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July 30, 2004

Ms. Beth O'Donnell  
Executive Director  
Public Service Commission  
211 Sower Boulevard  
P.O. Box 615  
Frankfort, KY 40602

**RECEIVED**

**JUL 30 2004**

**PUBLIC SERVICE  
COMMISSION**

RE: The Petition of ALLTEL Kentucky for an Increase in Rates,  
Case No. 2004-00193

Dear Ms. O'Donnell:

Enclosed for filing in the above-referenced matter is an original and eleven (11) copies of ALLTEL Kentucky's Response to Commission Order. Please file-stamp the extra copy and return it to me in the self-addressed, pre-stamped envelope I have enclosed for your convenience.

Thank you for your cooperation in this matter. Please do not hesitate to contact me with any questions you may have.

Sincerely,

WYATT, TARRANT & COMBS, LLP

Noelle M. Holladay

Enclosures

cc: Kimberly K. Bennett  
James H. Newberry, Jr.

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JUL 30 2004

**PUBLIC SERVICE  
COMMISSION**

**COMMONWEALTH OF KENTUCKY**

**BEFORE THE PUBLIC SERVICE COMMISSION**

**In the Matter of:**

<b>THE PETITION OF ALLTEL KENTUCKY FOR</b>	)	<b>CASE NO.</b>
<b>AN INCREASE IN RATES</b>	)	<b>2004-00193</b>

**RESPONSE TO COMMISSION ORDER**

ALLTEL Kentucky, Inc. ("ALLTEL Kentucky") responds to the Commission's June 1 and July 2, 2004 orders in this proceeding as follows:

**GENERAL STATEMENT OF POSITION**

Since October 13, 1998, ALLTEL Kentucky's intrastate operations have been regulated under the statutory alternative regulation plan set forth in K.R.S. §278.516 (the "Alt. Reg. Statute"). The Commission recognized ALLTEL Kentucky's election by order dated December 30, 1998 in Case No. 1998-00529. ALLTEL Kentucky operates and is regulated under the Alt. Reg. Statute because ALLTEL Kentucky clearly satisfied the statutory requirements to be regulated under K.R.S. §278.516 at the time of ALLTEL Kentucky's election in 1998. The Alt. Reg. Statute makes no provision for and does not otherwise contemplate the Commission ordering electing companies to return to traditional rate of return ("ROR") regulation. Subsection (7) of the Alt. Reg. Statute provides that a utility's election "shall remain effective until withdrawn by the filing with the commission of a verified resolution of the small telephone utility's board of directors or other governing body."

Because the Commission expressed a concern in its June Order about whether ALLTEL Kentucky should continue to be regulated under the Alt. Reg. Statute, ALLTEL Kentucky requests an informal conference pursuant to 807 K.A.R. 5:001, Section 4,

during which Commission Staff and all affected parties can discuss possible resolution of this issue and development of acceptable alternatives.

**COMMISSION ACTION GIVING RISE TO THE FILING OF THIS RESPONSE**

In 2002, ALLTEL Kentucky's affiliate, Kentucky ALLTEL, Inc. ("Kentucky ALLTEL"), acquired the Kentucky assets of Verizon South, Inc. (Case No. 2001-00399). On February 13, 2002, the Commission, in approving the acquisition by Kentucky ALLTEL, also ordered the filing of a plan no later than August 2, 2004 regarding the merger of ALLTEL Kentucky and Kentucky ALLTEL ("Plan Regarding Merger"). A Plan Regarding Merger in compliance with this Acquisition Order is being filed contemporaneous with this filing.

On April 23, 2004, ALLTEL Kentucky filed a notice of intent and associated tariff with respect to increasing its basic rates pursuant to the Alt. Reg. Statute. However, the Commission suspended ALLTEL Kentucky's tariff filing until January 6, 2005 and questioned whether ALLTEL Kentucky could still be defined as a "small telephone utility" under the Alt. Reg. Statute given the acquisition of Verizon's Kentucky properties by its affiliate, Kentucky ALLTEL.

In its Order dated June 1, 2004 suspending the tariff filing, the Commission provided as follows:

ALLTEL Kentucky's filing in this case raises two questions: (1) Given the 2002 acquisition of the Kentucky properties of Verizon South, Inc. by Kentucky ALLTEL, Inc. ("Kentucky ALLTEL"), an affiliate of ALLTEL Kentucky, may ALLTEL Kentucky still be defined as a "small telephone utility" pursuant to KRS 278.516(2) such that the alternate regulation provisions of the statute still apply to it? (2) Given that the statute explicitly prescribes that the increase permitted under KRS 278.516(3) is "not to exceed the sum of the annual percentage changes in the GDP for the immediately preceding two (2) calendar years," may a small telephone utility increase its rates based on the annual percentage changes of a sub-

category of the GDP so that its increase would in fact exceed the GDP percentage change for the preceding two calendar years? We tentatively conclude that the answer to both questions is no....

No later than 30 days from the date of this Order, ALLTEL Kentucky shall file one of the following: (a) An argument in support of its alleged right to adjust its rates pursuant to the KRS 278.516 procedure for small telephone utilities and an argument in support of a small telephone utility's alleged right to calculate an increase under KRS 278.516 based upon the percentage increase in a sub-category of the GDP rather than the percentage increase of the GDP as a whole; or (b) A notice stating that its petition to increase rates pursuant to KRS 278.516 shall be withdrawn....In the event that ALLTEL Kentucky does not file in support of its petition to increase rates pursuant to KRS 278.516...the tentative findings and conclusions contained herein shall become final.

At ALLTEL Kentucky's request, in its subsequent Order dated July 2, 2004, the Commission granted an extension of the filing date to August 2, 2004.

