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Before the  
**FEDERAL COMMUNICATIONS COMMISSION**  
Washington, D.C.

In the Matter of )  
 )  
Petition on Behalf of the State of Hawaii, )  
Public Utility Commission, for Authority )  
To Extend Its Rate Regulation of Commercial )  
Mobile Radio Services in the State of Hawaii )

PR Docket No. 94-103

**REPORT AND ORDER**

**Adopted:** May 4, 1995; **Released:** May 19, 1995

By the Commission:

**I. INTRODUCTION**

1. On August 8, 1994, the Public Utilities Commission of Hawaii (hereinafter "Hawaii" or "HPUC"), on behalf of that state, petitioned us to retain state regulatory authority over the rates for intrastate commercial mobile radio services ("CMRS").<sup>1</sup> Thirteen parties filed pleadings opposing the petition, and one party filed a pleading supporting it.<sup>2</sup> By this action, we deny the petition because it fails to satisfy the statutory standard Congress established for extending state regulatory authority over CMRS rates.

**II. BACKGROUND**

2. In 1993, Congress amended the Communications Act ("Act") to revise fundamentally the statutory system of licensing and regulating wireless (*i.e.*, radio)

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<sup>1</sup> Hawaii Public Utility Commission Petition, on Behalf of the State of Hawaii, for Authority To Extend Its Rate Regulation of Commercial Mobile Radio Services in the State of Hawaii, PR Docket No. 94-103, filed Aug. 8, 1994 ("Hawaii Petition").

<sup>2</sup> A list of parties that filed pleadings in this proceeding appears at Appendix A.

telecommunications services.<sup>3</sup> Among other things, Congress: (1) established new classifications of “commercial” and “private” mobile radio services (“CMRS” and “PMRS,” respectively) in order to enable similar wireless services to be regulated symmetrically in ways that promote marketplace competition;<sup>4</sup> (2) reallocated up to 200 megahertz of spectrum from government to private use so as to expand opportunities for innovative utilization of spectrum by the private sector;<sup>5</sup> and (3) authorized competitive bidding as a means of improving licensing efficiency within the context of the Act’s public interest goals, which include promoting investment in new and innovative wireless telecommunications technologies.<sup>6</sup>

3. Congress also provided that, as of August 10, 1994, no state or local government shall have authority to regulate “the entry of or the rates charged” for CMRS and PMRS services, although states are permitted to regulate the “other terms and conditions” of CMRS.<sup>7</sup> As an exception to this general rule, Congress also provided that, if a State had “any regulation” concerning the rates for any commercial mobile radio service in effect as of June 1, 1993, it could retain its rate regulation authority by petitioning the Commission no later than August 9, 1994, and demonstrating that either: (1) “market conditions with respect to such services fail to protect subscribers adequately from unjust and unreasonable rates or rates that are unjustly or unreasonably discriminatory;” or (2) “such market conditions exist and such service is a replacement for land line telephone exchange service for a substantial portion of the telephone land line exchange service within such State.”<sup>8</sup>

4. In our proceeding to implement OBRA, we concluded that, since Congress intended generally to preempt state and local rate and entry regulation of CMRS, a state

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<sup>3</sup> See Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, Title VI, § 6002 (“OBRA” or “Budget Act”), *codified in principal part at* 47 U.S.C. § 332.

<sup>4</sup> See Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services, Second Report and Order, 9 FCC Rcd 1411, 1417-18 (1994) (*CMRS Second Report and Order*), *reconsideration pending*.

<sup>5</sup> National Telecommunications and Information Administration Organization Act, § 113(b)(1).

<sup>6</sup> The competitive bidding methodology is to promote “the development and rapid deployment of new technologies, products, and services for the benefit of the public, including those residing in rural areas, without administrative or judicial delays ....” 47 U.S.C. § 309(j)(3)(A). Regulations for the conduct of such auctions, when they prescribe area designations and bandwidth assignments, are required by OBRA to promote “investment in and rapid deployment of new technologies and services.” 47 U.S.C. § 309(j)(4)(C)(iii).

<sup>7</sup> See 47 U.S.C. § 332(c)(3)(A).

<sup>8</sup> See 47 U.S.C. § 332(c)(3)(B).

seeking to retain regulatory authority must “clear substantial hurdles” in demonstrating that continued regulation is warranted.<sup>9</sup> We also determined that the nature of a state’s burden of proof is delineated generally by the statute itself. Specifically, we found that:<sup>10</sup>

[I]n implementing the preemption provisions of the new statute, we have provided that states must, consistent with the statute, clear substantial hurdles if they seek to continue or initiate rate regulation of CMRS providers. While we recognize that states have a legitimate interest in protecting the interests of telecommunications users in their jurisdictions, we also believe that competition is a strong protector of these interests and that state regulation in this context could inadvertently become as [*sic*] a burden to the development of this competition. Our preemption rules will help promote investment in the wireless infrastructure by preventing burdensome and unnecessary state regulatory practices that impede our Federal mandate for regulatory parity.

5. We also concluded that, while a state should have discretion to submit whatever evidence it believes is persuasive, a petition to retain regulatory authority must be grounded on demonstrable evidence.<sup>11</sup> In that regard, we adopted Section 20.13 of our Rules as a guide to the kinds of evidence and information that we would consider to be pertinent and helpful to our consideration of a state petition.<sup>12</sup> Moreover, in addition to the evidence, information, and analysis that a state must submit, we determined that a petitioning state also is required to identify and provide a detailed description of the specific existing or proposed rules that it would continue or establish if we were to grant its petition.<sup>13</sup> We noted that the standards for preemption established in *Louisiana PSC* do not apply to petitions submitted under Section 332 of the Act, nor to Section 20.13 of our Rules.<sup>14</sup> In *Louisiana PSC* the

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<sup>9</sup> See *CMRS Second Report and Order*, 9 FCC Rcd at 1504.

<sup>10</sup> *Id.*, 9 FCC Rcd at 1421.

<sup>11</sup> *Id.*, 9 FCC Rcd at 1504.

<sup>12</sup> 47 C.F.R. § 20.13.

<sup>13</sup> See *CMRS Second Report and Order*, 9 FCC Rcd at 1505.

<sup>14</sup> Under *Louisiana PSC*, the Commission may preempt state regulation of intrastate service when it is not possible to separate the interstate and intrastate components of the asserted Commission regulation. *Louisiana Pub. Ser. Comm’n v. FCC*, 476 U.S. 355, 375 n.4 (1986). In construing the “inseparability doctrine” recognized by the Supreme Court in *Louisiana PSC*, Federal courts have held that where interstate services are jurisdictionally “mixed” with intrastate services and facilities otherwise regulated by the states, state regulation of the intrastate service that affects interstate service may be preempted where the State regulation thwarts or impedes a valid Federal policy. See *California v. FCC*, 905 F.2d 1217 (9th Cir. 1990); *Illinois Bell Tel. v. FCC*, 883 F.2d 104 (D.C. Cir. 1989); *National Ass’n of Reg. Util. Comm’ners v FCC*, 880 F.2d 422 (D.C. Cir. 1989).

Supreme Court found that Section 2(b) of the Communications Act prohibits the Commission from exercising Federal jurisdiction with respect to “charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications services.”<sup>15</sup> Here, Congress has explicitly amended the Communications Act to preempt state and local rate and entry regulation of commercial mobile radio services without regard to Section 2(b).

### III. DECISIONAL FRAMEWORK

6. In order to prevail on the merits, the HPUC must sustain its statutory burden of demonstrating that “market conditions with respect to [commercial mobile radio] services fail to protect subscribers adequately from unjust and unreasonable rates or rates that are unjustly or unreasonably discriminatory.”<sup>16</sup> A question arises as to what showing is necessary to sustain this burden. Although we addressed this issue in the *CMRS Second Report and Order*, we revisit it in view of the parties’ debate in this record. As explained more fully below, we do not agree that our decision to forbear from regulating interstate CMRS under certain provisions of Title II makes it impossible to grant a state’s petition. At the same time, we conclude that a state must do more than merely show that market conditions for cellular service<sup>17</sup> have been less than fully competitive in the past. In order to retain regulatory authority, a state must show that, given the rapidly evolving market structure in which mobile services are provided, the conduct and performance of CMRS providers ill-serve consumer interests by producing rates that are not just and reasonable, or are unreasonably discriminatory.

