

ORAL ARGUMENT – 02/13/02
01-0086
CITIES V. SOUTHWESTERN BELL

CAGLE: The basic scheme of incentive regulation for telephones is a mixture of regulation and competition. A utility elects to freeze its rates and in exchange those frozen rates are not longer subject to review.

This case involves one of three exceptions to incentive regulation. And this exception provides an opportunity for a rate increase for the utility. Now the issue in this case is whether this exception, which is found at section 58.058 of the Public Utility Regulatory Act...

ENOCH: You said that under the new regulations, the particular rates that had been frozen are no longer subject to a reasonableness review. You mean by that to say that where there is a request for recognition that the city of Austin has now moved into this higher category under that previously frozen rate that that is subject to a reasonableness rate review?

CAGLE: Yes.

ENOCH: So you agree with Southwestern Bell that what the PUC did here was they did consider the reasonableness of the overall revenue, reasonableness of the rate, and your argument is that they are permitted to do that under the statute that they were operating under?

CAGLE: No. What the commission performed in this hearing was they looked at the reasonableness of the request. They did not look at Bell's overall revenues. A rate group reclassification is a term of art that describes a procedure that the commission has been performing for a long time.

O'NEILL: What's the purpose of the rate group reclassification?

CAGLE: It has two purposes.

O'NEILL: One of them directly impacts revenue. It's hard for me to divorce those two concepts and say one is not related to another.

CAGLE: It absolutely impacts revenue. And the other piece of it though is that it's to ensure that the rates are spread equitably across the different - I'm going to say population sizes just because that's sort of an easy term for the sizes of the exchange access arrangements.

HECHT: I don't understand that part. Why is it equitable - I understand the argument is always throughout these briefs, we shouldn't put Austin in with Ft. Worth and San Antonio, but then you're keeping it in with smaller cities. The same way with Dallas. We shouldn't put them in

with Houston, but then you're keeping it in with cities that are much, much smaller. So I don't understand why if the equity argument only ratchets one way.

CAGLE: That goes back to the initial strict structure when the legislature said we want to have rate group reclassifications be performed and the rate groups that Bell's customers have been placed in.

HECHT: Right. In 1983 the PUC thought this structure was a good idea. And at the time they thought it was a good idea that a city that had more than 400,000 EAA should go in group 6. Now they don't think that.

CAGLE: Right.

HECHT: Well why is that?

CAGLE: Because what they've tried to do is essentially each of the top four groups has one major metropolitan area in it. Eight is Houston; Seven is Dallas, Six is Ft. Worth; then we get down to five which looks at Austin.

HECHT: San Antonio is in the third one I guess.

CAGLE: San Antonio is just above Austin. But I guess the other point of that is that that goes to more an abuse of discretion point perhaps that that initial rate group structure might perhaps you know it sounds to me like your question goes to the initial rate group structure, which is actually not the issue that's before the court.

HECHT: Well no. My problem is they say we have got to do this because the arguments of the four petitioners are that this has got to be done, because otherwise a terrible inequity will result, the rates will be completely unreasonable, the legislature could never have intended that, this will completely thwart the transition to competition, and, therefore, it's absolutely essential. But then as I look at the chart, I think well you're not doing anything different than what could have been done in 1983. We're just trying to keep the what revenues the same, or what?

CAGLE: No. Actually the revenues didn't stay the same. They went up. I think what the commission is trying to do is first off provide a reasonable interpretation of the statute. Since it omitted technical term of art and did not include a definition, the commission looked to what has it done in the past when it performed rate group reclassifications.

ENOCH: Here's a reference to Sprint here. So I will use this as an example. Does Sprint have the same rate band that Southwestern Bell has? Are the numbers exactly the same in the rate band?

CAGLE: No. Each rate band was done according to utilities.

ENOCH: So this utility, as a part of its tariff, it doesn't say - the tariff says nothing about Austin will be charged X rate. The tariff says that if you're in a population center, access lines, of this amount or less, the rate for that will be charged.

CAGLE: Yes.