**ALLTEL KENTUCKY'S CONTINUES TO BE REGULATED PURSUANT TO  
K.R.S. §278.516**

As noted previously, ALLTEL Kentucky's intrastate operations have been regulated under the intrastate Alt. Reg. Statute since October 13, 1998.<sup>1</sup> The Commission recognized that election on December 30, 1998 and found that after reviewing ALLTEL Kentucky's filing, "it complies with the requirements of the statute."

Contrary to the Commission's tentative conclusions reached in this proceeding, ALLTEL Kentucky continues to operate and be regulated under K.R.S. §278.516 ("the Alt. Reg. Statute") because ALLTEL Kentucky clearly satisfied the statutory definition at the time of its election in 1998 and because K.R.S. §278.516(7) only provides for termination of the election by ALLTEL Kentucky's Board of Directors.

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<sup>1</sup> ALLTEL Kentucky is an incumbent local exchange carrier ("ILEC") serving approximately 27,700 access lines in the Zoneton, Mt. Washington, and Shepherdsville exchanges. ALLTEL Kentucky is required to comply with the Commission's service quality standards applicable generally to other ILECs and, as of the date of this filing, has received only about twenty-three Commission consumer complaints since 2000.

The Commission's orders in this proceeding ask whether ALLTEL Kentucky may "*still be defined* as a 'small telephone utility' pursuant to KRS 278.516(2) such that the alternate regulation provisions of the statute *still* apply to it." (Emphasis supplied.) This focus on whether the conditional requirements are being met today rather than at the time of election is incorrect. In K.R.S. §278.516, the Kentucky Legislature only established a procedure whereby companies wishing to elect under the plan need satisfy the requirements *at the time of election*. It is undisputed that ALLTEL Kentucky satisfied the requirements at the time of its election in October 1998 as evidenced by the Commission's acknowledgement of this fact in its December 1998 order. The Kentucky Legislature did not make any provision for electing companies having to continuously re-qualify or be faced with being ordered to return to ROR regulation.

Significantly, K.R.S. §278.516(7) requires that the decisions to *begin* and *end* being regulated thereunder (as long as the company met the initial test of eligibility at the time of election) rest solely with the board of directors (or other similar governing body) of the electing utility. Specifically, subsection (7) provides as follows:

*A small telephone utility may elect, at any time, to be regulated by the provisions, in their entirety only, of this section by filing a verified resolution of the utility's board of directors, or other governing body, so electing with the commission. An election shall be effective immediately upon filing with the commission and shall remain effective until withdrawn by the filing with the commission of a verified resolution of the small telephone utility's board of directors or other governing body; provided, however, that all resolutions of election or withdrawal shall remain in effect for at least one (1) year from the date of their filing with the commission. A resolution electing to be regulated by the provisions of this section shall mean that the small telephone utility so electing shall be regulated by this section and shall not be regulated by KRS 278.020(1) and 278.300. Nothing in this section, however, shall be construed to alter the applicability of KRS 278.020(3) or 278.030(2) to small telephone utilities electing to be regulated by the provisions of this section.*

(Emphasis supplied.) The Legislature did not also exclude application of K.R.S. §278.020(4) which pertains to acquisitions and transfers of control, nor did the Legislature provide that, given those circumstances, an electing company would have to re-qualify under the Alt. Reg. Statute.

In short, ALLTEL Kentucky's election remains effective until its Board of Directors determines that the election should be withdrawn and the Board's verified resolution to that effect is filed with the Commission. As noted above, ALLTEL Kentucky's Board has not so acted. Nevertheless, all affected parties should participate in an informal conference to discuss the Commission's concern (expressed in its June Order) about whether ALLTEL Kentucky should continue to be regulated under the Alt. Reg. Statute.

### **GDP INDEX**

In its June 1, 2004 Order, the Commission also requested that ALLTEL Kentucky explain how it may increase its rates based on the annual percentage changes of a sub-category of the gross domestic product ("GDP") given that the statute prescribes that the increase permitted under KRS 278.516(3) is "not to exceed the sum of the annual percentage changes in the GDP for the immediately preceding two (2) calendar years." The Alt. Reg. Statute is silent as to which particular price index an electing company is to use and instead only provides for use of "the GDP." ALLTEL Kentucky located the GDP price indexes on the National Income and Product Accounts Table located at [www.bea.doc.gov](http://www.bea.doc.gov). From that table, ALLTEL Kentucky selected the GDP for "Personal Consumption - Services" because that category was the most representative of ALLTEL Kentucky's business. (The other categories were durable goods and nondurable goods.)

ALLTEL Kentucky selected the GDP price index that was most indicative of ALLTEL Kentucky's business product.

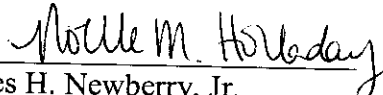
### **CONCLUSION**

ALLTEL Kentucky's intrastate operations have been regulated under the Alt. Reg. Statute for almost six years. At the time of its election in 1998, ALLTEL Kentucky satisfied the requirements to elect under the statutory plan as acknowledged by the Commission. The Kentucky Legislature provided that electing companies like ALLTEL Kentucky may continue operating under K.R.S. §278.516 until their board of directors decided that withdrawal from the plan is appropriate. Based on the Commission's tentative conclusions, ALLTEL Kentucky is aware that the Commission believes that ALLTEL Kentucky should not continue being regulated under the Alt. Reg. Statute. ALLTEL Kentucky, therefore, requests an opportunity to discuss these matters and proposed solutions with Commission Staff and affected parties in the context of an informal conference.

Dated: July 30, 2004.

Respectfully submitted,

**KENTUCKY ALLTEL, INC.**

By:   
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