7. Since the Budget Act does not explicitly construe or elaborate on the phrase “market conditions ... fail to protect subscribers adequately from unjust and unreasonable rates or rates that are unjustly or unreasonably discriminatory,” we look to the “design of the statute as a whole and its object and policy” to give that phrase meaning.<sup>18</sup> We begin that task by reference to other Sections of the Communications Act, such as Section 201, which also speak of just and reasonable rates.<sup>19</sup> We have generally described the measure of reasonableness under these Sections in terms of rates that reflect or emulate competitive

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<sup>15</sup> *Louisiana PSC*, 476 U.S. at 373, quoting Communications Act, § 2(b), 47 U.S.C. § 152(b).

<sup>16</sup> 47 U.S.C. § 332(c)(3).

<sup>17</sup> Although the provisions of Section 332(c)(3) of the Act apply to rate or entry regulation in the case of any commercial mobile radio service provider, the HPUC Petition is oriented to the provision of cellular service.

<sup>18</sup> See *Crandon v. United States*, 494 U.S. 152, 157 (1990); *McCarthy v. Bronson*, 500 U.S. 136, 139 (1991).

<sup>19</sup> See 47 U.S.C. § 201; see also 47 U.S.C. §§ 623 (b)-(c) (provisions governing reasonableness of cable television rates).

market operations.<sup>20</sup> The more formal description, however, is whether rates fall within a “zone of reasonableness” that is bounded at one end by the “investor interest in maintaining financial integrity and access to capital markets” and at the other by the “consumer interest in being charged non-exploitative rates.”<sup>21</sup> Regardless of how the test is characterized, it is well established that determinations whether rates fall within this zone are not dictated by reference to carriers’ costs and earnings,<sup>22</sup> but may take account of non-cost considerations such as whether rates further the public interest by tending to increase the supply of the item being produced and sold.<sup>23</sup> These principles define basic components of a state’s demonstration under Section 332. Specifically, a state must show that market conditions fail to produce rates that fall within a “zone of reasonableness,” which is defined by reference to investor and consumer interests viewed in the context of relevant public policy considerations.

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<sup>20</sup> See Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, 4 FCC Rcd 2873, 2886 (para. 25), 2889-2900 (1989); see also Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket Nos. 92-266 & 93-215, FCC 94-286, released Nov. 18, 1994, at paras. 24, 34-37, 64-79.

<sup>21</sup> See, e.g., FERC v. Pennzoil Producing, 439 U.S. 508, 517 (1979); AT&T v. FCC, 836 F.2d 1386, 1390 (D.C. Cir. 1988); see also FPC v. Hope Natural Gas, 320 U.S. 591, 602 (1944); Duquesne Light Co. v. Barasch, 488 U.S. 299, 308 (1989).

<sup>22</sup> See FERC v. Pennzoil Producing, 439 U.S. 508, 517 (1979) (the zone of reasonableness is not defined by a “rigidly . . . cost-based determination of rates, much less . . . one that bases each [carrier’s] rates on its own costs.”) (citation omitted); see also Permian Basin Area Rate Cases, 390 U.S. 747, 769, 797-98, 800-05, *reh’g denied*, Bass v. FPC, 392 U.S. 917 (1968) (upholding ratemaking based upon area-wide average costs).

<sup>23</sup> See, e.g., Mobil Oil Corp. v. FPC, 417 U.S. 283 (1974), in which the Supreme Court upheld a Federal Power Commission incentive plan that permitted an increase in rates in order to encourage increased production. In doing so, the Court emphasized that it was permissible for the agency to consider non-cost factors:

Mobil’s argument assumes that there is only one just and reasonable rate possible for each vintage of gas, and that this rate must be based entirely on some concept of cost plus a reasonable rate of return. We rejected this argument in *Permian Basin* and we reject it again here. The Commission explicitly based its additional “non-cost” incentives on the evidence of a need for increased supplies.

*Id.* at 316. See also Farmers Union Cent. Exch. v. FERC, 734 F.2d 1486, 1502-03 (D.C. Cir), *cert. denied*, 469 U.S. 1034 (1984) (acknowledging agency authority to consider non-cost factors in establishing just and reasonable rates); Public Service Comm’n of New York v. FERC, 589 F.2d 542, 559 (D.C. Cir. 1978) (stating that agencies have authority to adopt incentive-based regulatory approaches in order to serve the public interest).

8. We also consider the meaning of the relevant language in the statute in the context of the overarching command of Section 332(c)(3), which is: “no State ... shall have any authority to regulate” CMRS rates.<sup>24</sup> As we concluded in the *CMRS Second Report and Order*, that provision, as well as the title of Section 332(c)(3) (“State Preemption”), express an unambiguous congressional intent to foreclose state regulation in the first instance.<sup>25</sup> Moreover, OBRA reflects a general preference in favor of reliance on market forces rather than regulation. Section 332(c), for example, empowers the Commission to reduce CMRS regulation,<sup>26</sup> and it places on us the burden of demonstrating that continued regulation will promote competitive market conditions.<sup>27</sup>

9. Unlike some of the opponents of the HPUC Petition, we do not view the statutory preference for market forces rather than regulation in absolute terms. If Congress had desired to foreclose state and Federal regulation of CMRS entirely, it could have done so easily. It chose instead to delineate the circumstances in which such regulation might be applied. Tellingly, it did so in the context of a broad statutory framework with several other principal components. Under the OBRA: (1) substantial amounts of spectrum reserved for Federal government use are to be identified and transferred to commercial and public safety uses;<sup>28</sup> (2) this and other available spectrum, if allocated to commercial telecommunications uses, are to be licensed “rapidly” through the use of competitive bidding systems to promote the development and deployment of new technologies, products, and services, with the goal of stimulating economic opportunity and competition;<sup>29</sup> and (3) in contemplation of the deployment of spectrum to commercial wireless services, and to promote regulatory parity, Congress also articulated definitional criteria for determining common carrier status consistently so success in the marketplace will not be determined by regulatory strategies but by technological innovation, service quality, competition-based pricing decisions, and responsiveness to consumer needs.<sup>30</sup>

10. Viewing all three components together, the statutory plan is clear. Congress envisioned an economically vibrant and competitive market for CMRS services. It

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<sup>24</sup> 47 U.S.C. § 332(c)(3).

<sup>25</sup> *CMRS Second Report and Order*, 9 FCC Rcd at 1504.

<sup>26</sup> 47 U.S.C. § 332(c)(1)(A).

<sup>27</sup> 47 U.S.C. § 332(c)(1)(C).

<sup>28</sup> OBRA § 6001, amending the National Telecommunications and Information Administration Organization Act.

<sup>29</sup> See OBRA § 6002(a), amending Section 309 of the Communications Act.

<sup>30</sup> See 47 U.S.C. § 332(d)(1); *CMRS Second Report and Order*, 9 FCC Rcd at 1420.

understood that such a market was still evolving,<sup>31</sup> and it provided the resources (*e.g.*, additional spectrum) and administrative authority (*e.g.*, licensing through competitive bidding) to accelerate that process. Finally, Congress delineated its preference for allowing this emerging market to develop subject to only as much regulation for which the Commission and the states could demonstrate a clear-cut need. The public interest goal of this Congressional plan is readily discernable. Congress intended to promote rapid deployment of a wireless telecommunications infrastructure. Robust investment is a prerequisite to achieving that goal.<sup>32</sup> Thus, in implementing the statute, we have attempted to facilitate the achievement of this goal by ensuring that regulation creates positive incentives for efficient investment -- rather than burdening entrepreneurial activities -- and by establishing a stable, predictable regulatory environment that facilitates prudent business planning.<sup>33</sup>

11. We emphasize the important impact on our decisionmaking of these fundamental elements of the OBRA statutory framework, which have no counterparts in other sections of the Communications Act. They are devoted exclusively to wireless telecommunications services, and to CMRS in particular. Our analysis of "market conditions" in the context of Section 332(c)(3) necessarily is governed by that framework.