ENOCH: Now you begin by saying that under the election the rates are frozen. So why isn't what the PUC did for all the reasons that you say that while this is not a rate change, this isn't anything else, but they are affecting the rate tariff that was frozen by the election. How do they not affect the frozen rate tariff by going in and taking the rate bands that set the rate and changing those rate bands, so that a different tariff now gets charged?

CAGLE: They do. The first three words of 15.058 are notwithstanding subchapter B. Subchapter B contains several provisions, but the two main parts that it contains are: first, the provision that rates are frozen. The legislature and the commission both agree that rates can go up as a result of this.

ENOCH: So that goes to your argument that they are not restricted to looking at the reasonableness of the rates since that's in subchapter B, and this being excluded?

CAGLE: I guess I need to finish my answer to that one because the commission didn't look at the reasonableness of the rates. They looked at the reasonableness of this particular change. And the only two things that this did is not...

ENOCH: If I change that rate band, I am changing the rates.

CAGLE: Actually what the commission did was keep two of the 52 groups of customers in the same rate band. So actually the difference that...

ENOCH: No they didn't, because the charge is not based on the city of Austin. The charge is based on access lines of 500,000 or 400,000, and so what they did is they took some customers that had 500,000 access lines that should be charged X rate, and they moved the line so that a different rate now applies to them.

CAGLE: Actually the record in this case, Bell came in and they filed an application to move 52 exchanges, and that application shows what the exchange access lines were of each of those 52 exchanges. And it also shows where those exchanges were prior to the application. Of those exchanges, the only two exchanges that moved differently under the commission's ruling - actually that don't move are Austin and Dallas.

ENOCH: But Austin and Dallas are not referenced in the rate bands. What got changes is customers who have access lines of a certain amount are now put in a different rate structure than they were at the time the rates were frozen.

CAGLE: And I guess that's what I am saying. When a company like Southwestern Bell comes in and petitions for this type of reclassification, they petition to move particular exchanges. And that's why I say they do actually reference these specific exchanges.

The first three words of 58.058 are notwithstanding subchapter B. Subchapter is where the prohibition is that says the commission can't hold hearings and look at reasonableness.

HECHT: If the company is right about the mandatory nature of .058, then notwithstanding chapter B doesn't matter?

CAGLE: Actually that's not the commission's position. Because rate group reclassification - the question is what is mandatory. And the commission's position is that what is mandatory is a rate group reclassification of the same type that the commission had performed in the past.

HECHT: I understand that. But if you lose on that, and if the company is right about the mandatory nature of the rate group reclassification without adjusting the boundaries, then notwithstanding phrase doesn't matter?

CAGLE: It becomes superfluous.

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BOYLE: I would like to follow up on Justice Enoch's question about the reasonableness review. Because the section that is quoted and referenced, 58.025, is reference for the purpose that what we're doing with rate group reclassification is doing this reasonableness review.

If you will look at 58.025, it has four elements to it. And it says there's a reasonableness review of the company's rates, its overall revenues, its return on invested capital, and its net income. So let's take those elements. Review of net income is the entire net income. It's the company's net income. It's not a piece or a part or looking at it in a one rate type situation. It's the entire company. By the same token when you're looking at return on invested capital and that's what we used to have rate of return regulation before incentive regulation, you looked at the return on invested capital, the entire rate base or invested capital of the company. If you're looking at overall revenues, you are trying to make a determination by looking at all the costs, all the expenses, the reasonableness of them, whether they are necessary are not, you're looking at the reasonableness of the company's revenues. By the same token here it's important to note is the reasonableness of the company's rates. And what you're doing when you put that in context, that's looking at all of the company's rates. What 58.025 did in no uncertain terms was prevent anyone from coming in and saying, we need to review whether you need a rate decrease, or whether we need to look at a revenue requirement review. That is what it was about. And you can see those terms are very specific and you will find all of them. If you will look at 53.051, and look at subchapter B of chapter 53, all those

terms are contained there. Now they don't use the term "company's rates". They say the "public utility's rates." But you're putting all those at issue.

