

TABLE OF AUTHORITIES

Page(s)

Federal Cases

Brown Shoe Co. v. United States, 370 U.S. 294 (1962)	27
City of Malden, Mo. v. Union Electric Co., 887 F.2d 157 (8th Cir. 1989)	14
Competitive Telecommunications Association v. FCC, 998 F.2d 1058 (D.C. Cir. 1993)	27
Hunt-Wesson Foods, Inc. v. Ragu Foods, Inc., 627 F.2d 919 (9th Cir. 1980), cert. denied, 450 U.S. 921, 101 S.Ct. 1369, 67 L.Ed 348 (1981)	43
MCI Communications v. American Telephone and Telegraph Co., 708 F.2d 1081 (7th Cir. 1983), cert. denied, 464 U.S. 791 (1983)	14
Metro Mobile CTS, Inc. v. New Vector Communications, Inc., 661 F. Supp. 1504 (D. Ariz. 1987)	49
Metro Mobile CTS, Inc. v. New Vector Communications, Inc., 892 F.2d 62 (9th Cir. 1989)	49
People of State of California v. F.C.C., 567 F.2d 84 (D.C. Cir. 1977), cert. denied, 434 U.S. 1010 (1978)	73
Twin Sport Service, Inc. v. Charles O. Finley & Co., 512 F.2d 1264 (9th Cir. 1975)	27
United States v. E.I. DuPont de Nemours & Co., 351 U.S. 377 (1956)	26, 27

FCC Decisions

Bundling of Cellular Customer Premises Equipment and Cellular Service, Report and Order in CC Docket 91-34, 7 F.C.C.R. (1992)	22
Cellular Auxiliary Service Offerings, 3 F.C.C.R. 7033 (1988)	18
Cellular Communications Systems (reconsideration), 89 F.C.C.2d 58 (1982)	71
Cellular Communications Systems, 86 F.C.C.2d 469 (1981)	14, 71, 72
Cellular CPE (Structural Separation of BOCs), 57 R.R.2d 989 (1985)	14
Cellular CPE NPRM, 1984 FCC LEXIS 2461, CC Dkt. No. 84-637, FCC 84-271 (released June 26, 1984)	14
Cellular Interconnection (Declaratory Ruling), 2 F.C.C.R. 2910 (1987)	73
Competitive Common Carrier Services (First Report and Order), 85 F.C.C.2d 1 (1980)	5
Competitive Common Carrier Services (Second Report and Order), 91 F.C.C.2d 59 (1982)	5
"FCC Clears Way for Licensing of PCS; Provides Framework for Competitive Mobile Communication Market," FCC Report No. DC-2564 (February 3, 1994)	2
FCC Public Notice, Prt. No. CL-92-29 (December 11, 1991)	35
FCC Public Notice, Rpt. No. CL-92-62 (March 13, 1992)	35
Personal Communications Services, (Notice of Proposed Rulemaking and Tentative Decision), Gen. Docket No. 90-314, 7 F.C.C.R. 5676 (1992)	4
Personal Communications Services, 8 F.C.C.R. 7700 (1993)	29, 30, 41, 45

CPUC Decisions

D.84-06-113 (15 CPUC 2d 426)	13
D.87-07-017 (24 CPUC 2d 541)	16, 23, 24, 26, 27, 34, 43, 47, 49, 65
D.88-12-091 (30 CPUC 2d 384)	24, 65
D.89-10-031 (33 CPUC 2d 43)	59
D.90-06-025 (mimeo)	4, 8, 9, 14, 18, 22, 49, 50, 53, 57, 59, 61, 64, 74, 77
D.93-02-010 (mimeo)	18, 24, 43, 47, 49, 62, 65
D.93-05-069 (mimeo)	12

Statutes

Communications Act of 1934	
Section 2(a) (47 U.S.C. § 152(a))	73
Section 201	14, 73
Section 202	14
Pub. L. No. 103-66, Title VI, § 6002(a), 107 Stat. 312 (1993)	29

Other Authorities

California Public Utilities Commission's A Report to the Governor, "Enhancing California's Competitive Strength: A Strategy for Telecommunications Infrastructure" (November 1993)	1-3, 5-7, 57, 60-62
Charles River Associates, "An Economic Analysis of Entry by Cellular Operators Into Personal Communications Services", (November 1992)	28
Department of Commerce estimate, 1991 U.S. Industrial Outlook	76
North Carolina Public Utilities Commission Order Regarding Cellular Reseller Regulation and the Regulation of Other Mobile Services, Docket Nos. P-100, Sub. 114; P-100, Sub. 124 (January 31, 1994)	7
Public Service Commission of Maryland, "A Report on Cellular Telephone Service in Maryland,"	

