3) because price cap rates reflect costs and take into account profits, AT&T would meet its statutory mandate, ensuring just and reasonable rates (id. at 5).

Finally, in responding to NECTA's argument that NYNEX's Plan violates a "comprehensive statutory scheme" for regulation of telecommunications carriers, NYNEX argues that none of the other statutes cited by NECTA would preclude the Department's adoption of the Company's Plan because, according to NYNEX, the statutes cited by NECTA give the Department the authority to conduct certain investigations but do not require that the Department do so (NYNEX Objection at 10).

IV. STANDARD OF REVIEW

The Department's Procedural Rule, 220 C.M.R. § 1.06(6)(e), authorizes a party to move for dismissal of "all issues or any issue in [a] case" at any time after the filing of an initial pleading. The Department's current standard for ruling on a

motion to dismiss for failure to state a claim upon which relief can be granted was articulated in Riverside Steam & Electric Company, D.P.U. 88-123, at 26-27 (1988). [23] In Riverside, the Department denied the respondent's motion to dismiss, finding that it did not "appear[] beyond doubt that [the petitioner] could prove no set of facts in support of its petition." [24] Id. & n.10.

In determining whether to grant a motion to dismiss, the Department takes the assertions of fact included in the filing and pleadings as true and construes them in favor of the non-moving party. Riverside, at 26-27. Dismissal will be granted by the Department if it appears that the non-moving party would be entitled to no relief under any statement of facts that could be proven in support of its claim. See id.

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[23] Procedures for dismissal and summary judgment properly can be applied by an administrative agency where the pleadings and filings conclusively show that the absence of a hearing could not affect the decision. Massachusetts Outdoor Advertising Council v. Outdoor Advertising Bd., 9 Mass. App. Ct. 775, 783-786 (1980); Hess and Clark, Div. of Rhodia, Inc. v. Food and Drug Admin., 495 F. 2d 975, 985 (D.C. Cir. 1974).

[24] Although Riverside refers to Massachusetts Rule of Civil Procedure 12(b)(6), the Department has not adopted the Massachusetts Rules of Civil Procedure. These rules, however, sometimes provide useful dispositive models. See, e.g., 220 C.M.R. § 1.06(6)(c); see Attorney General v. Department of Pub. Utils., 390 Mass. 208, 212-213 (1983) (rules of court do not govern procedure in executive department).

V. ANALYSIS AND FINDINGS

As noted in Section I., supra, the remaining issue that must be decided for purposes of NECTA's Motion is whether NYNEX's petition for alternative regulation [25] cannot be allowed under the existing statutory framework. While NECTA seems to concede that the Department has jurisdiction to adopt alternative regulation under G.L. c. 159, we recognize that our authority to approve NYNEX's Plan rests on our jurisdiction generally to adopt alternative regulation under G.L. c. 159. Therefore, to respond to NECTA's Motion, we must address the following two issues: (1) whether G.L. c. 159 prohibits the Department from adopting alternatives to the traditional rate-of-return model; [26] and (2)

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[25] The term "alternative regulation" implies the existence of a traditional or standard (but not necessarily statutorily mandated) method of regulation against which alternatives can be evaluated. The traditional form of utility ratemaking for the Department and most, if not all, utility ratemaking bodies at the state and federal level has been rate-of-return regulation. See Notice of Inquiry and Order Seeking Comment on Incentive Regulation, D.P.U. 94-158, at 1 (1994) ("The ultimate goal of the [Department] ... is to provide a framework that ensures that the utilities it regulates provide safe, reliable, and least-cost service. Mergers and Acquisitions, D.P.U. 93-167-A at 4 (1994). The Department has to date pursued this goal within a framework of traditional cost-of-service, rate-of-return regulation.").

[26] For purposes of addressing NECTA's Motion, our analysis will focus on the Department's authority under G.L. c. 159. We note, however, that the question of the Department's authority to adopt incentive ratemaking for electric and gas utilities under G.L. c. 164 is being considered in D.P.U. 94-158.

whether NYNEX has failed to state a claim upon which relief can be granted.

A. Whether G.L. c. 159 prohibits the Department from adopting alternatives to the traditional rate-of-return model?

1. G.L. c. 159

The Department's jurisdiction for regulation of intrastate telecommunications service within the Commonwealth is provided under G.L. c. 159. See AT&T Communications of New England, Inc., D.P.U. 91-79, at 13 (1992). The Department has broad general supervisory power over the provision of telecommunications services. G.L. c. 159, § 12. Specifically, section 12 states:

> The [D]epartment shall, so far as may be necessary for the purpose of carrying out the provisions of law relative thereto, have general supervision and regulation of, and jurisdiction and control over ... [the] transmission of intelligence within the commonwealth by electricity, by means of telephone lines or telegraph lines or any other method or system of communication, including the operation of all conveniences, appliances, instrumentalities, or equipment appertaining thereto, or utilized in connection therewith [emphasis added].

Sections 14 and 20 of G.L. c. 159 give the Department authority over the rates of common carriers subject to the Department's jurisdiction. See also G.L. c. 159, § 17 ("All charges made ... by any common carrier for any service rendered ... shall be just and reasonable ... and every unjust or unreasonable charge is hereby prohibited and declared unlawful"). Section 14 states:

> Whenever the department shall be of opinion, after a hearing had upon its own motion or upon complaint, that any of the rates, fares or charges of any common carrier for any services to be performed within the commonwealth, or the regulations or practices of such common carrier affecting such rates, are unjust, unreasonable, unjustly discriminatory, unduly preferential, in any wise in violation of any provision of law, or insufficient to yield reasonable compensation for the service rendered, the department shall determine the just and reasonable rates, fares and charges to be charged for the service to be performed ... [emphasis added].

Section 20 states:

> Whenever the department receives notice of any changes proposed to be made in any schedule filed under this chapter which represent a general increase in rates by a common carrier furnishing the service of transmission of intelligence by electricity, it shall ... make an investigation as to the propriety of such proposed changes .... After such hearing and investigation, the department may make, in reference to any new rate, joint rate, fare, telephone rental, toll classification, charge, rule, regulation or form of contract or agreement proposed, such order as would be proper in a proceeding under section fourteen. At any such hearing involving any proposed increase in any rate, joint rate, fare, telephone rental, toll or charge, the burden of proof to show that such increase is necessary to obtain a reasonable compensation for the service rendered shall be upon the common carrier. If [as regards] ... any proposed decrease in any rate ... it shall appear to the department that the said rate, joint rate, fare, telephone rental, toll or charge is insufficient to yield reasonable compensation for the service rendered, the department may determine what will be a just and reasonable minimum to be charged ... [emphasis added].