This is not a rate freeze here. It's a rate cap. So you have a rate cap on the one hand. They've taken care of that. That's in 58.054. And you have another situation in 58.055 where the company reduce its rates on its own application under certain circumstances. So you've taken care of that situation. The only situation you've left out there not covered, and that's what 58.025, is someone other than the company by complaint or otherwise comes in to reduce the company's rates. And traditionally that was called the §42.

ENOCH: Can I reduce if the tariff sets the rate for 500,000 access lines, and the PUC comes in and says we're now going to say that you can only charge that if it's got 600,000 access lines, however, does the PUC effectively reduce the rate of the utility under the guys of kind of being reasonable on who ought to be in these bands?

BOYLE: I don't think so. I mean the commission doesn't have the authority. It's shall allow for growth. And you can't move them down I don't think in any rate group. But historically, and that's what we had in the handout, which shows the history of how this works.

BAKER: As she said at the outset, each one of these units has at its top a metropolitan area. And you just said the PUC can't move them down. But when that top unit gets more access lines, it's supposed to be in the next higher group isn't it?

BOYLE: Yes.

BAKER: So if you move the level up haven't you basically under those facts moved that city down and reduced the rates?

BOYLE: In my opinion no. They are not moving from the rate group that they have. Now it's true, the boundary has changed and they stay in the same rate group. But what you are recognizing is what rate group reclassification is by definition. It's a value of service concept. If I can give one hypothetical: if you take the argument of the company that rates must be frozen, that's the argument - this is ministerial and they must be frozen - the boundaries I mean. If the boundaries must be frozen then you can have San Antonio, for example, move in to rate group 8, and Houston be 500,000 more access lines, but you've got radically different value of service. And what the commission...

HECHT: Why is that? I don't understand that.

BOYLE: Because that's the whole concept of rate group reclassification.

HECHT: When they set these bands in 1983, they thought this is a good way to do it. This is based on value. But then when the population changes they say, well it wasn't really based

on that. What we really want is somebody in the top group and somebody in the next group, but that just smacks of being revenue _____.

BOYLE: If you look at the orange sheet on the handout, you can see exactly the history of how this works. You were trying to do value of service. Someone that had 500,000 less access lines was not getting the same value. And that's what the groups were all about. And that is the concept. And one final word about that that cuts into it. We moved over to incentive rate regulation. Rate design or designing rates did not die. And you will see in the handout on the blue page many of the exceptions. All of these exceptions require rate design. Requires who is going to pay what. And whether residential is going to pay so much or business is going to pay so much or liken to there's a GTE rate rebalancing exception, whether local or long distance. All of those things. Whenever rate changes, you still have to go through that exercise. And it is a discretionary exercise.

HECHT: Did Sprint settle and was unopposed because there wasn't a lot of money involved?

BOYLE: I was not involved so I can't really say what happened there. I don't know. It was a black box settlement so I have no idea what was in there or what was going on.

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RESPONDENT

HEARON: This is simply a statutory construction case. The statutes here seem to be remarkably clear. Under 58.025(a), the commission cannot review the rates of Southwestern Bell for reasonableness. It didn't stop there. It went ahead and said under any circumstances.

The commission here is attempting to play on words saying, well we're not reviewing the rates. We are reviewing the rate bands that set the rates. But the rate bands themselves are a rate. And the case is as simple as that. By changing the rate bands they are changing the rates. Now Mr. Boyle tries to make the argument that well it says rates plural. But as Justice Baker points out, when you change the rates the overall income returns whatever of Southwestern Bell is reduced, because you have reduced the rates by elevating the rate boundaries and keeping a city in a lower category than it would be if because it had over 400,000 access lines it paid slightly more.

HECHT: The argument is as I try to piece it together, that this is a transition to competition from which utilities ought to benefit by becoming more efficient and giving the public a better service and add some initiative to do that more than they had before, and we should encourage that rather than a utility just benefitting from the fact that lots of people are moving to Texas.

HEARON: Mr. Boyle has argued that point throughout, but the legislature did two things in 1995. First, they said as to basic network services, which this is local service, we're going to cap the rate. But those rates can be increased, 58.055, under three circumstances, one of which is 58.058.