September 1990 7

R. A. Posner, Antitrust Law: An Economic Perspective
(Chicago, IL: The University of Chicago Press, 1976) . . . 22

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A Review and Critique,"
Journal of Economic Perspectives,
Vol. 1, No. 2 (Fall 1987) 22

Cross References to Questions in Appendix A to
the Order Instituting Investigation

<u>Question</u>	<u>Page</u>
1	30-32
2	30-32
3	39-30
4	14-22
6	52-59
7	11-59
8	43-48
9	22-24
10	14-24
11	59-67
13	75-78
14	4-12
15	11-59
16	43-48
22	27-34
24	65-67
26	51
28	4-12
29	4-12
31	67-75
32	67-75
38	35
47	65-67
48	65-67
49	65-67

50 75-78

PacTel Cellular and its affiliates (collectively "PacTel")¹ hereby submits its response to the Order Instituting Investigation on the Commission's Own Motion into Mobile Telephone Service and Wireless Communications ("OII").²

I. INTRODUCTION.

California's wireless telecommunications industry has entered a new era. The accelerating pace of technological change³ and the entrance of multiple new competitors have redefined the wireless telecommunications market. The imminent introduction of digital technology will increase network capacity, enhance the quality of wireless service and permit a proliferation of voice and data services. This change will require heavy investment by cellular carriers to retrofit existing cellular systems in order to keep ahead of growth.

At the same time, Congress and the Federal Communications Commission ("FCC") have eliminated the historic barrier to entry in the two-way mobile telecommunications market, the two facilities-based carrier market structure, allowing multiple competitors to provide cellular-like service such as Enhanced Specialized Mobile Radio Service ("ESMR") and Personal Communications Service ("PCS"). In light of these

1 PacTel Cellular (U-3001-C) is the managing general partner of the Los Angeles SMSA Limited Partnership (U-3003-C) and the Modoc RSA Limited Partnership (U-3032-C), and operates in its own interest in the San Diego market.

2 PacTel responds to the general discussion set forth in the OII and certain questions identified in Appendix A to the OII. PacTel reserves the right to respond to additional questions in its reply comments.

3 "We are dealing with a technology involving social and political change on a scale and at a speed never before experienced by human beings." California Public Utilities Commission's A Report to the Governor, "Enhancing California's Competitive Strength: A Strategy for Telecommunications Infrastructure," November 1993 (hereinafter, "Rprt. to Gov.") at 27 (quoting).

developments, the FCC has recognized the need to "change significantly the way in which mobile services are regulated by replacing a patchwork approach with a systematic approach that creates symmetry in the way providers of similar mobile communications services are regulated."⁴ This Commission must similarly recognize the need for radical change and regulatory parity in California's regulation of wireless service.

California's new regulatory framework for wireless service must enhance, rather than inhibit, the State's competitive advantage. Development of telecommunications is a critical factor in the economic success of California. Rprt. to Gov. at 3. California has the potential to be the largest and most vibrant wireless communications market in the world and to lead the way for the future development of wireless-mobile communications. While the cellular industry has been a bright spot in California's otherwise shrinking economy, that has been despite, not because of, regulation. The major factor inhibiting further development of the cellular market is existing regulation. That regulation has led to higher prices and limited consumer choice, and, unless altered, will derail California's leadership role in the future. California cannot afford to continue on this path.

The Commission's recent Report to the Governor suggested that the Commission is committed to a path of pro-competitive regulatory reform. The Commission declared that it seeks to enhance California's competitive advantage through a plan to "shape policy with the specific intent of expanding private sector opportunities within the state for

4 FCC Release, "FCC Clears Way for Licensing of PCS; Provides Framework for Competitive Mobile Communication Market," Report No. DC-2564, February 3, 1994.

new investment, new businesses and new jobs." Rprt. to Gov. at vi.

Specifically, the Commission seeks to:

- (1) "encourage relentless innovation in the ways advanced telecommunications is provided and used in the state";
- (2) "support a diverse mix of services and products to meet the widely-varying needs of California businesses, individuals and communities"; and
- (3) "increase affordable access to, and with it the value of, telecommunications" Rprt. to Gov. at vii.

The Plan's "success requires that the State work cooperatively with and unleash the private sector to ensure that every Californian is able to access the Information Age." Id. at 2.

