

anti-competitive or discriminatory practices or behavior by CMRS providers in California;<sup>31</sup>

- Evidence, information, and analysis demonstrating with particularity instances of systematic unjust and unreasonable rates, or rates that are unjust or unreasonably discriminatory imposed upon CMRS subscribers. Evidence of a pattern of such rates that demonstrates the inability of the CMRS marketplace in California to produce reasonable rates through competitive forces will be considered to be especially probative;<sup>32</sup> and
- Rate information for each CMRS provider, including trends in each provider's rates during the most recent annual period.<sup>33</sup>

In addition, the CPUC submitted no public evidence on two of the issues most crucial to its Petition.

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31 Section 20.13(a)(2)(vi) of the Commission's Rules. Although AirTouch and the public do not know what is contained in the confidential materials submitted by the CPUC to the FCC, those materials presumably do not meet the Commission's requirement that they be supported by an affidavit from a person having personal knowledge. Furthermore, as discussed above, any reliance upon such confidential, non-public materials would be a violation of the APA and otherwise unlawful. AirTouch denies that it has engaged in any anti-competitive or discriminatory practices or conduct.

32 Section 20.13(a)(2)(vii) of the Commission's Rules. The CPUC's failure even to allege that cellular rates have ever been unjust or unreasonable (because the CPUC was required, under state law, to find that they were just and reasonable), together with its failure to allege that there has been a pattern of such improper rates, must itself be "considered especially probative" that the CPUC cannot produce such evidence.

33 See Section 20.13(2)(2)(iii) of the Commission's Rules (emphasis added). Although the CPUC provided some public information on this topic, its failure to evaluate the data accurately and to recognize the substantial rate reductions that have occurred renders its rate information unreliable and legally inadequate. As AirTouch has demonstrated, its rates (except in Sacramento, which the CPUC admits are already among the lowest in the country), have been decreasing substantially and will almost certainly continue to decline if the CPUC's Petition is denied.

- The number of customers of each CMRS provider and the trends in each provider's customer base during the most recent annual period;<sup>34</sup> and
- Customer satisfaction with cellular service.<sup>35</sup>

The CPUC undoubtedly had discretion to decide what evidence it would submit in support of its Petition. However, its utter failure to present complete, public evidence on the majority of issues that this Commission considers pertinent to its decision makes it virtually impossible to reach a reasoned decision, or to allow the public notice and comment required under this Commission's rules. The CPUC's omission of this essential information, coupled with its failure to provide a detailed description of its proposed regulatory scheme, makes summary dismissal of the Petition necessary.

### **III. THE CPUC HAS IMPROPERLY ADOPTED A NEW REGULATORY SCHEME WHICH CONFLICTS WITH FEDERAL STANDARDS.**

The CPUC's plea for continued regulatory authority must be rejected on its face. To the extent it can be discerned, it appears the CPUC's regulation includes:

- the retention of the existing rate band regulations;
- future adjustments to the rate caps under the existing regulations, including potentially rate of return regulation;

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34 See Section 20.13(2)(2)(ii) of the Commission's Rules. Although AirTouch does not know whether the customer information submitted by the CPUC is accurate, it is plainly incomplete as it provides no information regarding other CMRS providers, including Nextel.

35 Section 20.13(a)(2)(vii) of the Commission's Rules. It is undisputed that customers are in fact quite satisfied with cellular service. See Section IV.B.5 infra.

- the creation of two tiers of regulation for wireless competitors--one tier with onerous conditions for cellular carriers and one tier without constraints for new entrants; and
- new requirements to unbundle cellular service at the wholesale level to allow interconnection with a reseller switch.<sup>36</sup>

The CPUC has adopted regulations that are beyond its authority and, if implemented, will frustrate the goals of Congress and the Commission for the wireless marketplace.

The CPUC is improperly attempting to impose new rate regulation prior to receiving authorization from this Commission. That new regulation appears to require physical interconnection requirements affecting interstate calls which is plainly preempted under Section 2(a) of the Communications Act and potentially may conflict with this Commission's jurisdiction over interconnection requirements generally.<sup>37</sup>

Additionally, the CPUC's existing regulation and the new regulation will significantly frustrate the goals of Congress and this Commission. The CPUC not only intends to violate the federal mandate for parity with its two-tiered scheme, it seeks unfettered authority from the Commission to institute whatever regulation it sees fit, including cost-based/rate-of-return regulation unheard of in any other state in the country. There can be no conceivable market condition that warrants granting the CPUC boundless discretion to implement regulation out of sync with the rest of the nation. The Commission can, without

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36 D.94-08-022 (mimeo) at 74-75, 80-84.

37 47 U.S.C. § 152(a).

further consideration, summarily deny the Petition on this basis.