Now there are lots of issues before the legislature in PURA 95 about how this system would work. And that issue was resolved in favor of an electing company. If you elect, you didn't have to, a part of the legislative bargain was that you could not increase any of your rates except for growth.

HECHT: Did everybody elect?

HEARON: I don't know. Now you add to that the fact that in PURA 95 there are a whole bundle of services that are essentially deregulated. This is not like necessarily some other state where the FCC, for what's now called competitive services, are essentially deregulated. There is no cap, no limit on what can or can't be charged. Furthermore, we now have even as the basic local services competition. The market is open. The PUC has decided that it's wide open. So it's not just a question of whether there is some idea about being able to earn more money by being efficient. Of course, that's always the case. The question here is whether what the legislature said would be the rules can be changed by the commission.

Now for some reason this commission doesn't like rate group reclassification due to growth. And from the beginning has thought up every argument you can imagine to defeat it. They said, well some of this growth must be due to marketing. So we will exclude that. The DC said that was wrong. The CA said they were wrong also for excluding growth that occurred during a prior rate settlement. Now the only issue...

BAKER: Did y'all give up on that?

HEARON: No we won on that.

BAKER: No. On the prior one that came on in your favor. That's not an issue today is it?

HEARON: That's not an issue today. My point is, that the only remaining barrier that the commission has thrown in face of the legislature's direction that it shall allow a rate group reclassification due to growth is this idea that they can change the rate boundaries. And the point at the very beginning I think as Justice Enoch made very clearly, the brackets themselves are the rates. The PUC can no more change those rate brackets to prevent a city from moving into a higher category than the IRS could change the tax brackets to keep a taxpayer from having to pay more money. It's as simple as that.

PHILLIPS: What's the process by which changed all this back in the 1970's and 1980's? Now my tax bracket is set by legislation.

HEARON: That's right. But that's no longer the case. In PURA 95, the legislature decided that it would cap the rates at the existing level. I've got a bunch of statutes in the handout, but I don't have time to go through all of them. But in reading them, you will see that an electing company is to charge the rates in effect when it elected in 1995. The legislature said, okay we're not

going to have any more rate cases, we're not going to have any ability to change those rates, and at least to basic network services Southwestern Bell, an electing company has to charge those rates.

The point is, that the legislature has taken over the task of determining when rate brackets need to be changed. The legislature has done that as to switched access charges for use of the local network by interexchange carriers. The court may recall from another recent case, the legislature actually itself changed the rates for switched access. And the point of that here is that if the commission has a complaint they need to go to the legislature and say these rate brackets need to be changed, or you need to give us the authority to change those rate brackets.

The legislature is monitoring this in every session. And the statutes prescribed in a couple of case that the commission is supposed to give a report to the legislature as to biannually as to how this is working, whether there are problems, whether there are recommendations, so the legislature can address it.

What has happened here is that the legislature has withdrawn from the commission any rate setting/rate approval powers.

HECHT: In your view the commission's sole responsibility when this reclassification is requested is to look over the numbers and make sure that the EAA's have been figured correctly?

HEARON: I'm not sure that's all. I think that the commission has a meaningful role. It's not automatic. It's not anything the company can do on its own. It has to file a report just like the tariff says. You certainly have to recount the lines just like you can have arguments about the census. You can decide what access lines there are. Right now there are thousands of access lines that are operated by competitors. Should those be counted or not? The whole hearing here before the commission was devoted not to changing the boundaries, that didn't even come up, but into hearing arguments, questions about how should the access lines be counted? Do payphones count? Does a computer modem count? It's not automatic. It does have a meaningful role. But under 58.059, that role is circular. It simply comes back to the question of whether there is growth in access lines that moves a city from a 400,000 category to a 500,000 or 600,000 category.

ENOCH: The role in evaluating the request that comes from the utility is predicated on this statement that notwithstanding subchapter B, which has the restriction on the PUC in evaluating reasonableness of the rates - I mean I understand the CA thought it produced absurd results and then the PUC comes in and says the opposite. Do it the other way and produce absurd results. Is it an answer to say well that phrase doesn't amount to anything because the balance of the phrase just says this is mandatory?