Thus, under G.L. c. 159, the Department is responsible for ensuring a "just and reasonable" standard for ratemaking purposes.[27] Section 14 also requires that rates be not unjustly

(continued...)

discriminatory or unduly preferential. See Attorney Gen. v. Department of Pub. Utils., 390 Mass. 208, 234 (1983), citing American Hoechest Corp. v. Department of Pub. Utils., 379 Mass. 408, 411 (1980).

However, a review of the plain language of the statutes reveals that while the General Court specified that rates were to be "just and reasonable" [28] and that rates should provide a

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[27](...continued)
[27] Although, as the Supreme Judicial Court has noted, "the line between ... sections [14 and 20] is not perfectly clear," it is apparent that the respective objects of these provisions are distinct. See New England Tel. & Tel. Co. v. Department of Pub. Utils., 376 Mass. 28, at 31 (1978). Section 14 sets forth (1) the Department's authority to investigate a common carrier's existing tariffs, either on its own motion or upon the complaint of a third party and (2) the standard for rates of common carriers. Section 20, on the other hand, prescribes the process by which a utility, on its own initiative, shall propose changes to an existing tariff or introduce a new tariff and the procedures and standards by which the Department shall investigate those tariffs. Id., at 32-33 (Court held that while under a § 14 proceeding the Department must establish rates, it has discretion, although not unlimited discretion, to refrain from fixing rates in a § 20 proceeding). In a § 20 proceeding, the Department may make "such order as would be proper in a proceeding under section fourteen." G.L. c. 159, § 20.

[28] The Department's "just and reasonable" standard is typical of the "broad [ratemaking] standards" established for regulatory commissions at the state and federal level and "[i]t is up to the various commissions ... to interpret this duty." Charles F. Phillips, Jr., The Regulation of Public Utilities 119, 874-75 (3d ed. 1993); see also James C. Bonbright, Albert L. Danielsen, David R. Kamerschen, Principles of Public Utility Rates 76 (2d ed. 1988) ("While some of the public utility statutes rest content with the requirement that rates be reasonable and not unjustly
(continued...)

utility "reasonable compensation" with reference to the services provided, neither of these two sections of the statute prescribe a particular method by which the Department must fulfill its statutory mandate of setting just and reasonable rates.

Nothing in G.L. c. 159 indicates that the legislature intended to limit the Department to a specific regulatory scheme, such as cost-of-service, rate-of-return ratemaking. Compare Special St. of 1918, c. 188, § 14 (General Court offered Bay State Street Railway Company the opportunity to reorganize pursuant to a ten-year plan whereby management would be undertaken by a board of trustees, with the power to "fix such rates and fares as, in their judgment, will produce sufficient income to meet the cost of the service ...")[29] (emphasis added) and St. 1978 c. 292, § 2 (setting forth specific standard for calculating pole attachment rates) with G.L. c. 159, § 14

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[28](...continued)
discriminatory, others go a certain distance toward prescribing or implying standards of reasonableness. This may take the form of an enumeration of objectives of rate-control policy or as a specification of measures or tests of reasonable rates which the regulating commission is instructed to follow or which it must take into consideration in reaching a rate decision. All of these statutory provisions leave much room for interpretation by a commission, subject to the rulings of the appellate courts.").

[29] The Supreme Judicial Court recognized that this was a specific requirement by the General Court for the cost-of-service method. Donham v. Public Serv. Comm'rs, 232 Mass. 309, 322-323 (1919).

(requiring just and reasonable rates) and G.L. c. 159, § 20 (requiring reasonable compensation and determination of a just and reasonable minimum charge). The just-cited comparison of statutes and special act demonstrates that when the Legislature intends to direct the Department to employ a particular regulatory method, it does so. The broad delegation made by the statute at issue in this investigation (i.e., G.L. c. 159) strongly bespeaks a different legislative intention.

A narrow construction of the Department's ratemaking authority under sections 14 and 20 is inconsistent with the broad authority that the Legislature vested generally in the Department under G.L. c. 159 and recognized by the Supreme Judicial Court. Donham v. Public Serv. Comm'rs , 232 Mass. 309, 313, 325 (1919) ("scope of the powers conferred by the statute upon the public service commission [the Department's predecessor commission that functioned under a virtually identical statutory scheme] is far reaching", such powers are "limited only by the requirement that [rates] be `just and reasonable'"); see also Board of Survey of Arlington v. Bay State St. Ry. Co. , 224 Mass. 463, 469 (1916) (St. 1913, c. 784 [which is now codified in c. 159] "marked a radical change in the policy of the Legislature in the regulation of street railways. It conferred upon the public service commission far greater powers over the operation and accommodations to be provided by such common carriers than had

been vested in any board by earlier acts. Summarily stated, it clothed the commission with full power to require safe, reasonable and adequate service to the public from all common carriers."); Holyoke St. Ry. Co. v. Department of Pub. Utils. , 347 Mass. 440, 450 (1964) (the Department can "exercise a wide range of discretion in appraising the public interest and in adopting reasonable policies, principles, and standards for its guidance."). In evident recognition of the need to respond flexibly to changing economic and technological realities, the Legislature vested broad authority in the Department to regulate common carriers. Evolving construction of economic regulatory statutes to adapt to changing economic circumstances and technology is a principle of long standing in Massachusetts law. Pierce v. Drew , 136 Mass. 75, 81 (1883) (accommodating discovery of the telegraph under prior laws).

2. Supreme Judicial Court Precedent

Our interpretation of the statutory scheme described above is consistent with that of the Supreme Judicial Court ("Court"). The Court has stated that the Department's statutory obligation requires only that rates "must 'yield reasonable compensation for the services rendered' and must be 'just and reasonable' having relation to 'the service to be performed'". See Donham , 232 Mass. at 313, citing Board of Survey of Arlington , 224 Mass.

at 469.[30] Thus, "[t]he only limitation upon the commission in the regulation of the rates and charges of public service companies is that the rates must not be set so low as to deprive the utility of the opportunity of earning a reasonable return on its property." See Irston R. Barnes, Ph.D., Public Utility Control in Massachusetts: A Study in the Commission Regulation of Security Issues and Rates 102 (1930); see also Fitchburg Gas & Elec. Light Co. v. Department of Pub. Utils., 371 Mass. 881, 884 (1977) ("Confiscatory rates violate arts. 1, 10, and 12 of the Declaration of Rights of the Massachusetts Constitution, and the Fourteenth Amendment to the United States Constitution."); Boston Edison Co. v. Department of Pub. Utils., 375 Mass. 1, 10, cert. denied, 439 U.S. 921 (1978) (confiscation is defined as depriving "a utility of the opportunity to realize a fair and reasonable return on its investment").[31] In addition, the Court has found

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[30] "Reasonable compensation" has been defined to mean "sufficient to yield a fair return on the reasonable value of the property used or invested for doing the business after paying costs and carrying charges." New England Tel. & Tel. Co. v. Department of Pub. Utils., 331 Mass. 604, 615 (1954) (quoting Opinion of the Justices, 251 Mass. 569, 610 (1925)).