In stark contrast, the new OII is proposing, at least for discussion, a program of heavy handed, invasive regulation flatly at odds with the Commission's stated goals. Despite the radical changes in the marketplace and the Commission's goal of enhancing competition, the OII proposes an antiquated form of rate regulation to be imposed on so-called "dominant" competitors. The OII is clearly predicated on erroneous assumptions regarding the wireless marketplace. Its proposal for extensive dominant/nondominant regulation will undermine rather than promote competition and technological innovation. Past experience has shown that California's regulation of the cellular industry has limited competition and has harmed consumers. The effects of the OII's proposal would be particularly perverse now that new competitors are entering the market. A dominant/nondominant classification imposing even more stringent rate regulation on a select group of competitors would only further retard competition and growth. As the Commission noted:

California's immense size and diversity, both of which are positive attributes in the rapidly changing world of telecommunications, also persuade us to counsel against a "command-and-control" telecommunications strategy. Rprt. to Gov. at 10.

The choice of the regulatory framework that meets the Commission's goals and keeps pace with market changes is straightforward. The Commission has indicated that the optimal mobile telecommunications market would have multiple competitors, thus obviating the need for regulation:

Were it our choice, we would license additional carriers to assure the public the full benefits of a well-working competitive industry without a need for substantial regulatory intervention. D.90-06-025 (mimeo) at 5.

* * * * *

[O]ur first preference is to encourage and rely upon effective competition to assure just and reasonable rates for mobile telephone service (footnote omitted). Where it is possible to enhance competition and avoid the imposition of economic regulation or relax such regulation and still provide just, reasonable and fair service to consumers, we will do so. OII at 10.⁵

The Commission must now adopt its "first preference" and rely upon effective competition, instead of regulation. Relaxed regulation is the only regulatory framework that can keep pace with technological and competitive changes in wireless communications and meet the Commission's goal to enhance California's competitive advantage. A relaxed regulatory framework ensuring a level playing field for all wireless service providers, in conjunction with a monitoring program to assess wireless communications competition, will encourage innovation while protecting consumers.

II. EXISTING REGULATION HAS HARMED, RATHER THAN PROTECTED, CONSUMERS. (Appendix A, Questions 14, 28 and 29)

Evidence from other states demonstrates that California consumers pay the penalty of regulation through higher prices and reduced choice.

5 Similarly, the FCC has endorsed competitive markets. See Personal Communications Services, Notice of Proposed Rulemaking and Tentative Decision, Gen. Docket No. 90-314, 7 F.C.C.R. 5676, 5678 (1992) ("In licensing mobile services, the Commission has squarely placed its faith in competitive markets").

Moreover, as the OII itself observes, "The current [California] cellular regulatory framework resembles a regulatory 'crazy quilt' more than a progressive environment for consumer protection and innovation." OII at 14-15. In an inexplicable about face, the OII then proposes a regulatory framework which can only aggravate the inefficiencies of the existing "crazy quilt." The Commission must not miss the opportunity to provide a "progressive environment" by imposing retrograde regulation totally unsuited for the dynamic wireless marketplace.

A. Regulation leads to higher prices for consumers.

Both the FCC⁶ and this Commission have acknowledged that needless efficiency losses inevitably occur as a result of excessive regulation:

"Policies that convey static short-term cost advantages but that unconsciously undermine innovation and dynamism represent the most common and most profound error in government policy toward industry . . . These sorts of policies, and many others that governments have adopted, usually defer, delay or eliminate the perceived need to improve and innovate, or send the wrong signals about where to innovate.'" Rprt. to Gov. at 9 (quoting Porter).

Regulation increases costs for service providers and thus prices for consumers. Direct costs incurred as a result of regulation include administrative, consulting, filing and legal fees. However, it is the long-term costs arising from regulation that have the most detrimental impact. Tariffing requirements slow the deployment of innovative services and undermine programs to increase consumer choice. As the Commission recognizes, "[u]nnecessary government protection and restrictions dampen the prospects that new products will come to market

⁶ See Competitive Common Carrier Services (First Report and Order), 85 F.C.C.2d 1, 5 (1980), citing C.M. Needy, "Regulation-Induced Distortions," 1978; Competitive Common Carrier Services (Second Report and Order), 91 F.C.C.2d 59, 60-61 (1982) (finding that regulatory burdens retard innovation and reduce efficiency).

and that consumers will receive their attendant benefits."⁷ Rprt. to Gov. at 13. Competitors further handicap the competitive process through protests.

An analysis conducted on behalf of PacTel in 1994 confirms that regulation of wholesale cellular rates has led to higher prices for consumers in states that regulate cellular.⁸ The study, based on a survey of the 40 largest cellular markets, shows that regulation has led to higher prices for consumers on the order of five to fifteen percent. Flexible cellular rate plans, lower cellular prices and greater consumer choice are most evident in unregulated states. For example, over the course of a year, one carrier offered an average of 18 plans in regulated markets in California versus 66 plans in unregulated markets outside of the State.⁹ Customers in unregulated states also have the benefit of customized service through customer-specific contracts and innovative offerings such as equipment and service packaging.