HEARON: Well, that's one answer. The balance says it's mandatory. But looking at notwithstanding itself, what the commission is doing is misusing that word. That word in the dictionary means despite or nevertheless. And what is subchapter B? Subchapter B is captioned Election of Incentive Regulation. So when you look at it it says notwithstanding the fact that

Southwestern Bell has elected incentive regulation and agreed to cap its rates. The commission shall allow a rate group reclassification due to growth. That is a very strained argument that the commission is making that notwithstanding wipes out all of section B. It wipes out the election process. It wipes out all the subheadings and in effect would repeal an important section, subchapter of PURA 95 or of the utility's code.

And in fact the parties are in agreement here that no substantive change was intended by this codification. Of course that's what the legislature said. And if you look at the prior PURA 95 language it expressly says notwithstanding the commitments in a particular section, which is the one where when Southwestern Bell elected incentive regulation it committed not to seek any rate increases.

HECHT: But we said in Fleming Foods you've got to go by the words. They don't seem to like that.

HEARON: But Fleming is distinguishable because as you also said in Fleming, if you can't reconcile it, you have to go by there. But here there is a clear way to read both sections, both the code and the pre-code the same way. And I don't understand the commission to be making any contrary argument.

I do want to point out one point that the commission raised in its reply brief for the first time: Continuing this effort to think up new reasons why the legislature's direction that a rate group reclassification shall be allowed can nevertheless be denied. That's an argument that in the old Southwestern Bell tariff, there was reference to how those proceedings, those proceedings to move cities into a higher or lower bracket were subject to §43(a), an old section 43(a). That section is now 55.004 of the code. And if you will look in Tab 1 under §58.052, the second section that's laid out there, this says that the basic network services will be regulated in accordance with this chapter - chapter 58, second to the extent not inconsistent with this chapter in accordance with other things. And of course, general rate making provisions whatever are in fact inconsistent with specific provisions in ch. 58. But you will note down there it says, and I highlighted it after ch. 55, except for 55.004, which used to be 43(a). So everybody at the PUC recognized that old 43(a) has nothing to do with this. It's been accepted by the legislature in this statute, and indeed as we also show here in the handouts, the PUC itself after the hearing in this case approved a revision of the tariff that took out any reference to 43(a), and simply replaced it by saying these proceedings will be governed by 58.058.

The arguments against this continue. How much easier it would have been if like Sprint this application had been granted shortly after it was filed in Dec. 1997.

HECHT: I take it since you were complaining about the lack of discovery below, you don't know about Sprint either?

HEARON: We couldn't find out about it. That's right. The CA held against us on that

point. We didn't present it here because to us the important issue is to get this statutory question resolved that the commission does not have the power to subvert a legislative direction by changing the boundaries. Now also we are entitled to a remand in an effort somehow to try to recompense Southwestern Bell for not having these revenues that it would have been entitled to receive.

O'NEILL: And how is that some how? You say somehow for them to be recompensed...

HEARON: Well we will have to wait and see what happens at the remand if that is what occurs. Right now there is a competition in the local exchange market as I mentioned. Exactly how that remand will work will be something that the company and the commission and the parties will have to work out. It's not a matter before the court now. It's unfortunate that it has taken so long to get this issue resolved when initially the monthly changes are minor: 25 cents, 50 cents a month residence, \$_____ for business.

O'NEILL: Well you're talking about \$40 million a year. Is that right?

HEARON: I think the number now would be something less than \$40 million a year. Probably \$28 million or so. Significant sum over the years that that might amount to as much as \$100 million.

BAKER: Do you say that because time has passed?

HEARON: Time has passed.

BAKER: So now since those years have passed if you had started today you would only be asking for \$28 million?

HEARON: No, no. I think what's happened is that through the application of some of these other exceptions or errors that the commission made, that they are going to have to be straightened out, that the \$28 million number is tied to what we're talking about here - the changes in the rate group boundaries.