12. Section 332(c)(3) must be interpreted in this context; it is an exception to the general prohibition against state regulation. We conclude that Hawaii, or any other state, should not be allowed to continue regulating CMRS overall, or cellular service in particular, merely by demonstrating that the market for cellular service has been less than fully competitive. Such a standard would effectively allow an exception permitting regulation to

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<sup>31</sup> The Commission's effort to establish new personal communications services (PCS) was initiated in 1989, four years prior to enactment of OBRA, in response to several petitions for rulemaking. During that period we established a formal proceeding to consider PCS issues and adopted major policy decisions that resulted in an allocation to PCS of far more spectrum than is allocated to cellular service. *See* Notice of Inquiry, GEN Docket No. 90-314, 5 FCC Rcd 3995 (1990); Policy Statement and Order, 6 FCC Rcd 6601 (1991); Notice of Proposed Rulemaking and Tentative Decision, 7 FCC Rcd 5676 (1992); Tentative Decision and Memorandum Opinion and Order, 7 FCC Rcd 7794 (1992); Second Report and Order, 8 FCC Rcd 7700 (1993); Memorandum Opinion and Order, 9 FCC Rcd 4957(1994); Third Memorandum Opinion and Order, 9 FCC Rcd 6908 (1994). We also made recommendations and participated, on behalf of the United States Government, in international allocations decision making fora that recognized and permitted the use of such spectrum for PCS and other emerging technologies on a global scale. *See* Report, GEN Docket No. 89-554, 6 FCC Rcd 3900 (1992). Congress was well aware of such activities, as witnessed by the fact that the Budget Act commanded us to begin granting licenses for such new services no later than May 1994. *See* OBRA § 6002(d)(2)(B).

<sup>32</sup> *See* CMRS Second Report and Order, 9 FCC Rcd at 1421; *see also* 47 U.S.C. §§ 309(j)(4)(B), 309(j)(4)(c)(iii); OBRA Conference Report at 483, 492-93.

<sup>33</sup> *Id.*

nullify a general prohibition against it, because it is commonly understood that such conditions have in the past adhered in the cellular marketplace. On numerous occasions since the Commission established the two-carrier cellular market structure in 1982, we have acknowledged that such a structure provided less than optimal competitive opportunities.<sup>34</sup> Other Federal agencies have taken similar positions.<sup>35</sup> One year prior to adoption of the Budget Act, the General Accounting Office (GAO) -- the investigatory arm of Congress -- examined the industry and reported that “[w]hile GAO found no evidence of anticompetitive or collusive behavior in the course of its work, the two-carrier (duopoly) market system that the FCC created may provide only limited competition in cellular telephone markets.”<sup>36</sup> It strains credulity to assert that Congress was blind to these conditions in 1993 when it broadly prohibited state regulation of CMRS.<sup>37</sup> Thus, we reject a reading of the statute that allows continued rate regulation merely on a showing of duopoly conditions, because it is not plausible to conclude that Congress adopted a self-defeating statutory scheme.<sup>38</sup>

13. It also is worth noting that this Agency’s recognition of imperfect cellular market conditions has been matched by our commitment to rectify those conditions as quickly as possible by strengthening and expanding cellular competition rather than by resorting to heavy-handed regulation.<sup>39</sup> For example, we have attempted to heighten cellular competition

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<sup>34</sup> See, e.g., Cellular Communications Systems, 86 FCC 2d 469, 474 (1981), *modified on reconsideration*, 89 FCC 2d 58, 71-74 (1982), *modified on further reconsideration*, 90 FCC 2d 571 (1982); Petitions for Rulemaking Concerning Proposed Changes to the Commission’s Cellular Resale Policies, 6 FCC Rcd 1719, 1725 & n.67 (1991) (*Cellular Resale Order*).

<sup>35</sup> See Reply Comments of the United States Department of Justice, CC Docket No. 91-34, filed June 19, 1991, at 4-5 (“[T]here is insufficient evidence to warrant the conclusion that the cellular service market is in fact workably competitive. In each service area there is still a duopoly[.]”); Comment of the Staff of the Bureau of Economics of the Federal Trade Commission, CC Docket No. 91-34, filed July 31, 1991, at 7 (“[T]he staff disagrees with the tentative conclusion that cellular service is produced in a competitively structured market.”), 10-12.

<sup>36</sup> United States General Accounting Office, “Telecommunications: Concerns About Competition in the Cellular Telephone Service Industry,” GAO/RCED-92-220 (July 1992) (GAO Report).

<sup>37</sup> Cf. *Goodyear Atomic Corp. v. Miller*, 486 U.S. 174 (1988) (Court generally presumes Congress is knowledgeable about existing law pertinent to legislation it enacts); *accord Miles v. Apex Marine Corporation*, 489 U.S. 19 (1990); *Cannon v. Univ. of Chicago*, 441 U.S. 677 (1979); *Minneapolis & St. Louis Railway Co. v. United States*, 361 U.S. 173 (1959).

<sup>38</sup> Cf. *McNary v. Haitian Refugee Center*, 498 U.S. 479 (1991) (Court generally presumes Congress legislates with knowledge of basic rules of statutory construction).

<sup>39</sup> See, e.g., GAO Report at 3 (The “FCC is relying on the introduction of advanced personal communications services to bring competition to the cellular telephone marketplace.”). The Commission policy of avoiding heavy-handed regulation of the cellular market while it was developing also has been determined reasonable in court. See *Cellnet Communication, Inc. v. FCC*,

at the retail level by prohibiting restrictions on the resale of cellular services, except in narrow circumstances where we determined that restrictions intensify competition between the two licensees in each local market.<sup>40</sup> We also have retooled policies initially tailored to promote competition in the wireline market upon determining that they were unlikely to have that effect in the unique setting of wireless telecommunications.<sup>41</sup> Most especially, we have chosen to address the structural infirmity of the cellular market by vastly expanding the amount of spectrum available for two-way wireless voice communications and other innovative wireless services and technologies.

14. The framework of our CMRS regulatory policy -- moderate regulation, symmetrical regulation of all services as appropriate, and a preference for curing market imperfections by lowering entry barriers in order to encourage competition rather than by regulating existing licensees -- aligns closely with the principal building blocks of OBRA. Indeed, that statute is in a very real sense a validation of our approach.<sup>42</sup> As the legislative history of OBRA makes plain, Congress intended those building blocks to establish a *national* regulatory policy for CMRS,<sup>43</sup> not a policy that is balkanized state-by-state.

15. That intention informs our review of petitions filed by states under Section 332(c)(3). Put simply, Congress intended such petitions to be evaluated in light of a general

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965 F.2d 1106, 1112 (D.C. Cir 1992) (petitions for review of FCC order declining to initiate rate regulation of cellular denied because “the FCC could reasonably conclude, in light of the novelty of the service and the speed of technological change, to wait and see how the market evolved...”).

<sup>40</sup> See *Cellular Resale Order*, 7 FCC Rcd at 4006-07. We have recently initiated a review of our resale policies to tailor them to conditions in an emerging wireless telecommunications market that has been expanded to include PCS. See *Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Services*, 9 FCC Rcd 5408 (1994) (*Notice of Proposed Rulemaking and Notice of Inquiry*), Second Notice of Proposed Rulemaking, FCC 95-149, released Apr. 20, 1995.

<sup>41</sup> *Bundling of Cellular Customer Premises Equipment and Cellular Service*, 7 FCC Rcd 4028 (1992).

<sup>42</sup> If Congress had concluded our approach was deficient, or that we should travel in a different policy direction, it is reasonable to conclude that it would have directed us accordingly.

<sup>43</sup> See Conference Report at 480-81, incorporating the findings set forth in the Senate Amendment, including the following:

[B]ecause commercial mobile services require a Federal license and the Federal Government is attempting to promote competition for such services, and because providers of such services do not exercise market power vis-a-vis telephone exchange service carriers and State regulation can be a barrier to the development of competition in this market, uniform national policy is necessary and in the public interest.

preference for allowing the policies embodied in OBRA to have an opportunity to work. With regard to the statutory prohibition on state regulation in Section 332(c)(3) in particular, the legislative history leaves no room for doubt on this point by providing that:<sup>44</sup>

[i]n reviewing [state] petitions . . . the Commission also should be mindful of the Committee's desire to give the policies embodie[d] in section 332(c) an adequate opportunity to yield the benefits of increased competition and subscriber choice anticipated by the Committee.