A. The CPUC does not have the authority to enforce its unbundling and interconnection orders pending disposition of its Petition.

The CPUC's failure to describe in detail its proposed regulatory scheme, including unbundling of wholesale rates and forced interconnection of reseller switches, is no oversight by the CPUC. These elements of the CPUC's proposed regulatory scheme are not part of the CPUC's historical regulatory framework. They were instead imposed in a CPUC decision adopted on August 3, 1994, only days before the CPUC filed its Petition. Even if this Commission does not dismiss the CPUC's Petition, it should not allow the CPUC to enforce its new regulatory scheme during the pendency of its Petition.

Section 332(c)(3) creates two categories of petitions for regulatory authority over CMRS rates. Those states that have never imposed rate regulation on CMRS providers and those states that want to modify their regulations after June 1, 1993 may petition for authority to impose such new or modified rate regulation under Section 332(c)(3)(A). States that had CMRS regulations in effect on June 1, 1993 may petition for authority "to continue exercising authority over such rates" (emphasis added) under Section 332(c)(3)(B). A state that files a petition under subsection (B) must make the same showing as a state that files a petition under subsection (A), but is granted additional limited authority to continue its "existing regulation" that had been in effect as of June 1, 1993 until

this Commission acts on the state's petition. The CPUC's Petition filed pursuant to Section 332(c)(3)(B), gives it limited authority to continue enforcing its "existing regulation" as of June 1, 1993 while this Commission considers the CPUC's Petition.

The CPUC's Petition states that it seeks to "retain its existing regulatory authority . . . over the rates for cellular service within California."<sup>38</sup> This statement misleadingly implies that the CPUC wishes simply to continue regulating those aspects of cellular service that it was regulating as of June 1, 1993. In fact, however, the most important parts of the regulatory scheme the CPUC seeks to impose--including the requirement that cellular carriers unbundle their wholesale rates and that they interconnect to a reseller switch<sup>39</sup>--are not part of California's "existing regulation." Those requirements were imposed upon the cellular carriers in a CPUC decision adopted on August 3, 1994. The CPUC's attempt to use the mechanism of a petition under Section 332(c)(3)(B) to evade preemption of its newly-imposed regulations is plainly invalid.

Section 332(c)(3)(B) specifically prohibits the CPUC's attempt to evade federal preemption pending disposition of its Petition. Under that provision, states are permitted only to enforce their "existing regulation" during the pendency of their FCC petitions.<sup>40</sup> The CPUC's August 3 decision, imposing new

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38 Petition at 1 (emphasis added).

39 Petition at 81-82.

40 47 U.S.C. § 332(c)(3)(B) (emphasis added).

rates for new segregated services that the carriers have never offered before, is plainly contrary to the statute.

In imposing these new regulations, the CPUC contended that Section 332(c)(3)(B) broadly preserves its "authority to regulate," rather than its "specific rules in effect" as of the statutory cut-off date.<sup>41</sup> This construction, however, cannot be squared with the actual statutory language. The statute does not refer to a state's "regulatory authority," but rather only to the state's "existing regulation" in effect as of June 1, 1993. The CPUC's interpretation simply and unlawfully reads the words "existing regulation" out of the statute.

While the CPUC could, consistent with Sections 332(c)(3)(A) and (B), propose new rate regulations not in effect as of June 1, 1993 to take effect after this Commission granted its Petition, the CPUC chose not to do so. Instead, it hastily imposed new rate regulations just before filing its Petition, then sought authority to "retain" its existing regulatory structure without informing this Commission that its proposal involves regulation that was not in effect as of June 1, 1993. In effect, the CPUC is unlawfully attempting to enforce its proposed regulatory scheme before this Commission has granted it permission to do so. Such actions cannot be condoned.

**B. The CPUC's interconnection order is preempted not only by Section 332, but by Section 2(a) as well.**

The CPUC's attempt to impose new rate regulation during the pendency of its Petition is not the only aspect of its Petition

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41 D.94-08-022 (mimeo) at 82.

that may intrude upon this Commission's exclusive authority. The Petition also states that it has required cellular carriers to interconnect their central switches with "reseller switches" operated by competitors.<sup>42</sup> While the CPUC notes that it believes that "[t]he reseller switch will not interfere with any of the 'unitary' functions performed by the cellular carrier's MTSO,"<sup>43</sup> the CPUC fails to mention that its interconnection order does not distinguish between intrastate and interstate calls, and apparently requires interconnection of all calls.<sup>44</sup> To the extent that the CPUC seeks authority to require interconnection of interstate calls, it is plainly preempted under Section 2(a) of the Communication Act. 47 U.S.C. § 152(a).