[31] See U.S. Const. amends. V and XIV ("[N]or shall private property be taken for public use, without just compensation") (emphasis added); Mass. Const. Pt. 1, Art. 10 ("And whenever the public exigencies require that the property of any individual should be appropriated to public uses, he shall receive a reasonable compensation therefor.") (emphasis added); Duquesne Light Co. v. Barasch, 488 U.S.

(continued...)

that the "just and reasonable" standard involves a balancing of the public interests and the interests of utility investors. Donham, 232 Mass. at 326 ("the public service commissioners may make such changes therein as in its judgment are required by the public interests and the rights of the owners of invested capital"). [32,33]

In considering the Department's ratemaking authority under G.L. c. 164, § 94 to permit recovery of an electric utility's prudent investment in plant reasonably abandoned before completion, the Court suggested that the question of what form

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[31](...continued)
299, 308 (1988) ("If the rate does not afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments.") (emphasis added).

[32] See also Jeffrey L. Hess, Sun-Peak -- Over the Rate Regulation Edge: Are Market-Based Rates "Just and Reasonable" or De Facto Deregulation?, 28 Idaho L. Rev. 193, 197, 199 (1991-92) ("setting 'just and reasonable' rates requires the regulator to evaluate the two elements of the utility's interest [i.e., the 'fair value' of the property dedicated by the utility to a public use, and the reasonable rate of return on that 'fair value'] and then balance them against the consumer's interest"); ("'Just and reasonable' ... is a fluid concept always ebbing and flowing like the sea, yet constantly and rigidly bound by public and utility interests.").

[33] We note that, not the petitioner NYNEX but, others opposed to NYNEX's Plan express anxiety about allegedly confiscatory effects that allowance of the Plan might have on the Company. The Plans' opponents are advancing a claim of harm on NYNEX's behalf that one would expect NYNEX instead to have made, but NYNEX has not done so. See note 34, below.

regulation should take is one of policy:

> We do not substitute our judgment for that of an administrative agency where no constitutional question is presented. We decline to prescribe a common law of utility ratemaking. Ratemaking is a legislative, not a judicial, function. Our involvement, beyond constitutional questions, has been to assure that the agency has adhered to statutory requirements. Where agency action is irrational, we will find an error of law. But, as we have said and ruled in a variety of contexts, questions of policy are for an administrative agency.

Attorney Gen. v. Department of Pub. Utils. , 390 Mass. 208, 228 (1983) (citations omitted); see also Massachusetts Oilheat Council v. Department of Pub. Utils. , 418 Mass. 798, 805 (1994) (Department has discretion under G.L. c. 164, § 94 to allow gas companies to use special contracts "to promote the policy of increased competition in the energy market").

While the Court has never addressed the precise question of whether the Department can permit substitution of an alternative regulatory scheme, such as price cap regulation, for traditional cost-of-service regulation, the Court has repeatedly held, within the context of cost-of-service, rate-of-return regulation, that the Department has "wide discretion in choosing its approach to rate regulation" by selecting among different theories or methods. New England Tel. & Tel. Co. v. Department of Pub. Utils. , 371 Mass. 67, 71, 83-85 (1976) ("Our 'fundamental law requires no particular theory or method to be used in determining a rate base, provided the resulting rates are not

confiscatory.'"; [34] Company's use of "value of service" standard to determine rate structure, rather than traditional cost-of-service standard, was reasonable); see also New England Tel. & Tel. Co. v. Department of Pub. Utils., 372 Mass. 678, 683-684 (1977) ("Rejection of the plan I price structure was not an abuse of discretion. ... This court will not overrule departmental action merely because the department used one approach in its decision-making rather than another, as long as the resultant decision is not confiscatory or otherwise illegal."); New England Tel. & Tel. Co. v. Department of Pub. Utils., 360 Mass. 443, 453 (1971), citing New England Tel. & Tel. Co. v. Department of Pub. Utils., 331 Mass. 604, 616 (1954) ("[The Court] would not construe the Constitution of this Commonwealth as compelling `the use of any particular theory or method or combination of theories or methods for determining a rate base,' and ... `[w]e would not be justified in laying hold of any part of our fundamental law for purposes of overriding the

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[34] NYNEX has not raised the objection of confiscatory effect as an obstacle to Department authority to allow the Plan petitioned for. Protection from confiscatory effects of ratesetting is a Federal and state constitutional protection. Granting voluntarily petitioned-for approval to provide services in accordance with an industry-based cost index would hardly seem to risk unconstitutional or extrastatutory confiscatory action by the Department. With due respect to the arguments of those who oppose NYNEX's Plan, their argument in this regard seems little more than that the Department should disallow the Plan to protect NYNEX from itself.

department merely because a particular approach to rate regulation was not used.'").

The Legislature has acted with a consistent approach in delegating authority over utilities other than common carriers. The Court also has found that the Department has similarly broad rate regulation authority of the electric, gas, and water industries under G.L. c. 164, § 94. See American Hoechest Corp., 379 Mass. at 413 ("[W]hen alternative methods are available, the department is free to select or reject a particular method as long as its choice does not have a confiscatory effect or is not otherwise illegal."). [35]

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[35] See also Attorney Gen. v. Department of Pub. Utils., 392 Mass. 262, 268-269 (1984) ("Where the result of employing a specific [cost of capital] methodology in rate setting is not impermissible, the choice of the methodology is a matter committed to agency discretion and is beyond the scope of our review."); Attorney Gen. v. Department of Pub. Utils., 390 Mass. 208, 233 (1983) ("A choice between alternative methods of allocation of revenue needs made by [a utility] and approved by the Department is appropriate as long as it does not have a confiscatory effect and is not otherwise illegal. ... Cost of service need not be the sole criterion used in establishing rate classifications."); Massachusetts Elec. Co. v. Department of Pub. Utils., 376 Mass. 294, 302 (1978) ("When alternative methods [for determining a utility's cost of equity] are available, the Department is free to select or reject a particular method as long as its choice does not have a confiscatory effect or is not otherwise illegal."); Boston Edison Co. v. Department of Pub. Utils., 375 Mass. 1, 19, cert. denied, 439 U.S. 921 (1978) ("The Department is not compelled to use any particular method for calculating the rate base, provided that the end result is not confiscatory -- a matter in which the utility bears the burden of proof."); Fitchburg Gas and

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Furthermore, the Court has held that in some circumstances the Department is not even bound to adhere to cost-based standards. Id., at 411-412, citing Monsanto Co. v. Department of Pub. Utils., 379 Mass. 317, 320 (1979) (For purposes of cost allocation and rate design, the Court stated that "[w]hile cost of service is a well-recognized basis for utility rate structures, it need not be the sole criterion. ... The Department approved the reduced rate as `an experiment in alternative rate-design. It may turn out that there are economic factors justifying the reduced rate."); see also Trustees of Clark Univ. v. Department of Pub. Utils., 372 Mass. 331, 336-337 (1977) ("A Massachusetts utility's rates need not be structured on a cost-related basis, unless, after fair warning, the department requires that approach.").