16. In deference to the states, with whom we have and will continue to share telecommunications jurisdiction under the dual regulatory system of the Communications Act, we have not presumed to establish a rigid blueprint for the demonstration required under Section 332(c)(3). Moreover, unlike many opponents of the petition before us, we do not agree that a state's burden is so great that it is impossible to carry. For example, our decision to forbear from most CMRS regulation is not dispositive of the question whether states may initiate or continue rate regulation of such services. We think it unlikely that Congress would have established two separate statutory procedures -- one to govern our forbearance, and another to govern states' petitions<sup>45</sup> -- if it intended our decisions under the former procedure to control automatically the outcomes under both of them. Instead, we conclude that the exemption in Section 332(c)(3) is designed to permit a state to demonstrate that market conditions in that state warrant a departure from national OBRA policies.

17. Such a demonstration begins but does not end with a showing of less than fully competitive market conditions. Almost all markets are imperfectly competitive,<sup>46</sup> and such conditions can produce good results for consumers.<sup>47</sup> In particular, as noted previously, Congress was aware of the duopoly cellular structure when it generally proscribed state regulation of CMRS. If a showing of less than perfect competition in the past could justify granting a state petition, regulation might be imposed in a great many circumstances. Nothing on this record convinces us that Congress intended that result.

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<sup>44</sup> H.R. Rep. No. 103-111, 103d Cong., 1st Sess. at 261-62.

<sup>45</sup> See 47 U.S.C. §§ 332(c)(1) (forbearance) and 332(c)(3) (state petitions).

<sup>46</sup> In general, perfect competition can exist only where goods are homogeneous, and all buyers and sellers have full information and accept price as given (*i.e.*, they do not try to influence price). There are also certain necessary conditions regarding cost of production. See D. Carlton & J. Perloff, *MODERN INDUSTRIAL ORGANIZATION* 87 (1995). Under perfect competition, price equals marginal cost, which is the incremental cost of producing the last unit of a good. Such conditions are theoretical constructs.

<sup>47</sup> See, *e.g.*, W. Baumol, J. Panzar & R. Willig, *CONTESTABLE MARKETS AND THE THEORY OF INDUSTRY STRUCTURE* 15-46 (1982).

18. Instead, we believe that a state must establish the existence of an environment of unjust and unreasonable, or unreasonably discriminatory, rates, given the dynamic and evolving structure in which CMRS is provided. When we implemented the Section 332(c)(3) state petition process in the *CMRS Second Report and Order*, we adopted a rule designed to elicit the information needed to make such a showing. Such information permits us to perform a Structure-Conduct-Performance (“SCP”) analysis,<sup>48</sup> which is a standard paradigm of modern industrial organization analysis.<sup>49</sup> This paradigm, as applied to the mobile telecommunications industry, holds that market structure is impacted by basic conditions such as the number of licenses issued by the Commission and the state of technology. Conduct, in turn, depends on the structure of the market, *e.g.*, on the number of competitors, the cost structure, and the degree of integration with other wireless providers. Performance, in turn, depends on the conduct of providers and other industry participants with regard to activities such as pricing, inter-firm coordination, and technical standards. Such an analysis permits an evaluation of the degree of rivalry within a particular industry structure and allows us to determine whether and how consumer interests are being served by such activity.

19. Nothing in our rule governing the state petition process suggests that merely showing the existence of a cellular duopoly structure is enough to support a petition. In the first instance, the rule signals our insistence that a petition must be based on demonstrable evidence of anticompetitive activity, or unjust and unreasonable, or unreasonably discriminatory, rates. For example, in order to determine whether an anticompetitive environment presently exists within a state, we requested that a petitioning state produce “specific allegations of fact,” to be supported by a sworn affidavit of an individual with personal knowledge thereof, regarding “anticompetitive or discriminatory practices or behavior by commercial mobile radio service providers.”<sup>50</sup> We also requested “[e]vidence, information and analysis demonstrating with particularity instances of systematic unjust and unreasonable rates ... [or a] pattern of such rates, that demonstrates the inability of the commercial mobile radio service marketplace in the state to produce reasonable rates

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<sup>48</sup> Section 20.13(a)(1) requires states to include “demonstrative evidence” establishing failed market conditions. *See* 47 C.F.R. § 20.13(a)(1). Section 20.13(a)(2) provides an extensive, detailed list of the types of information that states are encouraged to supply in order to meet this evidentiary burden. *See* 47 C.F.R. § 20.13(a)(2)(vi).

<sup>49</sup> *See, e.g.*, F. Scherer & D. Ross, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE*, 4-7 (3d ed. 1990) (“Scherer and Ross”); D. Carlton & J. Perloff, *MODERN INDUSTRIAL ORGANIZATION*, chs. 1, 9 (2d ed. 1994); J. Tirole, *THE THEORY OF INDUSTRIAL ORGANIZATION* 1-3 (1988).

<sup>50</sup> 47 C.F.R. § 20.13(a)(2)(vi).

through competitive forces,” and we indicated that we would consider such evidence “especially probative.”<sup>51</sup>

20. In order to assess present market conditions so as to predict the future effectiveness of market forces within the state, we requested information on the number and type of CMRS providers in the state as well as their respective customers,<sup>52</sup> and “an assessment of the extent to which services offered by the commercial mobile radio service providers the state proposes to regulate are substitutable for services offered by other carriers in the state.”<sup>53</sup> We also requested information and complaint statistics revealing customer satisfaction with CMRS providers within the state.<sup>54</sup> In addition to this information, and as a further aid in projecting CMRS growth rates and other trends within the state, we also requested information on “trends” in each commercial radio provider’s rates and customer base<sup>55</sup> and on “opportunities for new providers to enter into the provision of competing services” as well as “an analysis of any barriers to such entry.”<sup>56</sup> In short, although states have the discretion to adduce such evidence in support of continued rate regulation as they see fit,<sup>57</sup> the comprehensive list of anticipated documentation in Section 20.13 gives states guidance concerning the evidence of structure, conduct, and performance that we would find persuasive in evaluating their petitions.

21. The purposes to which such evidence must be put also are straightforward. For example, with regard to industry structure, while a state seeking to regulate two-way mobile voice services may draw attention to the cellular duopoly, it is incumbent on that state to consider factors that have a direct and substantial impact on that structure. In particular, in evaluating a cellular-oriented petition, we will look with disfavor on any petition that fails to consider the immediate and near-term impact of PCS. Given the general statutory purpose of facilitating PCS-type services, it would be difficult to ignore or downplay the importance of fundamental structural changes when considering Section 332(c) petitions.

22. While PCS is not yet available to the public, it is an accepted antitrust principle that a firm may be considered in competitive analysis if it could enter the market in

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<sup>51</sup> 47 C.F.R. § 20.13(a)(2)(vii).

<sup>52</sup> 47 C.F.R. § 20.13(a)(2)(i) and (ii).

<sup>53</sup> 47 C.F.R. § 20.13(a)(2)(iv).

<sup>54</sup> 47 C.F.R. § 20.13(a)(2)(viii).

<sup>55</sup> 47 C.F.R. § 20.13(a)(2)(ii) and (iii).

<sup>56</sup> 47 C.F.R. § 20.13(a)(2)(v).

<sup>57</sup> *CMRS Second Report and Order*, 9 FCC Rcd at 1504.

question.<sup>58</sup> Under the caselaw potential entry must be reasonably prompt, a typical period being two years from the present in order to expect a significant impact on existing competitors,<sup>59</sup> and there is little doubt that PCS licensees will enter the market for CMRS in competition with cellular providers within this timeframe. We recently concluded an auction designed to license rapidly two additional competitive providers of wireless two-way voice and data communications in every local market in the country. As shown in the table below, the winning bidders in the Hawaii market have committed to pay substantial sums for the right to operate wireless systems in that state. Having done so, it is reasonable to conclude they will deploy the facilities necessary to become operational as quickly as possible so as to begin recouping their investment.