Moreover, even if the CPUC's interconnection order were interpreted as requiring only interconnection of intrastate calls, its proposal might unlawfully thwart or impede federal policy. While this Commission has not yet explicitly preempted state regulation of intrastate interconnection arrangements among CMRS providers, it has recognized that, because of the inseparable nature of the physical plant used in interconnection, it has authority to do so.<sup>45</sup> This Commission

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42 Petition at 82-83.

43 Petition at 82.

44 D.94-08-022 (mimeo) at 82.

45 Equal Access NPRM, ¶¶ 142-43. Apparently, recognizing that no state had in effect rate regulation for such interconnection arrangements as of June 1, 1993, the Commission has determined that "[w]ith respect to state jurisdiction over the intrastate  
(continued...)

has also invited public comment on the question whether it should "preempt any state from imposing [any interconnection] obligations."<sup>46</sup>

C. The CPUC's existing and proposed regulation will undermine federal goals.

Even if the CPUC had submitted its proposed rules, the Petition must be rejected. Congress has established the goals that regulation should "enhance competition and advance a seamless national network" of wireless services and should "foster the growth and development of [such] services[, which], by their nature, operate without regard to state lines as an integral part of the national telecommunications infrastructure."<sup>47</sup> Congress sought to ensure that the Commission would "establish a symmetrical regulatory structure that will promote competition in the mobile services marketplace and will thus serve the interests of consumers while also benefiting the national economy."<sup>48</sup> Even if the CPUC had submitted the requisite rules, the proposed regulation must be rejected.<sup>49</sup> A key factor in making these goals a reality is

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45(...continued)  
interconnection rates charged by CMRS providers, the CMRS Second Report determined that the Budget Act preempts any state regulation of CMRS interconnection rates." (Id. at ¶ 143) (emphasis added).

46 Id. at ¶ 142.

47 H.R.Rep. No. 111, 103d Cong., 1st Sess. 259-261 (1993).

48 Second Report and Order at 1418.

49 Congress' decision to require regulatory parity between previously rate regulated cellular carriers and unregulated service providers such as ESMRs was made especially clear not  
(continued...)

uniformity of regulation among all types of providers of mobile wireless services.<sup>50</sup> The CPUC's Petition to extend and augment its regulation of cellular carriers is flatly at odds with these federal goals.

The CPUC's unbundling directive, imposed solely on cellular carriers, and not on new head-to-head competitors, creates the very type of disparate regulatory burden that Congress sought to eliminate. The "reseller switch" and the corresponding "unbundling" of the wholesale tariff is simply another attempt by the resellers to resurrect the concept of cost based rates that previously was rejected by the CPUC.<sup>51</sup> The resellers have consistently maintained that the reseller switch will not

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49(...continued)  
only by the direct effect of amended Section 332, but also by the legislative history. In that legislative history, Congress stated that it expected the Commission to ensure that "consistent with the public interest [] similar services are accorded similar regulatory treatment." Conference Report at 494. This fundamental policy determination was underscored by the statement in the House Report that, in reviewing any state rate petition, "the Commission also be mindful of the Committee's desire to give the policies embodied in Section 332[] an adequate opportunity to yield the benefits of increased competition and subscriber choice anticipated by the Committee." H.R. Rep. No. 111, 103d Cong., 1st Sess. at 261 (1993). In response, the Commission has recognized that its job is "to implement the congressional intent of creating regulatory symmetry among similar mobile services" such as cellular, ESMR, and PCS. Second Report and Order at 1413.

50 Because "the disparities in the current regulatory scheme could impede the continued growth and development of commercial mobile services," the fundamental objective of Congress' creation of these new classifications was to ensure that "similar services are accorded similar regulatory treatment." H.R. Conf. Rep. 103-213, 103rd Cong., 1st Sess. 494 (1993), 1993 U.S.Code Cong. & Ad. News 1088 ("Conference Report").

51 See D.90-06-025 (mimeo) at 105 (Conclusion of Law 23); see also Petition at 82-83.

survive without cost-based/rate-of-return regulation. Indeed, the resellers admitted their switch could only make "economic and competitive sense" if cost based regulation is imposed.<sup>52</sup> In other words, absent a regulatorily imposed subsidy to inefficient competitors, the proposal has no merit.<sup>53</sup> Yet, the CPUC has ordered "unbundling" of the wholesale tariff based on capped rates. Despite the lack of evidence supporting such a policy, and the absence of any specifications on actual implementation, the CPUC concludes that competition will somehow be enhanced. But unbundling based on capped "market" rates is merely the first step. The CPUC has indicated its intention to consider cost based regulation,<sup>54</sup> despite its prior conclusion that such regulation would be catastrophic for cellular service. Indeed, the CPUC has rejected such regulation even for local

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52 See Cellular Service Inc.'s Phase II Opening Comments in CPUC I.88-11-040, dated August 11, 1989, at 1.

