

## Why the PSC Should Reject Verizon's Attempt to Deregulate Basic Phone Service in Maryland

**History:** Most states have a government agency that regulates public utilities (i.e. telephone and electricity companies) because these utilities are de facto monopolies without market competition to keep prices fair and service acceptable. In Maryland, basic telephone service (i.e., simple local and long distance calling) is regulated by the Maryland Public Service Commission (PSC).

For decades, the PSC has granted Verizon a de facto monopoly (and guaranteed profits) to provide basic telephone service to Marylanders in exchange for Verizon charging customers reasonable rates and maintaining minimum levels of service quality. For most of its history, Verizon has been solely a telephone company providing only basic phone service through old-fashioned copper wires.

But now Verizon also offers cell phone service as well as “bundled services” of basic phone and/or cable television and/or internet access through advanced “fiber optic system” (or FIOS). Basic phone service remains regulated by the PSC because Verizon's ownership of the copper lines makes it a de facto monopoly in the many jurisdictions in Maryland where copper lines are the only affordable way to get basic phone service. By contrast, the PSC does not regulate Verizon's cell phone business because Verizon must compete for customers against Sprint and other companies. And the PSC does not regulate Verizon's bundled services offered through FIOS because Verizon must compete in that market against cable companies (which deliver these services via cable) and wireless companies such as DirecTV.

Millions of Maryland consumers – especially in poor and rural areas not serviced with FIOS -- only receive (or can only afford) basic phone service through copper wires and therefore rely on the PSC to regulate this part of Verizon's business. In doing so, the PSC finds year after year that Verizon woefully fails to meet service quality requirements set forth by the PSC. Over the past few years, the PSC has launched numerous cases (investigations) into Verizon's failure to restore service to customers – sometimes for weeks on end -- yet according to Verizon's own documentation service quality continues to deteriorate.

Verizon's shifting of manpower and resources away from its regulated basic telephone service into its unregulated FIOS network is a major reason for deteriorating service for basic phone customers. Verizon does so because it believes it can make more money selling bundled service through FIOS than it can make selling basic phone service through copper. In essence, Verizon treats the guaranteed profits flowing from the regulated part of its company as a cash cow to finance construction of a FIOS network. This represents a violation of Verizon's agreement with the PSC by which it gets the privilege of receiving monopolist and guaranteed profits for basic phone service in exchange for decent service.

**Problem:** Verizon argues that because some customers get phone service as part of “bundled services” from unregulated cable companies, basic phone service via copper should also be deregulated. This argument is false because:

1. Verizon competes against unregulated companies to provide bundled services. Verizon also has a huge and captive market in Maryland of millions of customers – most of them poor, many of them rural – who only get basic phone service via copper. PSC regulation of monopolist Verizon guarantees the company makes a good profit in this huge and captive market.
2. The part of Verizon's company that offers basic phone via copper is and should remain totally separate from the unregulated parts (e.g., cell phones, FIOS). Each part has a different way to

make a profit because as long as there are poor Marylanders and Marylanders without access to FIOS, there will be a big market for basic phone service via copper. In exchange for monopolist control of this market and guaranteed profits, Verizon should not be allowed to treat it as a cash cow to neglect and from which to suck money to finance FIOS investment.

If the PSC agrees to deregulate basic phone service, millions of low-income, elderly and rural Marylanders will be at the mercy of monopolist Verizon. Given Verizon's documented and deplorable record of service quality, there is every reason to believe the monopolist will gouge customers and neglect service.

But deregulate is exactly what Verizon proposes. In December of 2008, Verizon submitted a proposal (called a "settlement offer") to the PSC to dismiss the many cases lodged against Verizon for poor service. Verizon's settlement offer proposed a mere \$4 million in reimbursement credits for the thousands of customers who experience service outages or missed service appointments in exchange for deregulating basic telephone service in Maryland and allowing Verizon to raise monthly rates by \$1 for the first three years and another \$12 a year thereafter.

The PSC rightly rejected this settlement offer in March of 2009 for the following basic reasons:

- The \$4 million in credits offered by Verizon was not nearly sufficient to compel the company to improve its service quality because the settlement offer would allow Verizon to raise its rates by \$11 million.
- The PSC ruled Verizon must meet its service quality requirements for at least a year before the PSC would consider any price increases.
- Most importantly, the PSC ruled that there is not nearly enough competition in the copper basic phone service market to justify deregulation at this time.

Upon rejection by the PSC, Verizon lobbied the Maryland General Assembly to enact by legislation the provisions of the settlement offer, but lawmakers rightly rejected the legislation.

But Verizon just won't quit. In August of 2009, Verizon went back to the PSC with a slightly revised offer. Now Verizon offers to increase the possible reimbursement credits from a derisory \$4 million to a still insulting \$6 million. Worse, the company says it is now willing to make price increases dependent upon the company's meeting for one year a service quality benchmark lower than the current benchmark.

Not surprisingly, Marylanders – many thousands of whom have firsthand experience with Verizon's lousy service – oppose deregulating basic phone service by a huge 67% - 14% margin (with 19% undecided), according to a September 2009 Gonzales statewide poll.

**Solution:** The PSC should side with regular Marylanders and reject Verizon's latest insulting offer.

The PSC should:

1. Rule out deregulating basic phone service any time soon because there is no sign of a competitive market for this service.
2. Require that reimbursement credits paid by Verizon to customers for faulty service at least mirror the price increases that Verizon requests.
3. Stipulate that Verizon meet service quality every year in order to be eligible to hike rates every year.
4. Compel Verizon to address the PSC's concern that Verizon is withholding sufficient funds for copper network maintenance and additional technicians.

In essence, Verizon's current Settlement Offer to the PSC is exactly the same as its insulting March offer – except now Verizon is willing to add a mere \$2 million more in fines it is willing to pay if it fails to maintain its copper network for basic phone service customers. This extra \$2 million is a drop in the bucket compared to the monopolist super-profits Verizon would reap if the PSC agrees to deregulate basic phone service in our state. For this reason and given Verizon's documented history of poor maintenance and service for customers, the PSC should not deregulate prices for basic telephone service.