But however that works out, the important point is for this court we submit to disavow these arguments of technical meaning. The statute says a rate group reclassification due to access line growth, which obviously means not a rate group reclassification due to changing the boundaries. It also means that this rate group reclassification has to be allowed notwithstanding subchapter b, because subchapter b is the election that otherwise would have prevented(?) it.

It also means that the procedural provisions of §59 simply give the commission the meaningful role to determine whether access line growth has occurred, but not the right to trump the shall allow direction that has been given.

The legislature here is the entity that is monitoring, receiving reports and if

it believes that the bracket should be changed, there was some argument earlier that well suppose everybody moves to Houston and it becomes tremendously large, shouldn't the rate brackets be changed. Perhaps so, but not by the commission. That would be to go back to the legislature and say look give us the right to do this because of what's happened in Houston.

Now I've shown in Tab 6 the particular rate decrease that occurs here. Down at the bottom of that page it shows the two charts. The chart at the top of the page is how the rates used to be. That is the brackets and then the rates for each of the brackets. The second chart shows in boldface the changes to the brackets that the PUC made and the corresponding changes in the rates, because the rates are tied to the brackets. And then the rate effect of that in Austin and in Houston.

So there is no question but that we have here a violation of 58.025(a), that the commission shall not under any circumstances review the existing rates for reasonableness. They have done that. They've changed them. There's a violation of 58.058, which is an exception to Southwestern Bell's agreement and when it elected incentive regulation not to seek a rate increase, and the court we submit should affirm the opinion of the CA reversing the commission on this point.

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REBUTTAL

CAGLE: I would like to begin with Southwestern Bell's first point about their most important issue here is to disavow the term rate group reclassification because the term the legislature included in the statute is rate group reclassification due to access line growth.

The problem with that argument is that the legislature included this term for the first time in 1995. Prior to that every rate group reclassification has involved access line growth. So for them to say rate group reclassification due to access line growth does not by any extent change the definition. And that also takes me to 3.2(?) the point about if you keep Austin in the same rate boundary isn't that in effect lowering the rate. I guess what I would like to point out is that the commission does this: adjust the boundaries when the exchange lines are growing at a similar rate. So what they're doing is preserving the distinction that existed initially. If you've got a city and Austin for example is one that at least in the past has been considered for this is growing at a rate much faster than the other cities. Then that city might move up to the next rate group. But that otherwise what they're doing is the population is growing pretty consistently and they're trying to preserve those distinctions among differently sized populations.

BAKER: And where does that authority come from?

CAGLE: That authority comes from the history of rate group reclassification. But that's what that term has always meant. And when the legislature incorporated that term of art that's why they did it.

ENOCH: But that is simply something that was created by the PUC to help them figure out how to set rates isn't it?

CAGLE: Yes.

ENOCH: It is arbitrary that Houston is in one deal and Dallas is in another one. We just can't figure out how to regulate telephone rates anymore efficiently than to say well maybe the person who owns this telephone line if they can reach 500,000 people without having to pay an extra fee instead of 200,000 they ought to pay for that additional _____ since they are not paying long distance. And that's just a kind of a rate setting scheme that the PUC adopts in order to help provide some basis for regulating the telephone industry. So for all of what you said, if they change the rate band it is a ratemaking decision that they are doing isn't it?

CAGLE: First off it was a proceeding that the commission had adopted, but it's also the language that the legislature adopted. When they incorporated this as an exception to incentive regulation, they incorporated - the only history that existed which is what the commission had been doing in the past. But I would also add that...

BAKER: Well do I understand that to mean that these various brackets that the PUC initially devised have now been put into the statute? And the reason why I ask that question that way, your opponent said that the rate bracket changing is a legislative function not a PUC because it's now in the statute.

CAGLE: The problem with that argument that my opponent made is that there is nothing in the statute that supports that. The statute says rate group reclassification where there's access line growth, and a rate group reclassification is adjusting the boundaries. The only way that this procedure can be performed at all...