3. Department Precedent

In addition, the Department's practice over many decades in the regulation of common carriers and other industries shows a consistent pattern in construing its authority to adopt alternative methods of regulation in response to changing market

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[35](...continued)
Elec. Light Co. v. Department of Pub. Utils., 371 Mass. 881, 886 (1977) (In upholding the Department's exclusion of property from the utility's rate base, the Court held "the Department [is] free to select a rule of its choice on this subject as long as the rule was consistently applied, did not have a confiscatory effect, and as long as no special circumstances compelled application of a different rule." , emphasis in original).

circumstances and consumer needs so as to better fulfill its statutory mandate. The Department's actions under its broad statutory authority have been accorded deference in the realm of economic regulation by the Court. See, e.g., Massachusetts Oilheat Council, 418 Mass. at 802-807.

Like other utility commissions, the Department traditionally has employed cost-of-service, rate-of-return regulation to determine just and reasonable rates for utilities under its jurisdiction; [36] but has also often utilized alternative or "incentive" methods to traditional rate regulation where it determined that a different method would better satisfy its public policy goals and statutory obligations. In the Department's current investigation into incentive regulation for the electric and gas industries, we noted that:

> The Department has ... taken several steps towards increasing the application of financial incentives in utility operations, through approval of such initiatives as margin sharing, see Boston Gas Company, D.P.U. 93-60, at 312-326 (1994), and Boston Gas Company, D.P.U. 92-259 (1993)[, aff'd sub nom. Massachusetts Oilheat Council v. Department of Pub. Utils., 418 Mass. 798 (1994)]; marginal cost-based economic development rates, see Commonwealth Electric Company, D.P.U. 93-41 (1993); and an incentive

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[36] See D.P.U. 94-158, at 1, citing Mergers and Acquisitions, D.P.U. 93-167-A at 4 (1994) (Department has to date pursued goal of providing safe, reliable, and least-cost service within a framework of traditional cost-of-service, rate-of-return regulation); D.P.U. 91-79, at 41 (monopoly provider of utility service traditionally subject to rate base, rate-of-return regulation).

mechanism for electric power generation, see Boston Edison Company, D.P.U. 89-100 (1989). See also New England Telephone and Telegraph Company, D.P.U. 1731 (1985); Gas Transportation, D.P.U. 85-178 (1987); Pricing and Ratemaking Treatment for New Electric Generating Facilities Which Are Not Qualifying Facilities, D.P.U. 86-36-A (1987); AT&T Communications of New England, D.P.U. 91-79 (1992). [37]

See D.P.U. 94-158, at 3.

The Department's efforts in alternative ratemaking also extend to the telecommunications industry. Instead of requiring all common carriers under its jurisdiction to submit to cost-of-service, rate-of-return regulation, the Department has varied the type of regulation for these companies, based on competitive considerations and the carrier's market power. For example, the Department does not impose traditional cost-of-service, rate-of-return regulation on resellers of telecommunications services, mobile radio and cellular common carriers, and most interexchange carriers. See, e.g., First Phone, Inc., D.P.U. 1581 (1984); Cellular Resellers, D.P.U. 84-250-1 (1984); GTE Sprint Communications Corporation, D.P.U. 84-157, at 4 (1985). In addition, in IntraLATA Competition, D.P.U. 1731, at 63 (1985), the Department decided

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[37] See also Integrated Resource Management for Electric Pricing Arrangement Tariff, D.P.U. 86-36-A (1987)-D.P.U. 86-36-G (1989); Massachusetts Electric Company, D.P.U. 91-205 (1991).

not to apply rate-of-return regulation and revenue requirement determinations to nondominant carriers but continued the requirements for dominant carriers such as AT&T and NYNEX. The Department found in that proceeding that the alternative regulatory treatment for nondominant carriers would result in just and reasonable rates. Id. at 64. Finally, in D.P.U. 91-79, the Department changed the method of regulation for AT&T, by allowing market-based pricing for AT&T's sufficiently competitive services and adopting price cap regulation for its basic message telecommunications service. D.P.U. 91-79, at 34-35, 42. In sum, the Department's historical regulation of telecommunications common carriers is consistent with the Department's interpretation of its authority to implement alternative regulation.

4. Other Jurisdictions

Although not controlling of our authority, decisions of foreign jurisdictions on alternative regulatory proposals are instructive and useful. Statutory and decisional law in other jurisdictions provides "persuasive authority by analogy." Commonwealth Elec. Co. v. Department of Pub. Utils. , 397 Mass. 361, 366 n.3 (1986), cert. denied , 481 U.S. 1036 (1987). United States Supreme Court decisions are, of course, binding where germane. We describe other jurisdictions' regulatory schemes because these schemes demonstrate that Massachusetts law is

consistent with similar statutory frameworks elsewhere.

a. United States Supreme Court

A review of United States Supreme Court ("Supreme Court") cases also supports the proposition that just and reasonable rates can be achieved through alternative ratemaking. In the context of a case dealing with cost-of-service ratemaking, the Supreme Court has recognized that state regulators are not bound by a single ratemaking method in their determination of just and reasonable rates. In upholding a decision of the Pennsylvania Public Utility Commission to allow an electric utility to recover the costs associated with cancelled nuclear generating units through increased rates, the Supreme Court stated:

> The designation of a single theory of ratemaking as a constitutional requirement would unnecessarily foreclose alternatives which could benefit both consumers and investors. The Constitution within broad limits leaves the States free to decide what ratesetting methodology best meets their needs in balancing the interests of the utility and the public.