Other states have recognized the negative impact that regulation has on competition and price.¹⁰ For example, the North Carolina Public

7 The delays and uncertainties inherent in state regulatory activity threaten future investment in and by cellular companies. Such investment is critical to ensuring development of the telecommunications infrastructure.

8 See also Affidavit of Jerry A. Hausman, United States v. W. Elec. Co., Inc., Civil Action No. 82-0192 at 10 (July 29, 1992) (hereinafter, "Hausman Affidavit") and Statement of Jerry A. Hausman submitted by PacTel Cellular et al. in its Phase II response in I.88-11-040, at 18-19.

9 State Regulation of Cellular Telephone Service, (updated) CTIA Study, June 7, 1993, at section "Eight Ways That State Rate Entry Regulation Hurts Consumers."

10 Cellular service is not regulated at either the wholesale or retail level in 29 states. Fourteen states have partial regulation at the wholesale level, while the retail level is untariffed. Nine states regulate both wholesale and retail; however, no state regulates with
(continued...)

Utilities Commission deregulated cellular service in February 1992 on the basis that:

. . . the Commission concludes that exempting carriers from regulation holds the prospect for even lower prices for North Carolina consumers in the future . . . [E]xempting cellular carriers from regulation . . . will increase the degree of competition. The elimination of the notice and filing requirements for tariff changes and new service offerings will give carriers more freedom to offer special promotion and discounts--in effect--sales and to experiment with different pricing strategies.¹¹ (No. P-100. Sub.114, February 14, 1992 at 10.)

Deregulation has been such a success that the North Carolina Public Utilities Commission has issued an order prohibiting it from petitioning the FCC to retain jurisdiction over cellular service rates.¹²

California cannot afford to ignore what other states have learned. Restrictive regulation will only undermine California's ability to obtain a competitive advantage.

A state gains a competitive advantage when its businesses and other sectors of its economy are more productive than the economy of other states . . . When a state has superior productivity, and consequently a competitive advantage, it attracts business or jobs. . . .

The Commission should remove regulations and streamline procedures which frustrate the attempts of California businesses to receive services from telecommunications providers in a timely manner and in a manner that fits their specific needs. Rprt. to Gov. at 8-9, 55.

10(...continued)

cost of service regulation. PacTel is not aware of any state that has increased regulation in the past five years. Even in states regulating cellular, state regulators allow cellular companies wide discretion in setting prices, discounts and service options. Hausman Affidavit at 7.

11 Similarly, the Public Service Commission of Maryland concluded in September 1990 that regulation of cellular service was not necessary to protect the public. Public Service Commission of Maryland, A Report on Cellular Telephone Service in Maryland, September 1990, at 1-2.

12 North Carolina Public Utilities Commission Order Regarding Cellular Reseller Regulation and the Regulation of Other Mobile Services, Docket Nos. P-100, Sub. 114; P-100, Sub. 124, January 31, 1994, at 5.

In order to meet its goals, California must be a leader in promoting innovation, not a laggard behind other states.

B. California's existing regulation has stifled competition.

The Commission has previously recognized the benefits of competition and pricing flexibility in the cellular industry. See D.90-06-025 at 76. Based on four years of review of the cellular industry, the Commission adopted a regulatory framework for the California cellular industry which relied on market competition as the principal force to set prices and expand service:

"This decision reflects a basic philosophical direction to rely on competitive forces to set prices for cellular service and to promote the most rapid expansion of service and use of new technology that is reasonably possible. . . . We intend to promulgate a flexible and forward-looking regulatory framework that will meet customer needs while accommodating some of the changes that appear likely in the near future."¹³ D.90-06-025 at 3, 5.

However, since D.90-06-025 was entered, the flexibility originally envisioned has been gradually and substantially undercut by the rejection of innovative pricing proposals and creation of an artificial retail markup for resellers. The rejection of these proposals was prompted by protests of competitors,¹⁴ not cellular customers, and thus the options available to consumers decreased.

The erosion of the Commission's original decision to permit pricing flexibility has been accomplished through subsequent decisions and resolutions which include the denial of requests to: (1) reduce rates

13 The Commission expressly recognized that regulation based on market competition maximized the opportunity for technological innovation, reduced rates and increased consumer choice. Id., Findings of Fact 11, 12.