BAKER: If Austin is in a band that each customer pays - that there's a \$5 rate, but the next bigger band is the \$10 rate, and you move the band to keep Austin at \$5, that's a change in Austin's rate isn't it?

CAGLE: If Austin has never paid \$10 it's perhaps a theoretical change but it's not an actual change. Because what the band's change did was just keep Austin where it was before.

BAKER: So it keeps paying \$5 instead of going up to \$10, which is how Southwestern Bell when you put the whole package together was asking for \$40 million more. And by moving the boundary, you restrict the request for additional revenue. Isn't that right?

CAGLE: Yes.

BAKER: But that also encompasses a rate change.

CAGLE: Yes. In the commission's understanding that's why it's an exception to that entire package.

BAKER: The decision by the PUC to make that decision and keep Austin instead of moving it to where they should be, is that based on what's reasonable under the circumstances?

CAGLE: It was based on what's reasonable and particularly on trying to preserve the distinctions between the different communities as it has in the past.

BAKER: In other words to preserve a distinction between cities but not between rate bands? Do I understand the policy was we're going to have a big metropolitan advisably so in each one of these even though the number gets smaller as you get to fewer access lines? So in the PUC's viewpoint to grant this change was not reasonable so you're going to move the boundary to arrive at a reasonable disposition of the request?

CAGLE: Yes. If I understood the question.

BAKER: Is it right to say that the statute prohibits that conduct? You can't talk about the reasonableness of rates when you're doing a rate band change.

CAGLE: No. Because the rate group reclassification says it's notwithstanding subchapter B. And subchapter B contains two parts. It contains the freeze on the rates, which says you can't raise rates; and it also contains the provision that says the commission can't look at the reasonableness of the rates.

HECHT: Cannot?

CAGLE: Yes. So when the legislature said notwithstanding this subchapter. And they didn't say notwithstanding half of subchapter B. They say notwithstanding subchapter B. Southwestern Bell's _____(interrupted).

BAKER: What is reasonable now is no longer an issue because you can look at it? The inability to look at reasonableness under the second part doesn't apply anymore because it was the host (inaudible).

CAGLE: Yes.

JEFFERSON: Let me ask one question about that. What incentive would the company ever to elect that statutory to mean it was the incentive if and therefore which would imply there's some form of proof of predictability on the rates if _____(inaudible) change those rates through some other means and talks about reclassification or any of the means. Why doesn't that company ever elect to do that.

CAGLE: It has two reasons to elect to do that. The first is, and the commission has said throughout this, this provides an opportunity for a rate increase. Southwestern Bell got a 2 million dollar a year rate increase and the commission has always taken the position that this provision does not mean, um, I guess also going, um, back to Justice Enoch's earlier question, the commission does not believe they can lower rates. They cannot (interrupted).

OWEN: But they can keep them the same. They can keep them from ever marching up in the chain.

CAGLE: And, but that's only if they're being done consistently and they're still getting the revenue. And I guess the second reason is that Wall's tariff requires Bell to file for a rate reclassification and always has anytime they've got this sort of growth. There's a place to come in and those boundaries are supposed to get looked at. The problem is that Bell was remiss and didn't come in for a ten-year period to get those boundaries adjusted and so, I guess that's the second reason, but the first one and the primary one is that they can and do get a rate increase and it's just that that increase is subject to review for reasonableness in light of _____ (cut off).

ENOCH: The only reason they get the rate increase is because you didn't change the boundaries on a couple of those other categories, but you could have. You could have stopped the entire rate increase by just changing the boundaries in all the categories.

CAGLE: I'm afraid that's a hypothetical that I can't say what the commission would have done.

ENOCH: But PUC's view is they could have.

CAGLE: Yes, except that it would be rare to see everyone moving completely at the same rate, would be my guess, but what I guess is most important for the _____ (inaudible) is that the commission took the position in this case that Southwestern Bell was entitled to a rate increase and they did so (interrupted).

OWEN: Inaudible – they can smooth the banners and keep everybody where they are indefinitely.

CAGLE: That's one option, but that's not what they did in this case.

PHILLIPS: Any other questions? Thank you. That concludes today's arguments.