Duquesne Light Co. v. Barasch, 488 U.S. 299, 316 (1989). Duquesne Light Company reaffirmed the landmark decision Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944). In Hope, the Supreme Court upheld an order of the Federal Power Commission reducing rates of a natural gas company, pursuant to a "just and reasonable" standard under the Natural Gas Act, stating:

> We held in Federal Power Commission v. Natural Gas

> Pipeline Co. [315 U.S. 575, 586 (1942)] ... that the Commission was not bound to the use of any single formula or combination of formulae in determining rates. Its rate-making function, moreover, involves the making of "pragmatic adjustments." And when the Commission's order is challenged in the courts, the question is whether that order "viewed in its entirety" meets the requirements of the Act. Under the statutory standard of "just and reasonable" it is the result reached not the method employed which is controlling. It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end.

Federal Power Comm'n v. Hope Natural Gas Co., at 602 (citations omitted) (emphasis added).

In a line of cases building on Hope, the Supreme Court has gone even further, ruling that Constitutional and statutory standards can be satisfied by alternative regulatory schemes that rely on non-cost factors for determining just and reasonable rates. In Wisconsin v. Federal Power Comm'n, 373 U.S. 294 (1963), the Supreme Court upheld an order of the Federal Power Commission to consider a departure from traditional cost-of-service ratemaking standards in regulating natural gas producer rates. The Supreme Court stated:

> [T]o declare that a particular method of rate regulation is so sanctified as to make it highly unlikely that any other method could be sustained would be wholly out of keeping with this Court's consistent and clearly articulated approach to the question of the Commission's power to regulate rates. It has been repeatedly stated that no single method need be followed by the Commission in considering the justness and reasonableness of rates ....
>
> ....

> [This] Court has never held that the individual company cost-of-service method is a sine qua non of natural gas rate regulation. Indeed the prudent investment, original cost, rate base method which we are now told is lawful, established, and effective is the very one the Court was asked to declare impermissible in the Hope case less than 20 years ago.
>
> To whatever extent the matter of costs may be a requisite element in rate regulation, we have no indication that the area method will fall short of statutory or constitutional standards. The Commission has stated in its opinion in this proceeding that the goal is to have rates based on the "reasonable financial requirements of the industry" in each production area ... and we were advised that composite cost-of-service data will be considered in the area rate proceedings. Surely we cannot say that the rates to be developed in these proceedings will in all likelihood be so high as to deprive customers, or so low as to deprive producers, of their right to a just and reasonable rate.

Wisconsin v. Federal Power Comm'n, 373 U.S. 294, 309-310 (1963) (citations omitted) (emphasis added). In 1968, the Supreme Court declared that the Federal Power Commission had constitutional and statutory authority to depart from traditional individual company cost-of-service regulation and adopt a system of "maximum area rates" based on composite cost data of gas producers, in order to provide a useful incentive for exploration and to prevent excessive producer profits, thus protecting both present and future consumer interests. In re Permian Basin Area Rate Cases, 390 U.S. 747, 768-790 (1968). [33] The Supreme Court stated:

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[33] The Supreme Court "has repeatedly held that the width of administrative authority must be measured in part by the (continued...)

> [In order for the regulatory scheme to be reasonable, in part, it must] maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable. ... The Commission's responsibilities necessarily oblige it to give continuing attention to values that may be reflected only imperfectly by producers' costs; a regulatory method that excluded as immaterial all but current or projected costs could not properly serve the consumer interests placed under the Commission's protection.

In re Permian Basin Area Rate Cases, 390 U.S. at 792, 815; see also Mobil Oil Corp. v. Federal Power Comm'n, 417 U.S. 283, 292 (1974) (upholding the Commission's area rates for Southern Louisiana area).

b. FCC

The FCC has also approved alternative regulation for providers of interstate telecommunications services. [34] In commenting on its authority to approve price cap regulation for dominant carriers, the FCC noted that the Communications Act,

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[33](...continued)
> purposes for which it was conferred....[R]ate-making agencies are not bound to the service of any single regulatory formula; they are permitted, unless their statutory authority otherwise plainly indicates, `to make the pragmatic adjustments which may be called for by particular circumstances'." In re Permian Basin Area Rate Cases, 390 U.S. at 776-777 (citations omitted) (emphasis added).

[34] The FCC has approved price cap regulation for AT&T and for Local Exchange Carriers ("LECs"). See Report and Order, 4 FCC Rcd 2873, at 3208, 3297 (1989); Second Report and Order, 5 FCC Rcd 6786, 6792 (1990).

which "mandates that rates for interstate telecommunications common carrier services be just, reasonable, and non-discriminatory," [35] "does not compel this Commission to utilize a rate-of-return methodology or any other particular regulatory model in fulfilling our statutory obligations." Further Notice of Proposed Rulemaking , 3 FCC Rcd 3195, at 3296 (1988). According to the Commission, "[a] review of court decisions involving [the FCC] and other federal agencies with rate authority similar to our own confirms that, rather than insisting upon a single regulatory method for determining whether rates are just and reasonable, courts evaluate whether the end results of particular regulatory schemes produce rates that fall within a 'zone of reasonableness'." Id. at 3297, citing , FERC v. Pennzoil Producing Co. , 439 U.S. 508, 517 (1979). The Commission also relied on the Supreme Court's pronouncements in Duquesne Light Co. v. Barasch , that "no single method need be followed by the Commission in considering the justness and reasonableness of rates" and that "[t]he designation of a single theory of rate making ... would unnecessarily foreclose alternatives which could benefit both consumers and investors." Report and Order , 4 FCC Rcd 2873, at 3296 (1989). The Commission stated:

> For rates to fall within the zone of reasonableness,

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[35] 47 U.S.C. §§ 201 (just and reasonable standard), 202 (non-discriminatory standard).

> the agency rate order must constitute a "reasonable balancing" of the "investor interest in maintaining financial integrity and access to capital markets and the consumer interest in being charged non-exploitative rates." While costs often offer the principal points of reference for determining whether rates are just and reasonable, the zone of reasonableness standard does not require an agency "to adhere `rigidly to a cost-based determination of rates, much less to one that bases each [carrier's] rates on his own costs.'".... Ultimately, the substantive mandate under which we operate requires only that we select a reasonable ratemaking approach that is capable of keeping rates in the zone of reasonableness, or of detecting and correcting for the failure of market forces to do so.

Further Notice of Proposed Rulemaking , 3 FCC Rcd at 3195, 3297-3298 (1988).

In adopting price cap regulation for AT&T, the FCC stated that its substantive mandate was to adopt a ratemaking approach capable of "keeping rates in the zone of reasonableness, or detecting and correcting for the failure of market forces to do so", and that the alternative form of regulation adopted for AT&T "fulfills the Communications Act's substantive requirement of ensuring just, reasonable, and non-discriminatory rates". Report and Order , 4 FCC Rcd 2873, at 3297 (1989). In describing the elements of the price cap that satisfied the statutory mandate, the Commission stated:

> First, the initial caps are based upon existing rates that have been filed and reviewed, and have gone into effect pursuant to our existing rate-of-return regulatory scheme. Second, the plan's adjustment formula accounts for changes both in individual firm

> costs, and in economy-wide and industry-wide costs. [36] Third, we intend to engage in continued monitoring of individual carrier cost data, and will undertake a comprehensive review of, among other things, the relationship between costs and rates beginning after three years. Finally, tariff investigations under Section 204 of the Act, and complaint proceedings under Section 208 of the Act, will continue to involve evaluation of a carrier's rates in light of its costs and profits.