As demonstrated in I.88-11-040, the actual costs avoided by the carrier switch are very small or perhaps nonexistent when the additional engineering cost to reconfigure its system to accommodate the reseller switch are considered. In order to offset the inefficiencies of the reseller switch, the resellers were forced to advocate cost based rate of return regulation. See Testimony of Charles King in I.88-11-040 (Ex. W-7) at 11-12; Opening Comments and Workshop Proposals of Cellular Service, Inc. in I.88-11-040, dated December 17, 1990, at 5-8; Workshop Summary and Comments of Cellular Service, Inc. in I.88-11-040, dated March 22, 1991, at 3, 18.

53 In fact, the CPUC does not even know if interconnection of the reseller switch can be accomplished. It acknowledges that there are, "technical uncertainties" about the nature of the functions that reseller switches may be capable of performing. D.94-08-022 (mimeo) at 94 (Finding of Fact 53).

54 I.93-12-007 (mimeo) at 2-23; D.94-08-022 (mimeo) at 69-70; Petition at 19-20; but, see the concurring, plurality opinion of Commissioner Knight submitted herewith as Appendix D.

monopoly exchange carriers. The fact that the CPUC is considering such regulation calls into question its ability to provide the symmetrical regulatory framework conducive to the competition that Congress sought to encourage.<sup>55</sup>

**IV. THE CPUC'S PETITION MUST BE DENIED ON THE MERITS BECAUSE THE CPUC HAS NOT MET ITS BURDEN OF PROOF.**

**A. The CPUC has not shown that there are conditions unique to California that fail to protect subscribers.**

Congress recognized in 1993 that the distinction between virtually unregulated "private" mobile radio services ("PMRS") and traditionally regulated common carrier services ("CMRS") was outmoded and anti-competitive.<sup>56</sup> Accordingly, Congress decided to

"replace[] traditional regulation of mobile services with an approach that brings all mobile service providers under a comprehensive, consistent regulatory framework and gives the Commission flexibility to establish appropriate levels of regulation for mobile radio service providers."<sup>57</sup>

To implement this fundamental change in the regulatory framework and to ensure consistent regulation, Congress preempted state

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55 D.90-06-025 (mimeo) at 58-60, 93-94 (Findings of Facts 17-18), 100 (Finding of Fact 90).

56 Despite the similarities and competitive relationship between cellular carriers and ESMR providers, Congress and the Commission both recognized that there was a significant difference in their regulatory treatment. Most notably, because ESMR providers were classified as "private carriers" while cellular carriers were considered to be "common carriers," ESMR providers such as Nextel were not subject to rate regulation or tariffing requirements at either the federal or state level while competing cellular carriers were subject to such regulatory burdens. Second Report and Order at 1415.

57 Second Report and Order at 1418.

regulation of entry and rates for both CMRS and PMRS providers.<sup>58</sup>

Congress permitted only a limited exception to its universal preemption of state regulation of rates and entry. A state could continue existing regulation or impose new regulation only where the state could prove that the "market conditions" will "fail to protect subscribers adequately."<sup>59</sup>

"States must, consistent with the statute, clear substantial hurdles if they seek to continue or initiate rate regulation of CMRS providers."<sup>60</sup> Similarly, the Commission has stated that "we have vigorously implemented the preemption provisions of the Budget Act to ensure that state rate regulation of CMRS providers will be established only in the case of demonstrated market conditions in which competitive forces are not adequately protecting the interests of CMRS subscribers."<sup>61</sup> As even NARUC has admitted, states seeking to continue rate regulation face a "stiff" burden of proof.<sup>62</sup>

The CPUC has not met this "stiff" burden. The Petition presents no evidence that there are unusual or unique market conditions in California which "fail" to protect subscribers

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58 Section 332(c)(3) of the Communications Act.

59 Id.

60 Second Report and Order at 1421 (emphasis added). See Sections 20.13(a)(5) and (b)(1) of the Commission's Rules.

61 Second Report and Order at 1419 (emphasis added).

62 "Petition for Reconsideration and Clarification of the National Association for Regulatory Utility Commissions," Gen. Docket No. 93-252, filed May 19, 1994, at 3.