14 "The present regulatory requirement that tariffs must be authorized prior to implementation provides competitors advance notice of business strategy and enable competitors to use the regulatory forum to challenge and delay a competitor's service introduction." D.90-06-025 at 17-18.

for customers who agree to commit to service over an extended term; (2) pass savings on to customers who signed up for service on a reduced commission basis; (3) provide promotional gifts and discounted equipment packaging; and (4) waive activation fees or provide airtime credits by means of temporary tariffs.¹⁵

The review of temporary tariff filings has focused not on reduction of rates, but on protecting a select group of competitors by mandating the resellers' profit margin be incorporated into each rate element. The requirement of an exact corresponding reduction of the rate elements in the retail and wholesale tariffs is a mechanism unknown elsewhere in utility regulation. It serves to stifle innovation on the part of facilities-based cellular carriers by enforcing mimicry in lieu of competition. It creates both an artificially high profit margin and a price umbrella which insulate resellers from true competition. As with interexchange carriers, carriers should offer a simple wholesale rate to resellers and have the opportunity to offer pro-consumer retail price reductions set by the market, not by regulation. Instead, under current regulation, resellers have no incentive to offer their own innovative plans since their price is tied to the carriers' retail offering. Indeed, a review of reseller tariffs reveals few if any retail offerings different from the facilities-based carriers. It is not at all clear what competitive impetus resellers bring to the cellular market, other than by intervention in carrier tariff filings. Despite the Commission's prior conclusion that the retail market is competitive, the mandatory profit margin stands. See D.90-06-025 at 110 (Ordering ¶15).

¹⁵ See, e.g., Resolution T-14607; Resolution T-14392; Resolution T-14608; Resolution T-14621; Resolution T-14990; Resolution T-15037; D.92-02-076.

The cost to consumers has been significant. This unnecessary market interference needs to end.

At the behest of competitors' protests, California regulation has undermined price competition. For example, new market entrants have utilized regulation in an attempt to limit effective competition. A cellular carrier reduced prices in Los Angeles, only to have the price reductions protested by an unregulated ESMR competitor.¹⁶

The Commission has recently recognized, albeit insufficiently, that regulation can impede effective price competition. In issuing the Assigned Commissioner's Ruling dated March 25, 1993, the Commission granted cellular carriers downward pricing flexibility within ratebands. The Commission sought to "test" the "premise" that regulation keeps prices at higher levels in California than under free competition.¹⁷ The results of the test were clear: PacTel and other carriers responded overwhelmingly by offering new value plans and by reducing rates on existing plans.¹⁸

Similarly, the Assigned Commissioner issued a ruling in December 1993, taking further steps "to simplify the existing cellular regulatory framework and to provide the cellular industry an opportunity to demonstrate that price competition does exist in California."¹⁹ The

16 Protest of Fleet Call, Inc. (now known as Nextel) to Advice Letter Nos. 370 and 371 of Los Angeles Cellular Telephone Company.

17 Assigned Commissioner's Ruling in I.88-11-040, March 25, 1993, at 4.

18 See PacTel Cellular ALs 133, 134; Los Angeles SMSA, Ltd. ALs 236, 240; Los Angeles Cellular Telephone Company ALs 373, 375, 420; Bay Area Cellular Telephone Company ALs 205, 231, 233, 233-A, 240; GTE-Mobilenet ALs 199, 213, 231-A, 216, 224, 225, 232, 239; US WEST ALs 115; Sacramento-Valley Limited Partnership ALs 144, 151; GTEM of Santa Barbara ALs 79, 80, 82, 84, 91; Bakersfield CTC ALs 66, 67; Fresno MSA ALs 97, 108, 118, 129, 132, 136 and Fresno CTC ALs 103, 108, 123.

19 Assigned Commissioner's Ruling in I.88-11-040, December 2, 1993, at 2.

ruling eliminates some roadblocks to price competition, but inexplicably leaves others intact, including the gift limitation and the protectionist wholesale/retail margin. There is no justification for the remaining hurdles. Nonetheless, while the ruling remains mired in the regulatory process, carriers are waiting to implement responsive proconsumer offerings.

Until the artificial competitive roadblocks set up in cellular regulation are removed, cellular customers will be deprived of the commonly available benefits of free competition. The ad hoc dismantling of the roadblocks through separate rulings has permitted a modest increase in competitive offerings; however, this approach is clearly not the most efficient method of bringing the benefits of competition to consumers.

Based on the record of past regulation, it is inconceivable that more restrictive regulation, as proposed in the OII, will benefit consumers. In light of the dramatic changes in the wireless market, including increased competition, it would be unwise to maintain, much less increase, the level of regulation. At a minimum, hearings must be held before action is taken to scrutinize the OII's assumption that consumers have benefited from regulation.