Further Notice of Proposed Rulemaking , 3 FCC Rcd 3195, at 3299 (1988).

In response to criticism that the price cap plan would allow AT&T to earn "excessive profits in light of their costs [in part because of the absence of an earnings sharing mechanism]," [37] the FCC noted that "the use of rate of return generated existing rates to establish AT&T's initial price caps, and the subsequent price cap adjustments made pursuant to the [Price Cap Index] formula should keep AT&T's profit levels in check, even though the [Price Cap Index] formula is not explicitly tied to profits." Report and Order , 4 FCC Rcd 2873, at 3299 (1989). The FCC stated that "to the extent that AT&T is able to improve productivity faster than anticipated ... adjustments to the PCI formula [could

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[36] According to the FCC, "[t]his reliance upon historical industry productivity data and inflation data to account for carrier costs is analogous to the Federal Power Commission's use of area-wide average natural gas producer costs in ratemaking, which the Supreme Court upheld in Permian Basin Rate Cases ." Further Notice of Proposed Rulemaking , 3 FCC Rcd 3195, at 3299, n. 360 (1988).

[37] Unlike the AT&T price cap plan, the FCC price cap for LECs includes a sharing mechanism.

be made] to ensure that consumers share in that productivity improvement." Id. The Commission stated:

> Notwithstanding that our price cap system continues to monitor and consider profit levels to ensure they are not excessive in light of costs, it is also a system designed to permit greater earnings flexibility than a strict rate of return regime. This design is based upon the fundamental premise underlying incentive regulation and the benefits it will produce for ratepayers -- that is the potential to increase earnings that drives companies to improve their efficiency. Stated another way, we believe that rates resulting in somewhat higher profits may remain just and reasonable in the context of a regulatory regime that encourages carriers to become more efficient and to lower costs, with consumer benefits assured in the form of lower rates than would not otherwise have been achieved. We believe this approach to rate regulation is fully consistent with our statutory mandate to ensure just and reasonable rates.

Report and Order , 4 FCC Rcd 2873, at 3299-3300 (1989). [38]

c. Other States' Utility Commissions

At the state level, all but seven utility commissions have implemented or are currently considering alternative regulation

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[38] Implicit in this finding was the notion that profits that were higher than a carrier could be expected to earn under traditional rate-of-return regulation were within the zone of reasonableness and, therefore, were not excessive. Report and Order , 4 FCC Rcd 2873, at 3299-3300 (1989). The FCC stated that "as long as rates within the zone of reasonableness result, this Commission has broad discretion regarding the manner in which it deals with carrier profits." Id. at 3299, n.1839 citing Nader v. FCC, 520 F.2d 182 (D.C. Cir. 1975); MCI Telecommunications v. FCC, 675 F.2d 408, 416 (D.C. Cir. 1982). The FCC noted that " any ratemaking methodology that utilizes costs that are not firm-specific necessarily allows carriers to improve profits by reducing their costs below the benchmark set by the regulator . Such a result is implicit in the area-wide ratemaking scheme upheld in Permian Basin Area Rate Cases ... ." Id. (citations omitted) (emphasis added).

of telephone companies. [39] As of November 1994, alternative regulation was in effect in 36 states. [40] It is true, as asserted by NECTA and the Attorney General, that some states that have adopted alternative regulation for telephone common carriers, including price cap regulation, did so only after statutory amendments expressly authorizing alternative regulation; [41]

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[39] Vivian Witkind Davis, Ph.D., Nancy Zearfoss, Catherine E. Reed, The National Regulatory Research Institute, Preliminary Results of a Survey on Alternative Regulation and Competition in Telecommunications 4 (December 1994) ("NRRI Survey"). These alternatives primarily consist of revenue sharing, distinctions between basic and competitive services, and price cap plans. NRRI Survey at 4.

[40] Id. Approximately 12 states have adopted price cap plans, and eight more states could have price cap regulation in effect by December 1995. Those states that have adopted price cap regulation are: California, Delaware, Illinois, Michigan, New Jersey, New York, North Dakota, Oregon, Pennsylvania, Rhode Island, Vermont, and Wisconsin. NRRI Survey at 4; New England Telephone and Telegraph Company, Docket Nos. 5700/5702 (Vt. Pub. Serv. Bd. 1994). NYNEX Vermont opted out of the plan approved by the Vermont Board. NYNEX's Notice Pursuant to Vt. Stat. Ann. tit. 30, § 226b(g) (October 20, 1994).

[41] For example, Pennsylvania, New Jersey, Vermont, Illinois, North Dakota, and Oregon all adopted price cap regulation pursuant to legislation specifically enabling alternative regulation. See, e.g., Re Bell Atlantic--Pennsylvania Inc.'s Petition and Plan for Alternative Regulation Under Chapter 30, Docket Nos. P-00930715, P-00930715C001, P-00930715C002 (Pa. Pub. Util. Comm'n 1994); Pa. Public Utility Code, Chapter 30 ("Alternative Form of Regulation of Telecommunications Services"), 66 Pa. Con. Stat. Ann. §§ 3001-3009 (Supp. 1994); Re New Jersey Bell Telephone Company, Docket No. TO92030358 (N.J. Bd. of Regulatory Comm'rs 1993), 143 P.U.R. 4th 297 (1993); N.J. Stat. Ann. § 48:2-21.16 (West Supp. 1994) (granting authority to

(continued...)

however, it is not necessary for purposes of our analysis to determine whether these states could have adopted price cap regulation in the absence of a statutory change. [42] It is