adequately from unjust or unreasonable rates.<sup>63</sup> To the contrary, aside from the CPUC's counterproductive regulation, California's market conditions are particularly conducive to competition. California's favorable cellular demographics have attracted the first new facilities-based cellular competitors. Nextel has now instituted cellular-type service throughout much of California.<sup>64</sup> California is also likely to have facilities-based PCS competition sooner than virtually anywhere else in the country. Cox has been granted a pioneer's preference for the enormous Southern California MTA and has indicated its intention to utilize its existing infrastructure and begin operations as soon as possible. California is also unique in that its largest local exchange carrier, Pacific Bell, is no longer affiliated with a cellular carrier and is therefore eligible to obtain 30 MHz PCS licenses in its service areas. The competitive advantages of combining PCS and wireline services can be substantial.<sup>65</sup> Indeed, Pacific Telesis Group has already established a new subsidiary, Pacific Bell Mobile Services (PacBell Mobile) whose announced mission is "to win the PCS

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63 The CPUC previously made the same argument to the FCC "that adequate competition does not exist in California in order to ensure just, reasonable and nondiscriminatory rates." See "Comments of the People of the State of California and the Public Utilities Commission of the State of California" (Docket No. 93-252) filed on November 4, 1993 at 6. The FCC rejected the CPUC's arguments then and they must be rejected now. Second Report and Order at 1478-80. Any other outcome would be unlawfully inconsistent. See, e.g., Green County Mobilephone, Inc. v. FCC, 765 F.2d 235, 238 (D.C. Cir. 1985).

64 See pp. 31-37, infra.

65 See Affidavit of Professor Jerry A. Hausman ("Hausman Affidavit") submitted herewith as Appendix E, at ¶ 44.

licenses and provide a full array of telecommunications services to our customers."<sup>66</sup> PacBell Mobile plans to resell cellular services in California in preparation for providing PCS, and is soliciting bids for the construction of its facilities.<sup>67</sup>

As a result of these developments, cellular carriers in California now face more facilities-based competition than anywhere else in the country--as well as the certainty that more, very substantial PCS competition is right around the corner.<sup>68</sup> Far from being a market that needs special regulation to protect consumers from a lack of competition, California will lead the way to the multi-competitor wireless market envisioned by the federal regulatory reform.

The CPUC ignores these market realities and instead rests its case for continued regulation on four central "findings":

- that the "government-created duopoly structure" of the cellular industry, together with interlocking ownership interests among various cellular carriers, have permitted cellular carriers to "price their services at non-competitive levels and to earn returns above competitive levels"<sup>69</sup>;

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66 See Communications Daily, dated August 19, 1994, at 4.

67 Id.

68 This fact has been recognized by the State of California who has told the United States District Court for the District of Columbia that both of the two California MTAs "will soon be served by PCS suppliers in competition with existing cellular operators." "Comments of Amicus State of California in Support of Motion of Bell Companies for Modification of Section II of Decree," filed August 9, 1994 in U.S. v. Western Electric Co., Civ. No. 82-0192 (HHG) ("MFJ Brief of California").

69 Petition at 7.

- that there is insufficient "competitive pressure" from ESMR and PCS service providers to "check prices and earnings" of cellular carriers<sup>70</sup>;
- that "[p]rices of wholesale cellular carriers in California are among the highest in the nation," have remained "strikingly similar" in particular markets, and "have not significantly declined" during the past ten years<sup>71</sup>; and
- that cellular carrier earnings are "well above" those found in "competitive markets" and "cannot be explained completely by spectrum scarcity value."<sup>72</sup>

There are extensive factual errors contained within the CPUC's analysis supporting its "findings," which are addressed at pp. 28-41. But even if true, the "findings" do not make the required showing of a failure of competition unique to the California market. The "findings" basically track the effects of the Commission's historical duopoly structure for cellular which have been predicted and recognized from the inception of cellular service,<sup>73</sup> and which were clearly known to the Congress when deciding to preempt state regulation.<sup>74</sup> These "findings" would apply equally or with greater force to other cellular markets around the nation:

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70 Ibid.

71 Ibid.

72 Ibid.

73 See, e.g., An Inquiry Into the Use of the Bands 825-845 MHz and 870-890 MHz for Cellular Communication Systems, 78 F.C.C. 2d 984, 991 (1980); 86 F.C.C. 2d 469, 474-477 (1981). The CPUC was also aware of the economic consequences of a duopoly structure. See CPUC Order Instituting Investigation (I.88-11-040), dated November 23, 1988, at 11-12.

74 See, e.g., Hearings Before the Subcommittee on Telecommunications and Finance on H.R. 707 (Emerging Telecommunications Technologies), Feb. 4, 1993 and April 22, 1993.