III. DOMINANT/NONDOMINANT REGULATION WILL INHIBIT EXISTING AND FUTURE COMPETITION IN THE WIRELESS MARKETPLACE. (Appendix A, Questions 1, 2, 3, 4, 6, 7, 8, 9, 10, 16, 22, 26, 38)

The OII recognizes that the "Commission should only regulate when the benefits of regulation outweigh the costs." OII at 24. Ironically, without any cost-benefit analysis, the OII proposes a dominant/nondominant framework for regulation predicated on faulty assumptions regarding cellular competition and the new wireless market.

The OII asserts that: (1) there is limited competition in the mobile market due to cellular carriers' "control of the radio transmission bottleneck" and (2) cellular carriers have the "ability to control a substantial portion of the mobile market". OII at 15, 17. Based on these unsupported assertions, the OII proposes a strategy for handicapping facilities-based carriers with more stringent regulation just as new competitors are flooding the market.²⁰

These conclusions prejudge the issue without any evidentiary support. The question is whether cellular carriers are operating as competitively as possible given the constraints that have been imposed by spectrum limits and existing regulation. Market experience shows the answer is yes. Moreover, the question must now be asked what the level of competition will be in the wireless telecommunications market of tomorrow. As the Commission has recognized,

. . . we now anticipate a far-reaching redefinition of the cellular market over the next few years. The impending entry of competitive non-cellular alternative carriers into the mobile telephone market will result in deep changes to the competitive aspects of the industry. D.93-05-069 (mimeo), Ordering ¶ 3(b), at 12-13.

In light of the "deep changes to the competitive aspects of the industry," predicating a regulatory framework on a simple assumption regarding the level of competition in the wireless marketplace would be reckless.

The OII's attempt to base a regulatory framework on mere assumptions is at odds with the Commission's own approach to regulation. For

²⁰ Firms would be classified as dominant if they "control important bottlenecks which are essential to providing mobile services to some or all of the public, i.e., they possess significant market power." Id. at 16. Ironically, the Commission will grant nondominant status "routinely" to all new entrants until a market power problem is "conclusively demonstrated." Id. at 16 (n.13).

example, in establishing the dominant/nondominant regulatory structure for interexchange carriers, the Commission held extensive hearings and received evidence on the issue of whether AT&T had market power. Based on the evidence, the Commission found that AT&T had a 95% market share and concluded that meaningful interLATA competition would not occur until the availability of equal access. The Commission found that after equal access allowed equivalent service, mere flexible regulation might be appropriate. D.84-06-113, 15 CPUC 2d 426, 472-473.

Here, the Commission cannot abrogate its duty to establish a regulatory framework based on evidence of actual market conditions, rather than unsupported assertions. Indeed, the need is more compelling here, where no cellular carrier has the market dominance of AT&T, where the wireless market faces more rapid technological and competitive change, and where even the most cursory of examination of actual market conditions reveals that the OII's assumptions regarding both cellular competition and the new wireless market are unfounded.

A. Consumers have benefited from competition between cellular carriers.

The OII makes several faulty assumptions regarding the cellular marketplace: (1) cellular carriers control a bottleneck facility; (2) cellular carriers do not compete effectively; and (3) the cellular market is susceptible to collusive behavior. OII at 14-15. There is no evidence to support these assertions.

1. There is no radio transmission bottleneck.

It is a fundamental error to base a regulatory structure on the assumption that cellular service is a bottleneck. "Bottleneck facility" is a legal and regulatory term referring to refusals to deal by a monopolist controlling an "essential facility" or to multiple providers

acting in concert to control such a facility.²¹ There is no suggestion here of control of any essential facility.

In fact, the Commission has already expressly found that the cellular network is not a bottleneck monopoly facility:

In the cellular industry, there is no bottleneck monopoly, this is a discretionary service, and technological change and service expansion are key issues. By the same principles we are even less interested in conducting traditional rate cases here. D.90-06-025 at 59.

Cellular risk is substantially different from the monopoly telecommunications market . . . Unlike monopoly local exchange telephone companies, cellular carriers have no captive market of monopoly ratepayers. Id. at 99-100 (Findings of Fact 82, 87).

Similarly, the FCC does not characterize cellular as a bottleneck: "cellular operating companies do not possess a monopoly of bottleneck facilities; each will be competing against a nonwireline carrier. . . ." ²² A regulatory program designed to protect against a non-existent bottleneck would be a costly anti-consumer mistake.²³

21 See City of Malden, Mo. v. Union Electric Co., 887 F.2d 157, 160 (8th Cir. 1989); MCI Communications v. American Telephone and Telegraph Co., 708 F.2d 1081, 1132 (7th Cir. 1983), cert. denied, 464 U.S. 791 (1983); "Unclogging the Bottleneck: A New Essential Facility Doctrine," 83 Colum. L.R. 441, 470 (1983).