#### BROADBAND PCS AUCTION RESULTS

<b>Hawaii</b>					
<b>MTA #</b>	<b>Freq. Blk.</b>	<b>State</b>	<b>Market</b>	<b>Winning Bidder</b>	<b>Winning Bid</b>
M047	A	Hawaii	Honolulu	Western PCS Corporation	\$22,361,030
M047	B	Hawaii	Honolulu	PCS PRIMECO, L.P.	\$21,675,432

<sup>58</sup> See, e.g., *McCaw Personal Communications, Inc. v. Pacific Telesis Group*, 645 F.Supp. 1166, 1174 (N.D. Cal. 1986) (“the existence of low barriers to entry may rebut a prima facie showing of illegality, even where the combined market shares of the merged firms is quite high”), citing *United States v. Waste Management, Inc.*, 743 F.2d 976, 982-83 (2d Cir. 1984). See also *American Bar Association, I ANTITRUST LAW DEVELOPMENTS (THIRD) 307-11 (1992)* and cases cited therein.

<sup>59</sup> See *FTC v. Owens-Illinois, Inc.*, 681 F.Supp. 27, 37 & n.23 (D.D.C. 1988), *vacated on other grounds*, 850 F.2d 694 (D.C. Cir. 1988) (concerning “the extensive present and future intermaterial competition in the glass and other packaging industries,” “[a]n important, but undisputed, assumption of the economic analysis in this case is that the relevant time frame within which to view elasticity is approximately two years. In other words, conversions by purchasers between types of containers must be feasible within this time frame for demand and supply to be considered elastic”); Department of Justice & Federal Trade Commission, *Horizontal Merger Guidelines* (Apr. 2, 1992)(*Merger Guidelines*), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104 (Apr. 7, 1992) at 20,573-10 (Entry Analysis, Timeliness of Entry: “In order to deter or counteract the competitive effects of concern, entrants must quickly achieve a significant impact on price in the relevant market. The Agency generally will consider timely only those committed entry alternatives that can be achieved within two years from initial planning to significant market impact”) (footnote omitted). The *Merger Guidelines* consider firms to be present competitors if, under certain conditions, they could shift production to a new product within only one year. *Id.* at 20,573-4.

23. The nature of this impending competitive entry bears emphasis. Unlike the typical “ease of entry” case, where entry by new competitors is hypothetical or may occur only at an industry’s margin, PCS activity is undeniably real. It is not something that “may” occur, or that will occur only sporadically. It *is* happening, and it is happening on a nationwide scale. As the recently-completed auction demonstrates, some of this entry is being mounted by large, well-financed entities with long experience and success in the telecommunications business. That field of competitors will be strengthened further upon completion of additional spectrum auctions in the near future. Available evidence indicates that cellular companies, faced with the near-term entry of PCS, have reacted by preparing for impending competition, *i.e.*, by lowering prices and adopting new technologies. For example, there are reports that observable declines in cellular prices are attributable in part to cellular carriers’ knowledge that reasonably soon they will face new competition from PCS licensees.<sup>60</sup> The advent of PCS also appears unambiguously to be having an impact on the present marketplace; it is repeatedly cited as a precipitating factor in major mergers and joint ventures in the wireless industry.<sup>61</sup> Thus, the available evidence indicates strongly that such entry is not speculative. Instead, all evidence suggests that it is empirically real and in the very near term will be substantial and pervasive. This warrants our consideration when evaluating a state petition to regulate rates under Section 332(c)(3).

24. Evidence of industry conduct and performance is also relevant. For example, a state might demonstrate specific instances of collusive behavior on the part of licensees. A state also might demonstrate that the statutory purposes of OBRA were not coming to fruition in that state, or were not likely to do so. We would find highly relevant any evidence that demand for CMRS services in general and cellular service in particular is too low to promote market entry by the number of licensees needed to ensure that facilities-

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<sup>60</sup> See, *e.g.*, COMM. DAILY, Apr. 24, 1995, “*Cellular Industry Eyes Further Cuts, Adjustments to Challenge PCS*” (report on independent researcher’s projection of cellular service rate cuts “up to 40%” over next two years); COMM. DAILY, Telephony Section, Mar. 9, 1995 (NYNEX cellular company “said it will begin offering PCS-type services in metro N.Y. under Geographic Option Plan trademark, giving customers greater flexibility in setting rates and using service. Monthly charge is \$24.99, with additional min. at 29 cents in home county, 99 cents elsewhere”); M. Mills, *Wireless: The Next Generation*, WASH. POST, Feb. 20, 1995, Washington Business Section at 1, 14-15; M. Thyfault, *Bell Companies Get Personal -- Bell Atlantic, NYNEX Plan to Merge Their Mobile and Cellular Divisions as PCS Players Continue Consolidation*, INFORMATIONWEEK, Communications Section at 33, July 18, 1994 (Bell Atlantic announces a low-priced, low-range offering on its Annapolis, Philadelphia, and Pittsburgh cellular systems, intended to resemble PCS offerings).

<sup>61</sup> See, *e.g.*, Applications of Bell Atlantic Corp. and NYNEX Corp. for Transfer of Cellular Radio Licenses to Cellco Partnership, Report No. CL-95-17, File Nos. 00762-CL-AL-1-95 *et al.*, filed Oct. 18, 1994, Exhibit 2 (“Description of Transaction and Public Interest Statement”) at 12, 14; *Id.*, Attachment D, Affidavit of M. Lowenstein at para. 18; Motorola, Inc., Order, DA 95-890, released Apr. 27, 1995, at para. 17 (Wireless Telecommunications Bureau), *petition for reconsideration pending*; *Craig O. McCaw*, 9 FCC Rcd at 5862-63.

based competition will occur at a level adequate to warrant reliance on market forces, rather than rate regulation, as a means of protecting consumer interests.

25. Moreover, a very strong indication that industry conduct and performance are failing to serve consumer interests adequately would be evidence of a lack of investment on the part of licensees in CMRS facilities, or a failure by licensees to deploy adequately new facilities, technologies, and services. Such a showing might support a conclusion that licensees were restricting the output of a service solely to increase its price, and such activity might warrant an appropriate regulatory response. Of course, a successful showing of this nature requires more than evidence that a licensee is earning economic rents (*i.e.*, pricing above cost). It is readily conceivable that economic rents earned in the cellular industry also might advance important public policies, such as if they were applied in furtherance of the statutory goal of promoting investment in the cellular infrastructure. In that event, the rates underlying such profits would have been paid by those who ultimately benefit from reinvestment in cellular facilities. Specifically, as a cellular carrier adds large numbers of customers, it must expand capacity so that the quality of service to existing and new customers is not degraded. Thus, an analysis of economic performance must place great weight on reinvestment of profits in this high-growth industry, for, without such reinvestment, consumers might receive less value for their money. In short, the significance of economic rents under our Section 332(c)(3) analysis is found not simply in their existence in the first instance but in their subsequent application.

26. Finally, we note that SCP evidence typically may be segregated into two categories: static factors and dynamic factors.<sup>62</sup> For example, prices or rates of return in a given year are static factors. Growth and investment are dynamic factors. In addition, a dynamic analysis views price and other static factors at a given point in time in their relationship to static factors such as price in the future.<sup>63</sup> Thus, a rate of return that looks high today may be fair and reasonable when looked at in terms of its impact on future prices.<sup>64</sup> Furthermore, static factors are, as the name implies, static, or even temporary, whereas the long-term impact of dynamic factors is more important because their effects are cumulative and more permanent. Thus, we believe that evidence concerning dynamic factors is a more persuasive market indicator than evidence concerning static factors. Given the rapidly changing nature of the market in which wireless services are provided and the statutory purposes of OBRA, we conclude that evidence of where a market is going is more relevant than evidence of where it has been.

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<sup>62</sup> See, *e.g.*, J. Tirole, *THE THEORY OF INDUSTRIAL ORGANIZATION* 209-70 (1988).

<sup>63</sup> *Id.* at 239-70.

<sup>64</sup> In particular, consumers may be better off facing somewhat higher prices today in exchange for high levels of investment by existing competitors.

27. No single factor, standing alone, necessarily would tip the balance for or against a particular state petition. The statute allows the states flexibility to make their showings in the best manner they see fit, and it is conceivable that we might find a showing based primarily on one factor to be persuasive. Those demonstrations that are tied most closely to the statutory scheme are, of course, the most determinative. Our decisions in this proceeding and similar proceedings are based on the totality of the evidence.