- The duopoly market structure and pattern of interlocking ownership is no different in California than other states.<sup>75</sup>
- Whatever competitive pressure has been brought to bear to "check price and earnings" of cellular carriers by ESMR and PCS service providers, that pressure has been most effective in California, the only state where entry has already occurred. The competitive pressure has been more, not less, effective in California.
- California cellular rates have followed a pattern similar to rates in other benchmark regulated markets.<sup>76</sup> They have declined in like fashion, and the level of California rates, adjusted for demographics, is in line with other regulated markets.
- The CPUC has not and cannot establish that the rates of return in California are any different than rates of return in other cellular markets.

In sum, the CPUC's quarrel with cellular's historical duopoly structure, now remedied by federal action, cannot support continued state regulation. Far from needing special protection, California's cellular markets will likely lead the way to open and expanded competition. Continued state regulation can only impede that future.

**B. The CPUC's flawed analysis does not support its "findings" regarding market competition.**

As a result of its preconceptions regarding cellular service, the CPUC has presented an "analysis" of competition in the wireless market which is, as with its past regulation, fundamentally flawed. The CPUC's analysis does not support its "findings" that market conditions in California are not sufficiently competitive to protect consumers. The CPUC is clearly frustrated that its regulation of cellular has not

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75 Hausman Affidavit at ¶ 17.

76 Id. at ¶ 18.

fulfilled its own expectation for price volatility and price declines in California. However, the reason for the CPUC's failure to achieve its expectation is not lack of competition by the carriers. The failure is the CPUC's erroneous expectations compounded by misguided regulation. The CPUC has been expecting a duopoly to behave like a perfectly competitive market with no barriers to entry. Instead, the California cellular markets have exhibited all the indicia of intense competition in a concentrated market. The price and supply characteristics of the California markets are completely congruent with other benchmark cellular markets. The CPUC has continually misread this competitive dynamic as a market failure, and has then proceeded to impose counterproductive regulatory structures. The CPUC's actions have restricted avenues for competition and raised prices for consumers.

The CPUC now compounds this error by refusing to acknowledge the changing nature of the marketplace. The CPUC continues to cite historical barriers to entry despite the entrance of Nextel in California and imminent entry of PCS. Additionally, the CPUC relies on an obsolete view of the retail marketplace, totally ignoring the emergence of additional competitors, such as major retail chains, which are gradually replacing the resellers because they are a more efficient form of distribution. Despite its recognition of "deep changes to the competitive aspects of the industry,"<sup>77</sup> the CPUC has made simplistic assumptions regarding market share, prices for

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77 D.93-05-069 (mimeo) at 12-13 (Ordering ¶ 3(b)).

cellular service, and carriers earnings which are not supported by actual market conditions.

1. The CPUC's plea for continued regulatory intervention is principally based on a nonexistent "bottleneck".

The CPUC's central argument is that continued regulation is warranted because the duopoly structure has created a "bottleneck" which has "greatly limited competition."<sup>78</sup> In making this argument, the CPUC has ignored explicit findings that cellular is not a bottleneck by other authorities charged with cellular oversight, specifically this Commission,<sup>79</sup> and the MFJ Decree Court.<sup>80</sup>

This claim is also contradicted by the CPUC's own finding in 1990 that: "[i]n the cellular industry, there is no bottleneck . . . ."<sup>81</sup> Since 1990, the notion of any bottleneck has only become even more improbable.<sup>82</sup> As the State of

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78 Petition at 10.

79 "CMRS providers do not have control over bottleneck facilities." Second Report and Order at 1499. See also "Cellular operating companies do not possess a monopoly of bottleneck facilities; each will be competing against a nonwireline carrier. . . ." (Cellular CPE NPRM, 1984 FCC LEXIS 2461, CC Dkt. No. 84-637, FCC 84-271 (released June 26, 1984)).

80 The "cellular systems at issue do not constitute bottleneck monopolies." August 25, 1994 Opinion of Judge Greene at 17.

81 D.90-06-025 (mimeo) at 59.

82 There is no evidence of refusals to deal by a monopolist controlling an "essential facility" or to multiple providers acting in concert to control such a facility. See City of Malden, Mo. v. Union Electric Co., 887 F.2d 157, 160 (8th Cir. 1989); 82MCI Communications v. American Telephone and Telegraph Co., 708 F.2d 1081, 1132 (7th Cir. 1983), cert. denied, 464 U.S. 791 (1983). Cellular service is not an essential facility. The CPUC has concluded that cellular service is "discretionary,"

(continued...)

California recognized in a recent submission to the MFJ Court: "[c]ompetition between wireless suppliers generally exists at several levels, including basic airtime charges, calling area scopes, long distance charges and the quality of the service provided."<sup>83</sup>

Finally, under the CPUC's own definition, adopted especially for this proceeding, cellular service cannot constitute a "bottleneck." The CPUC asserts that a "bottleneck" arises when another firm "cannot duplicate the service."<sup>84</sup> Since the inception of cellular service there have been two carriers providing separate wireless networks. The recent entry of the third carrier (Nextel) and imminent entry of Cox and other PCS providers makes the "bottleneck" theory not only inapplicable but harmful as an analytic framework.