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[41](...continued)
approve alternative regulation for telecommunications); New England Telephone and Telegraph Company , Docket Nos. 5700/5702 (Vt. Pub. Serv. Bd. 1994); Vt. Stat. Ann. tit. 30, § 226b (Supp. 1994); Illinois Bell Telephone Company , 92-0448/93-0239 Consol. (Ill. Commerce Comm'n 1994); Ill. Ann. Stat. Ch. 220, § 5/13-506.1 (Smith-Hurd 1993) ("Alternative Forms of Regulation for Noncompetitive Services"); Re Implementation of SB 2320 , Case No. PU-2320-89-333 (N.D. Pub. Serv. Comm'n 1989), 112 P.U.R. 4th 359 (1990); N.D. Cent. Code §§ 49-21-01 to 49-21-22 (Supp. 1993); Re U.S. West Communications, Inc. , Order No. 91-1598 (Or. Pub. Util. Comm'n 1991), 128 P.U.R. 4th 135 (1992); Or. Rev. Stat. § 759.195 (1993). At least one state commission made its own determination that its enabling statutes required amendment to provide the commission with the authority to adopt alternative regulation. Re MFS Intelenet of Maryland, Inc., Order No. 71155 (Md. P.S.C. 1994), 152 P.U.R. 4th 102, 128-130 (1994) (legislative amendment necessary to establish authority to adopt price cap legislation for dominant local exchange carrier). In two jurisdictions, state supreme courts have ruled that alternative regulation adopted by public service commissions violated the requirements of existing statutes. Stewart v. Utah Pub. Serv. Comm'n , 244 Utah Adv. Rep. 11, 24 (Utah 1994) (commission's incentive regulation plan unlawful because "the plan essentially forsakes cost-of-service principles as required by [Utah public utility statute]"); South Carolina Cable Television Ass'n v. Public Serv. Comm'n , 437 S.E.2d 38, 40 (S.C. 1993) (commission lacked statutory authority to adopt a specific earnings sharing plan for LECs, where plan allowed rate of return based on anticipated expenses and profits from future technological changes, in violation of requirement that ratemaking be based on historical data, with allowances for known and quantifiable future changes). But see Tennessee Cable Television Ass'n v. Tennessee Pub. Serv. Comm'n , 844 S.W.2d 151 (Tenn. App. 1992) (commission had power under enabling statutes to require a telephone utility to use excess earnings to expand or improve service to its customers).

(continued...)

sufficient to note that some state utility commissions, with statutory authority very similar to that of the Department, including Rhode Island, California, and New York, have adopted alternative regulation without legislative change. See, e.g., Re Comprehensive Review of Telecommunications , Order No. 14003 (R.I.P.U.C. 1992), 135 P.U.R. 4th 408 (1992) (approving settlement providing for four-year price cap trial for NYNEX that included an earnings sharing mechanism; without discussion, commission implicitly found that it had authority under its statutory mandate to adopt alternative regulation); R.I. Gen. Laws, Title 39, § 39-2-1 (1956, 1990 Reenactment) ("The rate, toll, or charge ... made ... by any public utility ... for any telephone or telegraph message conveyed or for any service rendered or to be rendered in connection therewith, ... shall be reasonable and just, and every unjust or unreasonable charge for the service is prohibited and declared unlawful ..."); Id. § 39-3-12 ("At any hearing involving any proposed increase in

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[42](...continued)
[42] A lack of authority under prior statutes may not have been the reason for enacting such legislation. There may have been reasons for the enactment of "alternative regulation" legislation in these jurisdictions other than the one cited by NECTA and the Attorney General. For example, even if the existing statutes granted the public utility commissions authority to approve alternative regulation, statutory changes may have been necessary for the legislature to direct, rather than merely authorize, a public utility commission that was reluctant to consider alternative regulation.

any rate, toll, or charge, the burden of proof to show that the increase is necessary in order to obtain a reasonable compensation for the service rendered shall be upon the public utility ..."); In Re Alternative Regulatory Frameworks for Local Exchange Carriers , Decision 89-10-031 (Cal. P.U.C. 1989), 107 P.U.R. 4th 1, 166 (1990) (in adopting price cap regulation for Pacific Bell and GTE California, Inc., the state's two largest LECs, commission found that "there is no explicit legal bar to adoption of a regulatory framework not based on traditional rate base rate-of-return analyses"); Cal. Pub. Util. Code, § 451 (West Supp. 1995) ("All charges demanded or received by any public utility ... for ... any service rendered ... shall be just and reasonable. Every unjust or unreasonable charge ... is unlawful."); Id., § 454 ("No public utility shall change any rate ... except upon a showing before the commission and a finding by the commission that the new rate is justified."); Id., § 728 (West 1975) ("Whenever the commission ... finds that the rates ... charged ... by any public utility for or in connection with any service ... are insufficient, unlawful, unjust, unreasonable, discriminatory, or preferential, the commission shall determine ... the just, reasonable, or sufficient rates ..."); In Re New York Telephone Company , Opinion No. 85-17 (N.Y.P.S.C. 1985) (commission concluded a "moratorium plan" would promote utility regulation by incentive, since company would bear risk of many

cost increases but would retain benefit of increased productivity and sales during period covered by moratorium plan); In Re New York Telephone Company , Opinion No. 85-17(A) (N.Y.P.S.C. 1986), 74 P.U.R. 4th 590 (1986); Kessel v. Public Serv. Comm'n , 136 A.D.2d 86, 92 (N.Y. App. Div. 1988) (commission's use of an "expanded second-stage increase following 'formal but expedited hearings,' coupled with a moratorium on a general rate increase, falls within its broad authority to set public utility rates"); N.Y.P.S.C. Case No. 91-C-1323/1329 (AT&T) (1992) (commission approved incentive regulation for AT&T); (N.Y. Pub. Serv. Law, § 91(1) (Consol. 1983) ("All charges [of] ... any telephone corporation for any service ... shall be just and reasonable."); Id., § 91(3) ("No ... telephone corporation shall make or give ... undue or unreasonable preference ..."). The actions of other jurisdictions with similarly broad statutes offer "persuasive authority by analogy," for a determination that statutory amendment is not required to authorize Department adoption of alternatives to traditional rate-of-return regulation for common carriers. Commonwealth Electric , 397 Mass. at 366 n.3; see also Sutherland Statutory Construction Vol. 2B, § 52.03 (5th ed. 1992) (where meaning of statute in question, reference to legislation in other states and jurisdictions which pertains to same subject matter may be helpful source of interpretative guidance) (citing Kneeland v. Emerton , 280 Mass. 371 (1932)).

5. Conclusion

For all of the above reasons, we find that our statutory authority under sections 14 and 20 does not limit the Department to rate-of-return regulation, or any other particular regulatory scheme. The Supreme Judicial Court has stated:

> In questions of statutory interpretation, "ordinary precepts of statutory construction instruct us to accord deference to an administrative interpretation of a statute." ... This is particularly so "where, as here, an agency must interpret a legislative policy which is only broadly set out in the governing statute."
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> ....
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> "We grant substantial deference to an interpretation of a statute by the administrative agency charged with its administration."