22 Cellular CPE NPRM, 1984 FCC LEXIS 2461, CC Dkt. No. 84-637, FCC 84-271 (released June 26, 1984). In the order subsequently adopted, the FCC noted that cellular was not a monopoly service, and the BOCs' cellular subsidiaries must "compete with other carriers and resellers who are able to offer 'one stop shopping' for cellular service and CPE . . . Cellular resellers and CPE vendors are not disadvantaged, as non-cellular CPE retailers are, by the presence of a firm that has dominated the CPE market for a number of years." Cellular CPE (Structural Separation of BOCs), 57 R.R.2d 989, 992 (1985).

23 Moreover, price discrimination or access concerns arising from any purported "bottleneck" facilities are eradicated by the carriers' obligations under Sections 201 and 202 of the Communications Act of 1934 to offer just and reasonable service to all requesters in a nondiscriminatory manner. See Cellular Communications Systems, 86 F.C.C.2d 469, 511 (1981) ("Therefore . . . we will condition radio licenses to system operators such that no restrictions on resale and shared use of cellular services will be permitted.")

2. Cellular carriers have competed on the basis of both price and service.

Since the inception of cellular service there have been two carriers providing separate wireless networks allowing for choice of quality, features and price, as well as numerous FCC-mandated resellers. The cellular industry today reflects the characteristics of a competitive market: rapidly increasing volume, declining prices, expanded service offerings and significant technological change.²⁴

The cellular industry has scrambled to meet subscriber demand. Rapid development and deployment of new cellular technology has been necessary to meet that demand and avoid capacity shortages. As a consequence, in the early years PacTel focused on system coverage and research and development of technology to meet demand. During this period, the industry expanded rapidly into multiple channels of distribution: facilities-based carriers, carriers' agents, independent resellers and dealers and other distributors actively participate in the retail market. However, further innovations in distribution has been undermined by regulation, as nationwide distributors have faced the hurdle of reshaping their promotions to meet the requirements of California's regulation.

As the industry has matured, quality and price competition has intensified with carriers offering an increasing number of pricing and product innovations. The empirical evidence to date demonstrates that

24 See Huber, Kellogg and Thorne, The Geodesic Network II: 1993 Report on Competition in the Telephone Industry, at 4.3, 4.22-4.23, 4.129-4.130 ("Competitive performance in radio services is robust, characterized by vigorous technological innovation, rapidly declining price, soaring demand on the consumer side, and frequent new entry among producers."). See also Hausman Affidavit at 7, 9-14 (competitive forces operate in the cellular market as evidenced by a high degree of quality and price competition).

cellular providers compete aggressively, on the basis of price, service and innovative offerings.²⁵ Service prices have declined or remained flat despite a national inflation rate of 40.5% since 1984. Over that same period, the value of the service to customers has increased markedly through expanded geographic coverage and increased product offerings. This competition has become more intense with the emergence of the new competitors. Again, the main factor inhibiting the scope of competition has been regulation.

a. Prices have been driven down by competition.

Recent years have seen increasingly aggressive price competition in California markets resulting in both lower prices and greater consumer choice.²⁶ The overwhelming majority of PacTel customers subscribe to plans which offer a discount off the basic plan. For example, in PacTel's Los Angeles market, customers may choose from 14 different plans. The proportion of PacTel customers subscribing to the basic plan in Los Angeles has declined from 74.3% at the end of 1990 to 38.5% at the end of 1993. In San Diego, the number of customers subscribing to the basic plan declined from 78.8% in 1990 to 42.6% in 1993. The San Francisco market showed a similar decline, 77% on the basic plan in 1990 down to 41% in 1993. Innovative pricing programs have included:

25 The Commission has recognized that the quality of service, changes in prices and the mix of available services are relevant factors in assessing market competition. D.87-07-017, 24 CPUC 2d 541, 546.

26 The Commission should not lose sight of the fact that current wholesale prices are just and reasonable considering the investment of cellular carriers necessary to meet demand and the continued need for substantial investment driven by accelerating technological change. Historically, cellular carriers have invested substantially more than they have recovered. To date, PacTel has invested more than \$750 million in development of its California cellular network. Future cellular expenditures will be influenced by the costs of digital conversion, the rate and timing of capital replacement, new electronics and competition.