2. The CPUC relies upon an obsolete definition of the market which is contrary to its own findings and actual market conditions.

The CPUC has limited its market definition to cellular service, resulting in an erroneous analysis which ignores the new competition that has arrived in California. The CPUC's choice to ignore new competition and instead to construct a restrictive submarket limited only to cellular service, is flatly at odds with the approach called for in the Merger

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82(...continued)  
providing a mode of communications complementary to wireline service which provides the essential means of communication. D.90-06-025 (mimeo) at 7, 18, 99.

83 MFJ Brief of California at 3.

84 Petition at 26.

Guidelines which the CPUC allegedly relies upon.<sup>85</sup> The choice is also contradicted by other CPUC findings: "Carriers face competition not only from direct rivals but from providers of alternative telecommunications services,<sup>86</sup> . . . . "Emerging technologies such as PCS and ESMR services . . . [are] most likely candidates for substitution with cellular service."<sup>87</sup> Inexplicably, the CPUC rejects its own findings--and those of Congress--by excluding ESMR and PCS from its market definition.<sup>88</sup>

Finally, and most importantly, the CPUC's choice is contradicted by the facts. New wireless service providers are entering the market to challenge cellular service providers. With two cellular providers in each market, one nationwide ESMR provider, and four or more multi-state PCS providers, market competition provides a superior means to "protect" consumers than a regulatory process which will lead to regulatory costs to CMRS providers and actually will decrease competition.

The CPUC incorrectly asserts that "California consumers currently and in the near future will not have access to

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85 I.93-12-007 (mimeo) at 19 (n.17).

86 D.90-06-025 (mimeo) at 99 (Finding of Fact 78).

87 D.94-08-022 (mimeo) at 89 (Finding of Fact 15).

88 The CPUC's claim that the relevant market is limited to cellular service is undermined by the fact it will "entertain applications" from cellular carriers seeking non-dominant status by a showing the carrier controls no more than 25% of all bandwidth, including noncellular bandwidth. D.94-08-022 (mimeo) at 22.

alternatives to cellular service."<sup>89</sup> California already has access to ESMR service, and PCS is imminent. Nextel has been operational in Southern California for some time. In July of this year, Nextel announced commercialization of its wireless communications networks in the San Francisco Bay area and the Sacramento Valley, and will expand service to the rest of California by the end of 1994.<sup>90</sup>

PCS will be available in significantly less time than the five years claimed by the CPUC. The PCS broadband auctions are likely to begin by the end of 1994 allowing significant competition to enter in 1995-1996.<sup>91</sup> Cox Enterprises, with its Pioneer's Preference and existing infrastructure, is positioned to expedite service.

The CPUC, in determining that "[c]urrently, there are no substitutes for cellular service in California,"<sup>92</sup> presents requirements for substitution analysis that have no basis in sound economic theory. The CPUC lists seven characteristics which it believes a substitute for cellular services must

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89 Petition at 63.

90 See Nextel Prospectus, dated February 9, 1994, at 36; Nextel 1994 Annual Report; Nextel press release, dated July 8, 1994; stock analyst report of Paine Webber, dated August 10, 1994; and, report of Morgan Stanley, dated August 8, 1994. See also, Opening Comments of Nextel Communications, Inc. in I.93-12-007, dated February 25, 1994, at iii. The CPUC conveniently ignores Nextel's public statements, and relies upon an informal phone call with Nextel's counsel. Petition at 66.

91 Hausman Affidavit at ¶ 34.

92 Petition at 63.

possess, without offering any support for its definition.<sup>93</sup> In other proceedings, the CPUC has recognized that studying the cross-elasticities of demand is appropriate to measure substitutability of services rather than the arbitrary identification of certain attributes of the services.<sup>94</sup>

Nextel has in fact conducted studies that show customers consider ESMR as a substitute for cellular.<sup>95</sup> Nextel claims its services are "competitive with those offered by cellular mobile telephone providers in terms of quality of service, features offered, pricing of system access and airtime utilization, and capability of subscriber units."<sup>96</sup> Indeed, recent statements by Nextel<sup>97</sup> discuss the superior qualities of ESMR service, including larger geographical areas and seamless roaming arrangements.<sup>98</sup>

Moreover, there is no question that PCS works, and will be able to function quickly in California. The operation of PCS in the U.K. demonstrates that PCS will provide a competitive

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93 Petition at 64-65.