Greater Media Inc. v. Department of Pub. Utils. , 415 Mass. 409, 414, 419 (1993) (citations omitted); see also Sutherland Statutory Construction Vol. 3, § 65.03, at 330 (5th ed. 1992) ("[T]he modern and certainly the better trend is that statutes granting powers to administrative agencies should receive a reasonable interpretation, and where the statute has as its aim a system of public regulation that can be administered efficiently and properly only by a group of qualified experts a liberal interpretation to effectuate the purposes and objectives of the statute should be preferred."). The breadth of Department authority delegated under G.L. c. 159, the consistently practical interpretation given to that chapter and to kindred utility statutes by the Supreme Judicial Court, and the similarity of

Massachusetts' statutes to those in other jurisdictions that have adopted alternative regulation for telecommunications common carriers without statutory amendment, all lead us to but one conclusion: viz., that the Department has authority under G.L. c. 159 to permit alternatives to the traditional rate-of-return model.

B. Whether NYNEX has failed to state a claim upon which relief can be granted?

Having concluded that we have statutory authority, pursuant to G.L. c. 159, to adopt forms of alternative regulation, the next question we must answer is whether NYNEX has failed to state a claim upon which relief can be granted. [43] As discussed below, we find that NECTA's Motion must be denied.

As noted in Sections I. and III.A., supra, NECTA argues that the Department should dismiss the filing as patently deficient because the Plan cannot be allowed under the existing statutory framework. Specifically, NECTA and the Attorney General assert that the primary deficiency is that the Plan has no constraint on the level of profits the Company could earn and, thus, severs the link between the Company's costs and its earnings. NECTA contends that the Plan lacks any constraint on earnings because, as a so-called "pure" price cap, it does not include an earnings

[43] For purposes of this analysis, we take the assertions of fact included in the filing and pleadings as true and viewed in favor of NYNEX.

cap or earnings sharing mechanism. Thus, NECTA asserts that because NYNEX has proposed a "pure" price cap it has failed to petition for relief within the Department's authority to grant.

As we have already found, the plain language of G.L. c. 159, §§ 14 and 20 requires only that rates be "just and reasonable" and that a utility receive "reasonable compensation" in relation to the services provided. NECTA argues that "reasonable compensation" must be determined using a company-specific, cost-based measurement of earnings. According to NYNEX, however, the price cap mechanism itself will constrain the Company's rates and, in turn, its earnings. Thus, the price cap mechanism and pricing rules, according to the Company, will ensure that rate changes are tied to changes in industry-wide average costs rather than historical, company-specific costs as measured under rate-of-return regulation, and that rates will thus remain just and reasonable. Therefore, it does not appear that NYNEX would be entitled to no relief under any set of facts that could be proven in support of its petition because, when viewed in favor of the Company, we would accept the Company's assertion that the NYNEX Plan contains an adequate constraint on earnings, if one is indeed necessary in order for a price cap to be lawfully established. [44]

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[44] We note that in commenting on NECTA's Motion and in (continued...)

NECTA also argues that NYNEX's filing must be dismissed because the Plan's lack of a cap on earnings or an earnings sharing mechanism conflicts with what NECTA calls a "comprehensive statutory scheme" governing the Department's regulation of common carriers. NECTA points to statutory provisions dealing with supervision and regulation of common carriers, including G.L. c. 159, § 26 (which authorizes the Department to investigate the fair value of NYNEX's used and useful property for ratemaking purposes under G.L. c. 159, §§ 14, 20); § 31 (forms of accounts, records, and memoranda) and § 32 (annual return; form, time of filing; amendment), both of which set forth accounting and reporting requirements; and § 34A (supervision of companies affiliated with carrier), which makes interaffiliate transactions subject to Department review. NECTA

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[44](...continued)
responding to the Department's briefing questions, the intervenors raised concerns about specific elements of NYNEX's Plan (e.g., the term of the Plan, the amount of pricing flexibility provided by the Plan, specific anticompetitive aspects of the Plan, the starting rates, the level of the productivity factor, the lack of an earnings sharing mechanism, whether the transitional rate process should be continued, the mechanism for reviewing rates, the mechanism for reviewing new services, the pricing of access services, and the definition of pricing baskets), in arguing that the Company's Plan would not produce just and reasonable rates. Since we interpret these arguments as relating to deficiencies of particular elements of the Plan and not to the Department's authority to review the Plan, we will not respond to these concerns in this Interlocutory Order. These concerns go beyond NECTA's Motion and will be addressed in the Department's final Order.

also points to G.L. c. 166, §§ 12A, 14 and 22L; G.L. c. 6A, § 18D(4); and G.L. c. 25, §§ 17 and 18. According to NECTA, these provisions prescribe criteria for a Department analysis of NYNEX's costs and, therefore, the failure of NYNEX to include a cost-based earnings measurement would effectively "repeal" these sections (NECTA Reply at 12). [45]

However, as NYNEX argues, while the statutory provisions discussed by NECTA grant the Department the authority to conduct various investigations for ratemaking purposes, they do not require the Department to do so. The statutory sections NECTA cites only serve to assist the Department in collecting information, without purporting to direct the Department to employ a specific rate-setting methodology. See Massachusetts Oilheat Council , 418 Mass. at 803-804 (rejecting plaintiff's argument that the Department's adoption of a regulatory framework was in excess of its statutory authority because the argument "ignore[d] the permissive language of the statute and purport[ed]

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[45] NECTA also argued that NYNEX's proposal to freeze basic residential rates until August 2001 violates the statutory scheme for directory assistance (St. 1990, c. 291, § 7; G.L. c. 6A, § 18D(4)), by "eliminat[ing] the flow back of customer dividends to residential customers" (NECTA Response to Briefing Question No. 10). According to NYNEX, however, the Company will continue to treat revenues and expenses for directory assistance in accordance with the procedure established in D.P.U. 91-68 (NYNEX Response to Briefing Question No. 10). In addition, NYNEX states that the customer dividend will not be subject to the proposed freeze for basic residential rates (id.).

to turn a statutory grant of authority into a statutory mandate, thereby unduly limiting the very authority granted"). In addition, the Department has discretion to establish alternative reporting requirements for an alternative regulatory plan such as the plan it approved for AT&T. See G.L. c. 159, § 32; D.P.U. 91-79, at 52-53.

Based on the above analysis, we find that it does not appear that NYNEX would be entitled to no relief under any set of facts that could be proven in support of its claim. Riverside , supra , at 26-27. Therefore, we deny NECTA's Motion to Dismiss.

VI. ORDER

Accordingly, after due consideration, it is

ORDERED: That the Motion to Dismiss of the New England Cable Television Association, Inc., filed with the Department on May 11, 1994, be and hereby is DENIED.

By Order of the Department,

Kenneth Gordon
Chairman

Mary Clark Webster
Commissioner