- discounts for multiple unit accounts
- lower rates for volume resellers and bulk users
- special rates for occasional and off-peak users
- lower rates for long-term users
- packaged plans that discount air time for minimum usage
- neighborhood and second phone plans
- billing service options
- government rates
- reduced roaming rates
- promotional discounts resulting in free airtime and waiver of activation fees
- discounted emergency preparedness plans

In addition to these discounts, prices have declined as a result of the steady reduction in the costs of owning a cellular phone.²⁷

The cellular industry as a whole in California has reduced prices and offered customers a variety of choices. A study conducted on behalf of the Cellular Carriers Association of California reveals rate decreases for customers in large metropolitan markets of up to approximately 20% between 1988 and 1993. Similarly, by 1993 over 50% of the subscriber in large markets were on discounted rate plans. The only factor inhibiting even deeper discounts is existing regulation.

Cellular service providers must have the flexibility to create new pricing plans to respond to market demand. For example, the Los Angeles cellular market has already responded to the entrance of ESMR, as well as the grant of additional regulatory flexibility. Cellular providers decreased their prices by approximately 17% to 21% in the summer of 1993 for customers who would sign one year contracts.

b. Service quality has improved due to intense competition.

As the Commission recognizes, "price alone is not the only measure of effective competition. Effective competition can also be provided by

²⁷ See "The Cellular Industry on the Move - Part II," Merrill Lynch Telecommunications/Cellular, June 30, 1993, at 1; Hausman Affidavit at 12.

carriers which offer superior service." D.93-02-010 (mimeo) at 43. Despite the decline in prices, cellular customers have benefited from enhanced service quality and an expanding variety of services. Both the FCC and this Commission have concluded that cellular service quality is competitive. ". . . [I]n a competitive market, such as exists in mobile communications services, market forces compel service providers to offer the quality and quantity of products sought by customers."²⁸ "Experience has shown that cellular providers are willing to provide high-quality performance." D. 90-06-025, Finding of Fact 27; see also Ordering ¶33.

The incentive for such willingness is the carriers' desire to keep the customer from switching to a competitor . . . the quality of cellular service in California is good and . . . cellular carriers have a sufficient willingness to continue and to enhance quality cellular service without implementing any additional regulatory goals or policies. D.90-06-025 at 22.

Competition has improved network performance and led to introduction of product innovations.

i. Cellular carriers have enhanced the wireless infrastructure.

Since its inception in 1984, cellular has faced and met an extraordinary demand for service. As a consequence, the carriers have focused on system coverage and research and development of cellular radio technology to expand capacity and improve quality. The continuous development of innovations to enhance system performance demonstrates cellular carriers' commitment to service quality:

- PacTel has invested heavily in innovative cellular system engineering to expand subscriber capacity. Cellular service is currently available to 95% of California's population.

28 Cellular Auxiliary Service Offerings, 3 F.C.C.R. 7033, 7038 (1988). The FCC found that there was no need to establish specific cellular service quality standards for the provision of auxiliary service on cellular systems because competition would assure continued provision of high quality service.

- PacTel has extensively expanded geographic coverage. When service commenced in 1984 in the Los Angeles market, PacTel's coverage extended to 6,235 square miles. Today, service extends to 9,074 square miles. Similarly, the number of cell sites in the Los Angeles market has increased during that same period from 13 to over 470.
- PacTel was the first to introduce overlay/underlay cell sites to further enhance frequency reuse and system capacity. PacTel developed and deployed cell enhancers to provide coverage in difficult terrain areas.
- PacTel was the first cellular carrier to implement the widespread use of antenna downtilt in order to tailor cell coverage areas and to introduce cell site power control in Los Angeles to reduce interference.
- PacTel has designed and constructed microwave networks in Sacramento, San Diego and Los Angeles to interconnect cell sites to the MTSO, enabling PacTel to provide reliable links which can withstand the adverse impact of earthquakes and other natural disasters.
- PacTel has improved the functionality of its service by offering auto access roaming, automatic call hand-off, international direct distance dialing and free public service calls.

In addition, PacTel has continuously measured the performance of its cellular networks, reviewing the quality of voice service, the amount of downtime, the number of "dropped" calls, and the performance of subscriber equipment. When a performance problem is identified, immediate steps are taken to determine the extent of the problem, its effect on the customer and the appropriate course of corrective action.

Technological advances to date have made it possible to expand capacity rapidly enough to meet demand. But continued technological advances are required to meet future demand and to compete with the new wireless providers. The increased need for capacity will require introduction of digital technology which uses existing spectrum more efficiently.

PacTel will invest nearly \$250 million over the next five years to build its Code Division Multiple Access ("CDMA") digital cellular