#### IV. CONFIDENTIALITY

28. Hawaii states in its petition that it cannot provide data on the customers served by CMRS carriers subject to regulation, due to the reluctance of CMRS utilities to provide such data absent a guarantee that they will be protected from disclosure.<sup>65</sup> Other states, however, have submitted sensitive commercial data through procedures provided in this Commission's Rules, and such data have been considered on a confidential basis.<sup>66</sup> Any uncertainty on Hawaii's part regarding the treatment of confidential data in this proceeding was dispelled in the *First Confidentiality Order*, which explicitly invited Hawaii to submit supplemental data with a request for confidential treatment, in accordance with Sections 0.457, 0.459, and 0.461 of our Rules. Hawaii has not submitted such data. Thus, any decision not to use confidential data to support Hawaii's Petition is that State's alone.

29. Mobile Telecommunications Technologies Corp. (MTel) on October 19, 1994, filed supplemental reply comments with a motion for their acceptance, asserting that the replies filed timely on October 4, 1994, raised for the first time new arguments that could adversely affect Mtel. Although our rules generally proscribe the filing of supplemental pleadings in proceedings under Section 332(c)(3),<sup>67</sup> MTel presents good cause for waiving our rule in this instance. Moreover, nothing on this record suggests that any party is harmed by accepting MTel's filing, and doing so will expand the record of relevant record materials and thereby tend to improve it. For these reasons, we grant MTel's motion and consider its supplemental reply.

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<sup>65</sup> Hawaii Petition at 6.

<sup>66</sup> See Petitions of the Public Utilities Commission, State of Hawaii; the State of California and the Public Utilities Commission of the State of California; the Connecticut Department of Public Utility Control; and the New York State Public Service Commission, PR Docket Nos. 94-103, 94-105, 94-106, 94-108, DA 95-111, order issued by Wireless Telecommunications Bureau on Jan. 25, 1995, (*First Confidentiality Order*); Petitions of the Public Utilities Commission, State of Hawaii; the State of California and the Public Utilities Commission of the State of California; the Connecticut Department of Public Utility Control; and the New York State Public Service Commission, PR Docket Nos. 94-103, 94-105, 94-106, 94-108, DA 95-208, order issued by Wireless Telecommunications Bureau on Feb. 9, 1995 (*Second Confidentiality Order*).

<sup>67</sup> See 47 C.F.R. §§ 20.13(a)(5), 20.13(b).

## V. HAWAII PETITION

### A. Summary of PUC Request

30. Hawaii regulates five cellular companies and three radio common carriers in the state under Chapter 269 of the Hawaii Revised Statutes, which confers “broad regulatory oversight and investigative authority over all public utility companies.”<sup>68</sup> The subject cellular companies are GTE Mobilnet of Hawaii Incorporated (GTE Mobilnet), the only wireline cellular company in the state; USCOC of Hawaii 3, Inc., d/b/a United States Cellular (USCOC); Maui Cellular Telephone Company, Inc. (MCTC); Honolulu Cellular Telephone Company (HCTC); and Cybertel Corporation, d/b/a Cybertel Cellular (Cybertel).<sup>69</sup> The three radio common carriers are Dr. Mark Goldman, d/b/a Island Radio-Phone (Goldman); Ram Paging Hawaii (Ram Paging); and General Telcourier, Inc., d/b/a Pager One (General Telcourier).<sup>70</sup>

31. Hawaii asserts its primary objectives in carrying out regulatory functions are to assure adequate and efficient services and reasonable rates, and to provide a fair return to regulated CMRS utilities. Hawaii states that it seeks to continue its regulation of CMRS utilities’ rates and tariffs because it is uncertain whether the initial market driven rates that Petitioner approved for the CMRS utilities when they were certificated are currently just and reasonable.<sup>71</sup> Hawaii says that financial reports filed in the past three years indicate CMRS utilities are “generally beginning to experience either an increase in profits and a recovery of their prior accumulated losses or potential profits for the future. From the outset, the CMRS utilities used market driven rates rather than cost and/or the return on invested capital to structure their rates and tariffs.”<sup>72</sup> Based on data submitted by Hawaii, the average after-tax rate of return for cellular carriers was approximately 14 and 19 percent during 1992 and 1993, respectively.<sup>73</sup>

32. Hawaii asserts that financial data show CMRS utilities generally experienced heavy losses during the early years, and profitability after three or more years. The data also show that as the customer base increased, revenues seem to have increased

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<sup>68</sup> Hawaii Petition at 2 n.1.

<sup>69</sup> Evidence submitted by the Hawaii PUC concerning the financial performance of cellular companies operating in that state is presented in Attachment 1 to its Petition.

<sup>70</sup> Evidence submitted by the Hawaii PUC concerning the financial performance of radio common carriers operating in that state is presented in Attachment 2 to its Petition.

<sup>71</sup> Hawaii Petition at 3-4.

<sup>72</sup> *Id.*

<sup>73</sup> *See* Appendix B.

proportionately more than the incremental increase in the associated operating costs and the investment in plant and equipment. Hawaii states the increase in rate of return on the invested plant and equipment has substantially increased over the years, indicating the return will become greater as more customers subscribe.<sup>74</sup> Hawaii asserts that it “intends to test” the market driven rates against the cost of service and rate of return to determine whether the current rates and tariffs are excessive.<sup>75</sup>

In order to conduct this review and monitor the operating costs, the rate of return on rate base, and the overall financial condition of each of the CMRS utilities, Petitioner must continue to regulate the utilities’ rates and tariffs. Additionally, by regulating the rates, Petitioner will also be able to effectively monitor rate design and structure, as well as the availability and quality of service, since each of the CMRS utilities will be required to appear before Petitioner for all rate case filings.

33. Hawaii also states it should continue to regulate CMRS rates and tariffs to ensure true competition “once other companies are licensed by the FCC and certificated by Petitioner” and contends that “such regulatory oversight is necessary whether the tariffs of the CMRS utilities are based on market driven rates or cost and return on invested capital.”<sup>76</sup> Hawaii asserts it should at least continue to regulate CMRS rates and tariffs until the conclusion of its communications infrastructure docket (Docket No. 7702), instituted in May 1993, which it anticipates in mid-1995.<sup>77</sup>

34. Hawaii describes trends in the operators’ customer base in Attachments 1 and 2 and Exhibits A-1 through A-8 of its Petition. Rate information is provided in Attachment 3, but Hawaii asserts that it did not include trends because carriers have not sought a rate increase. The regulatory regime to be applied if the Petition is granted is described in Attachment 4 and summarized below.

#### **B. Rate Regulation for Which Continued Authority Is Sought**

35. Hawaii’s proposed general order setting standards for CMRS in the state requires that a tariff be on file and available for public inspection during business hours of

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<sup>74</sup> Hawaii Petition at 4.

<sup>75</sup> *Id.* at 4-5.

<sup>76</sup> *Id.*

<sup>77</sup> *Id.* at 5-6.

each CMRS business office.<sup>78</sup> The tariff is required to include exchange areas, base rate areas, and the “conditions and circumstances” under which service will be furnished, and defining the classes and grades of service available to customers. Maps showing the CMRS utility’s service area and facilities are required to be accessible at CMRS business offices as well.<sup>79</sup>

36. Hawaii also would require each CMRS utility to file an annual projection of capital improvements for the ensuing five years, “in considerable detail” for the first year. In addition, Hawaii would require that capital expenditures for single projects exceeding the lesser of \$500,000 or 10 percent of the utility’s plant in service be submitted for review at least 60 days prior to construction or commitment of funds.<sup>80</sup> The contemplated review process includes a hearing before a HPUC determination that any portion of the proposal should be disallowed from the rate base.

37. The proposed general order also addresses customer billing disputes and related matters,<sup>81</sup> the establishment of customer credit and deposits, and complaint procedures,<sup>82</sup> engineering standards,<sup>83</sup> inspections and tests,<sup>84</sup> service quality standards,<sup>85</sup> and safety requirements.<sup>86</sup>

38. The existing tariffs submitted by Hawaii as Attachment 3 to its Petition indicate tariffing practice of several years’ standing that generally comports with the proposed general order. Thus, for example, the HCTC tariff includes three cellular service plans apparently established in March 1986, and definitions of peak and off-peak rate periods

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<sup>78</sup> Hawaii defines “tariff” to include “the entire body of rates, charges, definitions, rules and regulations, including those contained in special contracts with customers and in supplemental tariffs, adopted and filed by the CMRS utility and authorized by the Commission.” Hawaii Petition Att. 4 at 2 (Sec. 1.3, “Definitions”). The accessibility requirement is at Sec. 2.3.a.