94 See, e.g., D.87-07-017, 24 CPUC 2d 541 at 556 (1987).

95 See, e.g., "Fleet Call Becomes NEXTEL, New Company Name Reflects New Business Designed to Serve Broader Wireless Communications Market," Business Wire, March 24, 1993, at 4.

96 Nextel Prospectus, dated February 9, 1994, at 36.

97 Nextel Presentation Agenda, seminar dated June 8-9, 1994.

98 See, e.g., report of Paine Webber, dated August 10, 1994, at 1; Morgan Stanley analysis, dated August 8, 1994 ("Considering the SMRs as a business providing competition to the existing cellular players, the DOJ has set the stage for approvals of follow-on transactions, including MCI, OneCall, and DialPage."); Hausman Affidavit at ¶ 33.

challenge to cellular service. PCS operates in the 1800 MHz band in the U.K., which is approximately the same frequency band that much of PCS is scheduled to utilize in the U.S.<sup>99</sup> The handsets offered, manufactured by Nokia and Motorola, are virtually identical to the smallest cellular handsets available in the U.S. Thus, PCS will offer convenience with a wider range of functions than are currently offered with cellular service. Since PCS began operation in the U.K. during 1993, cellular prices in the U.K. have decreased by about 20-33%. Thus, PCS will provide increased competition to cellular.

The CPUC erroneously concludes that PCS and ESMR do not represent viable substitutes for cellular service due to a variety of economic obstacles.<sup>100</sup> What the CPUC fails to acknowledge is that the new entrants in the mobile services market are not small, start-up businesses, but well-funded and experienced telecommunications companies. The great success of the narrowband auctions held earlier this year demonstrates that PCS will attract powerful competitors. In addition to Cox, potential entrants into the PCS arena include major telecommunications, cable and multimedia companies such as Pacific Bell, Time Warner Telecommunications, Inc., AT&T, and Viacom International. These are precisely the type of new entrants to which the CPUC refers in noting that potential entrants "will be in a much better position to develop a PCS system if they already have a network in place, as is the case

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99 Hausman Affidavit at ¶ 36.

100 Petition at 71-72.

with LECs, cable television operators, cellular carriers and possibly electric utilities."<sup>101</sup>

Nextel is both extremely well-funded<sup>102</sup> and poised to offer wireless service over a vast network through its ability to weave together its existing communications technologies. Nextel has already accumulated substantial ESMR spectrum in regions throughout the country. Nextel's existing SMR base will allow it to move quickly in building a nationwide digital network. In fact, Nextel recently announced plans to acquire the other two major ESMR providers Dial Page and One-Call.<sup>103</sup> The territory of these three ESMR companies covers almost the entire U.S. allowing Nextel to offer service to approximately 85% of the U.S. in almost every major MSA.<sup>104</sup> With approximately 200 million POPs in its service area when the acquisitions are completed, Nextel's coverage will far exceed that of McCaw with 63 million POPs.<sup>105</sup>

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101 Petition at 72.

102 Nextel has received considerable financial backing from Motorola, Comcast, Northern Telecom, Nippon Telegraph and Telephone and Matsushita, to say nothing of its very successful IPO. Nextel has publicly and repeatedly stated that MCI's decision not to invest in Nextel at this time (apparently caused by issues involving control and dilution between MCI and Nextel's soon to be largest shareholder Motorola) will not effect its roll out of services in California or elsewhere. See, e.g., Land Mobile Radio News, dated September 2, 1994, at 3.

103 Hausman Affidavit at ¶ 33.

104 Ibid.

105 Ibid.

Finally, The CPUC asserts that cellular carriers will have advantages over ESMR and PCS in part because "[c]ellular carriers have had a ten year head start and substantial imbedded infrastructure."<sup>106</sup> The successful entrance of the Block A (nonwireline) cellular carriers into cellular markets undercuts these arguments and demonstrates the ease of market entry.

In addition, while the cellular carriers had to build out relying entirely on projected analysis, the new entrants have the benefit of the actual empirical information regarding capacity and traffic learned from the cellular carriers' experience. The new competitors can recognize and compensate for the cellular carriers' weaknesses, thus reducing their capital expenditures and allowing them to engineer greater quality control.<sup>107</sup> Additionally, the new entrants are not saddled with the costly conversion from analog to digital facing cellular carriers. These competitors are able to develop new digital systems without the costs of retrofitting analog systems.

3. The CPUC's analysis of market share is flawed.

The CPUC, having created an unduly narrow definition of the relevant market, has inevitably made several faulty conclusions

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106 Petition at 74.

107 "ESMR territories can be built to conform to the best regional usage footprint right from the outset, saving time and money and creating a marketing edge in the process." "ESMR Invasion Spreads Across The Country," The RSA Newsletter, dated July 20, 1993, at 6.