<sup>79</sup> Hawaii Petition Att. 4 at 3-4 (Sec. 2.3.b.).

<sup>80</sup> Hawaii Petition Att. 4 at 4 (Sec.2.3.d.).

<sup>81</sup> Hawaii Petition Att. 4 at 5 (Sec. 4.1).

<sup>82</sup> Hawaii Petition Att. 4 at 5-9 (Sec. 4.2-4.4). The copies of the Attachment provided to the Commission lack page 8 but the internal organization indicates the absent text applies to consumer protection provisions.

<sup>83</sup> Hawaii Petition Att. 4 at 9-10 (Secs. 5.1-5.3).

<sup>84</sup> Hawaii Petition Att. 4 at 10-11 (Secs. 6.1-6.6).

<sup>85</sup> Hawaii Petition Att. 4 at 11-13 (Secs. 7.1-7.4).

<sup>86</sup> Hawaii Petition Att. 4 at 13 (Secs. 8.1-8.2).

that have not been altered since January 1990.<sup>87</sup> The rates and application of several options under the basic cellular plan and two options for the bulk service plan each date from August 1990.<sup>88</sup> The general terms of the HCTC reseller service plan date from March, 1986,<sup>89</sup> while rates under optional plans date from 1989 or 1990.<sup>90</sup>

## VI. CASE ON THE MERITS

### A. Pleadings of the Parties

39. Several commenters oppose the petition. BellSouth, GTE, and McCaw offer the specific perspective of cellular operators, while trade groups, including CTIA and PCIA, assert more general contentions about the state of cellular competition and standards for review of petitions. In addition, AMSC urges continued preemption of state authority over space and ground segments of mobile satellite services (MSS), and AMTA opposes state rate authority over reclassified private land mobile services.

40. Support for partial grant of the petition, limiting state rate authority to cellular providers, comes from resellers, *i.e.*, the NCRA. While Nextel, a competitor of incumbent cellular operators in its provision of Specialized Mobile Radio (SMR) and wide area SMR service, only asserts that such a selective grant is warranted in California, other parties contend the prospect of disparate rate regulation in Hawaii is raised by Nextel's suggestion. Similarly, E. F. Johnson asserts that if formerly private carriers are subject to rate regulation, local SMR service should be excepted, and only wide area SMR should be subject to continued rate authority as applied to cellular service. PCIA, Paging Network, and Mtel argue Hawaii has provided no basis for asserting rate authority over paging and other non-cellular CMRS, and these parties, joined by GTE, McCaw, and RCA, also address whether rate authority limited to cellular service would impair regulatory parity.

41. Opponents of any continued rate authority state that Hawaii does not even allege that market conditions fail to protect subscribers, or that the existing state regulatory regime better protects consumers than the Federal forbearance approach.<sup>91</sup> Indeed, GTE contends Hawaii's existing regulatory practice has substantially delayed new service offerings

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<sup>87</sup> See HCTC P.U.C. Tariff No. 1A, Original Sheet 5, First Revised Sheet 6.

<sup>88</sup> HCTC Tariff P.U.C. No. 1A, Second Revised Sheet 9-9A, and First Revised Sheet 12.

<sup>89</sup> HCTC Tariff P.U.C. No. 1A, Original Sheet 13.

<sup>90</sup> See HCTC Tariff P.U.C. No. 1A, First Revised Sheet 17, 17A; Second Revised Sheet 18, First Revised Sheet 18, Original Sheet 18A.

<sup>91</sup> BellSouth Opposition at 1-3; McCaw Opposition at 2-3.

and alternative rate plans.<sup>92</sup> McCaw and BellSouth assert that state petitions must demonstrate market conditions that are substantially deficient when compared to national duopoly circumstances, and that Hawaii's limited factual submission does not identify the state as distinctively problematic.<sup>93</sup> McCaw also asserts that Hawaii should be required to demonstrate that market conditions cannot be remedied by exercise of retained Federal authority under Sections 201, 202, and 208 of the Communications Act, and that the benefits of Hawaii's proposed regulation will exceed costs.<sup>94</sup>

42. Nextel similarly asserts that, with respect to "non-dominant" CMRS providers such as its SMR and wide area SMR operations, Hawaii has not satisfied the statutory standard. Nextel contends, however, that state regulation of "dominant" CMRS providers, *i.e.*, cellular operators, is justified. McCaw responds that both Congress and the Commission have rejected a regulatory distinction based on "dominance" of cellular service, and notes the Congress considered and rejected a proposal to authorize disparate regulatory requirements on existing and new service providers.<sup>95</sup> CTIA adds that the statutory preemption test is not premised on a dominance standard, but on review of market conditions with an eye toward similar regulatory treatment of similar services.<sup>96</sup> McCaw also notes that Nextel's support of continued regulation of cellular is unsupported by economic or other evidence.<sup>97</sup>

43. As to Hawaii's concern whether existing CMRS rates are reasonable in light of recently improved CMRS carrier earnings, opponents state that Hawaii's return data, even if accepted as valid,<sup>98</sup> do not establish the unreasonableness of rates in an industry

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<sup>92</sup> GTE Opposition at 4-8.

<sup>93</sup> BellSouth Opposition at 11-12; McCaw Opposition at 4-6.

<sup>94</sup> *Id.*

<sup>95</sup> McCaw Reply at 7-9.

<sup>96</sup> CTIA Reply at 1-3.

<sup>97</sup> McCaw Reply at 3-6. Nextel's argument in the California context occasioned responses from several parties in this proceeding concerned about regulatory parity. *See, e.g.*, GTE Opposition at 17-19; McCaw Opposition at 3-4; Mtel Opposition at 6-8; GTE Reply at 2-6; PageMart Reply at 1-4; RCA Reply at 1-4. As we deny Hawaii's Petition in its entirety, we need not consider these contentions.

<sup>98</sup> BellSouth asserts the accounting method returns used by Hawaii are inferior to economic return data on several grounds, and GTE criticizes HPUC's use of pre-tax return data for both cellular and paging services. *See* BellSouth Opposition at 12-14, Rozek Aff. at 6-7; GTE Opposition at 20-21.

facing quite different circumstances than a traditional public utility.<sup>99</sup> Indeed, GTE and BellSouth assert real cellular rates have declined over the last several years, such that Hawaii's rates are some of the lowest in the country.<sup>100</sup> Commenters stress that Hawaii has not otherwise sought to demonstrate or substantiate problematic market conditions,<sup>101</sup> and iterate the Commission's past determination that cellular industry characteristics in general, notwithstanding its duopolistic structure, warrant forbearance from selected elements of Federal regulatory authority.<sup>102</sup>

44. Opponents also assert that Hawaii's initiation of an inquiry into rate base regulation is not a continuation of current regulation, and much of its proposed future regulatory mechanism does not pertain to rates.<sup>103</sup> McCaw states that granting continued rate authority to enable review of market driven rates by reference to costs and returns is to invert Section 332 of the Act, which requires an initial demonstration of unreasonable rates as a basis for grant of rate authority. McCaw notes that Hawaii can file a subsequent petition if findings in its infrastructure docket enable such a demonstration.<sup>104</sup>

45. The NCRA supports the Hawaii petition, asserting that until "effective competition" arrives, continued state rate regulation is necessary to restrain the dominating market power of cellular duopolists. NCRA references reports issued by several Federal agencies describing the competitive deficiencies of cellular market structure, including the Department of Justice review undertaken with respect to generic wireless waivers sought by Bell Operating Companies.<sup>105</sup> For the Commission to reject the several states' petitions, which are the only form of regulatory oversight absent Federal monitoring of cellular, NCRA argues, it must reject its own views as well as those of the Department of Justice.<sup>106</sup> CTIA replies that the Commission's forbearance standard in the *CMRS Second Report and Order* was based on a finding of sufficient competition, and that proponents of state rate authority

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<sup>99</sup> BellSouth Opposition at 15-16; McCaw Opposition at 6-8.

<sup>100</sup> GTE Opposition at 3-4, 21-23; BellSouth Opposition at 21-22.

<sup>101</sup> BellSouth Opposition at 11-12; McCaw Opposition at 6-8; GTE Opposition at 13-17; CTIA Opposition at 2.

<sup>102</sup> CTIA Opposition at 8-9; McCaw Opposition at 2-3.

<sup>103</sup> BellSouth Opposition at 3, 18-19.

<sup>104</sup> McCaw Opposition at 8; *see also* PCIA Opposition at 11-12.

<sup>105</sup> NCRA Comments at 2-3, *citing* United States v. Western Electric, Memorandum of the United States in Response to Bell Companies' Motion for Generic Wireless Waivers, Civ. Action No. 82-0192 (filed July 25, 1994).

<sup>106</sup> NCRA Comments at 4-6.

generally have failed to support their assertions with empirical evidence of market power.<sup>107</sup> McCaw adds that NCRA's documents in most instances predate spectrum auction legislation, and all but one predate the *CMRS Second Report and Order*; none, asserts McCaw, adduce state-specific findings respecting market conditions.<sup>108</sup>

## **B. Discussion**

### **1. Qualification of Petition**

46. Hawaii has not submitted its currently effective tariffing and rate regulations, and the absence of requests for rate increases since CMRS carriers initiated service suggests limited occasion to exercise or develop various aspects of HPUC rate regulatory practice. Examination of tariffs submitted with the Petition, however, as well as comments submitted by carriers operating in the state, indicate that while Hawaii has not yet undertaken detailed rate-based regulation as a routine procedure, its present review of rates requires tariffing and its review of such tariffs apparently may entail significant and protracted delay of those tariffs' effectiveness.<sup>109</sup> Nor do cellular carriers operating in Hawaii dispute the presence of existing rate regulation; although BellSouth characterizes it as minimal.<sup>110</sup> GTE characterizes the state's review of new service offerings as "burdensome and time-consuming," asserting that all rates must be filed with and approved by the HPUC, and that "most rate or service offerings" are delayed 30 days before becoming effective.<sup>111</sup> Even recognizing that each instance of pre-effectiveness review of tariffed service offerings may not turn directly on the reasonableness of proposed rates, we consider such review a recognized element in the common understanding of "rate regulation." Hawaii's *existing* regime is sufficiently portrayed in the record to demonstrate that "regulation concerning the rates for any commercial mobile service" was being exercised by that state on June 1, 1993. Therefore, we conclude that Hawaii's Petition is properly before us.

### **2. Showing on the Merits**

47. Section 332(c)(3) provides that a state petition shall be granted if it "demonstrate[s]" that market conditions for the service at issue fail to protect subscribers

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<sup>107</sup> CTIA Reply at 4-5.

<sup>108</sup> McCaw Reply at 3-6.

<sup>109</sup> See GTE experience, described in GTE Opposition at 4-8.

<sup>110</sup> See, e.g., BellSouth Opposition at 22 ("BellSouth submits that the HPUC's generally hands-off regulation serves as a model demonstrating that market driven policies, not draconian rate of return regulation, better serve the public interest.").

<sup>111</sup> See GTE Opposition at 5-8.

adequately from unjust, unreasonable, or unreasonably discriminatory rates. On this record we conclude that Hawaii has not made such a demonstration and, accordingly, we deny its Petition.

48. Our decision is based in part on the fact that Hawaii's Petition in principal part does not argue that market conditions fail to protect subscribers adequately from unjust, unreasonable, or unreasonably discriminatory rates. Rather, Hawaii principally requests continued rate authority *in order to determine* market conditions. The statute is not satisfied by a showing of uncertainty about the need for rate regulation, however. Section 332(c)(3) requires a demonstration that market conditions *fail* to protect subscribers, not that they *may be failing* to protect them.

49. Our decision also is based on other factors. First, Hawaii does not address the direct and fundamental changes to the duopoly cellular market structure that are being realized by PCS and other services, such as wide area SMR. Second, Hawaii presents no systematic or authenticated evidence of collusive or otherwise anticompetitive practices concerning the provision of any CMRS. Third, Hawaii does not present evidence showing widespread consumer dissatisfaction with CMRS providers in that state, or discuss what specific rate regulations are needed to address whatever level of dissatisfaction may exist. Fourth, Hawaii fails to advance any persuasive analysis regarding the critical issue of investment by cellular licensees (or by any other CMRS providers).<sup>112</sup>

50. Another shortcoming of Hawaii's Petition is that it views any evidence of market imperfection as proof of a need for continued rate regulation, while all countervailing evidence is attributed to its regulatory oversight. Even assuming such an argument is reasonable in theory, the HPUC has not established its factual predicate. The HPUC does not appear to have prescribed any particular pricing or rate development formula, and with minor exceptions, all currently effective and previously effective cellular rates in Hawaii appear to have been carrier-initiated. On this record, we are not persuaded by the HPUC's implicit argument that, absent continuation of its rate regulation authority, even for a limited period of time, cellular or other CMRS rates will quickly fall outside the zone of reasonableness.

51. Finally, by default, rate of return information becomes the principal remaining girder upon which Hawaii might rest its case. In general, we are not persuaded that rate of return evidence alone constitutes sufficient ground to support a petition, even assuming, *arguendo*, that Hawaii's pre-tax return data accurately portray carriers' financial

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<sup>112</sup> An important indicator of market failure, in our view, would be evidence that cellular firms are withholding investment in facilities as a means of restricting output and thus boosting price. Here, in contrast, the record shows a general pattern of substantial investment by licensees. Record data demonstrate that CMRS carriers continue to invest in plant at levels significantly above their depreciation schedules. *See* Appendix C.

performance.<sup>113</sup> In this regard, the relevant observation is not how such returns compare with those earned by traditionally regulated public utilities in mature, stable environments. Rather, any such observation must account for the fact that CMRS is a dynamic and relatively infant industry that is still developing. A key element of the study of markets is the recognition that not all industries and markets are at the same stage of development.<sup>114</sup> Thus, the comparison necessary for determining whether prices are just and reasonable is not with mature industry, but with high growth industries. It has been shown that the rate of growth of output is one of the most important determinates of profitability, that is, all other things being equal, high growth firms (such as the cellular industry) tend to earn high profits.<sup>115</sup> Furthermore, even if profits are high now, the entry of PCS should contain those profits increasingly forcefully. Thus, evidence that cellular industry profits are higher than that we might allow, for example, for local exchange carriers, is not dispositive.

52. Hawaii's specific rate of return evidence does not dissuade us from this view. During 1992 and 1993, the weighted average after-tax returns are 14.2 percent and 19.6 percent, respectively. We do not consider this to be high in the context of a high growth industry. These levels likely will be reduced as the presence of PCS carriers grows in Hawaii -- an event we think it reasonable to measure in months, not years. That additional competition should drive prices and rates of return of cellular carriers down even further. Even now, the data Hawaii provided show negative or very low returns for many CMRS carriers. For example, during 1993, GTE Mobilenet, Inc.'s operations on the Islands of Hilo, Maui, Oahu and Kauai show returns of -12.2 percent, 3.39 percent, 8.55 percent, and -4.79 percent, respectively. Even where profits seem high in a given year, we recognize that short term profits must be earned to recover losses or lean returns in previous years, otherwise investment capital may turn to other more profitable investments. In sum, while we would be concerned if average rates of return were high in the long term, particularly after accounting for the high growth rate, Hawaii has not demonstrated that such conditions exist. For that and the foregoing reasons, we deny Hawaii's petition.

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<sup>113</sup> Because Hawaii has not adduced significant evidence in this or in other respects, we need not consider the several methodological arguments raised by commenters against the method used to develop HPUC return data. We do not suggest by this that the return data submitted by HPUC are accepted without reservation.

<sup>114</sup> For example, Prescott, Kohli, and Ven Katraman have shown that the determinants of rate of return on investment vary between mature industries and emerging industries. See J. Prescott, A. Kohli & N. Ven Katraman, "The Marketshare-Profitability Relationship: An Empirical Assessment of Major Assertions and Contradictions," *Strategic Management Journal*, Spring 1986, 377-94. They found, for example, that high market share is correlated with high rates of return in mature industries, but not for emerging industries.

<sup>115</sup> D. Ravenscraft, "Structure-Profit Relationship at the Line of Business and Industry Level" *REVIEW OF ECONOMIC AND STATISTICS*, Feb. 1983, at 22-31.