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 1989 WL 418621 (N.Y.P.S.C.), 29 N.Y.P.S.C. 421
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Re Regulatory Policies for Segments of the Telecommunications Industry Subject
 to Competition
 Case No. 29469
 Opinion No. 89-12
 New York Public Service Commission
 May 16, 1989

OPINION and order concerning the appropriate regulatory response to competition
 in the telecommunications industry.

P.U.R. Headnote and Classification

1.
 MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Cellular service.
 NY.P.S.C. 1989

Cellular telephone service was held subject to effective market competition.
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 to Competition

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P.U.R. Headnote and Classification

2.
 PUBLIC UTILITIES

s117 -- Telecommunications -- Cellular service -- Competition -- Regulatory
 policy.

NY.P.S.C. 1989

Based on its determination that the market for the provision of cellular
 telecommunications services was competitive, the commission announced that it
 would seek legislation to suspend application of most aspects of the Public
 Service Law, including certification and rate regulation, to the provision of
 cellular service; the commission stated that the legislation it seeks will allow
 it to monitor market conditions and reinstitute regulation to the extent
 necessary to maintain a competitive market.

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3.
 MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Resale services.
 NY.P.S.C. 1989

Telecommunications resale service was held subject to effective market
 competition.

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4.

PUBLIC UTILITIES

s117 -- Telecommunications -- Resale service -- Competition -- Regulatory policy.

NY.P.S.C. 1989

Based on its determination that resale activity in the telecommunications market generally tended to exhibit the characteristics of effective competition, the commission announced that it would propose legislation to reduce the level of regulation of telephone resellers; however, because of the potential for market failure, the legislation will provide for minimum service, rate, and interconnection requirements for alternative operator services, customer-owned, coin-operated telephone services, and shared tenant services.

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5.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Other common carriers (OCCs) -- InterLATA services. NY.P.S.C. 1989

Other common carriers (OCCs) operating in the interLATA services market were found subject to effective market competition.

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6.

PUBLIC UTILITIES

s117 -- Telecommunications -- Other common carriers (OCCs) -- InterLATA services -- Regulatory policies.

NY.P.S.C. 1989

In an opinion reviewing regulatory policies for segments of the telecommunications industry that were subject to competition, the commission found it appropriate to continue its limited regulation of other common carriers (OCCs) operating in the interLATA services market; however, it was deemed appropriate to modify the exercise of limited regulation (which required OCCs to be certified and to file tariffs and subjects OCCs to minimal service quality and financial reporting standards as well as to the commission's complaint jurisdiction) by reducing reporting requirements so that only basic financial statements, market share information, and the tabulation of complaints must be reported.

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7.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Market dominance -- InterLATA services.
NY.P.S.C. 1989

AT&T Communications of New York, Inc., was held to exert market dominance in the interLATA services market despite evidence of a steadily decreasing market share.

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8.

PUBLIC UTILITIES

s117 -- Telecommunications -- InterLATA service s -- Dominant carrier -- Regulatory policies.
NY.P.S.C. 1989

Based on its determination that the dominant interexchange carrier continued to possess substantial market power in the interLATA market, the commission determined that continued regulation was advisable; however, in light of the dominant carrier's declining market power, the commission found that additional pricing flexibility, especially for the more competitive service offerings, was appropriate and that, if its market power continues to decline and competition increases, the dominant carrier's interLATA services should be deregulated by January 1, 1992; nevertheless, the commission stated that any deregulation proposal would emphatically confirm the dominant carrier's universal service and nondiscriminatory common carrier obligations, would include consumer protection monitoring procedures, and would provide authority to reregulate.

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9.

RATES

s566 -- Telephone rate design -- Centrex service -- Flexible pricing -- Local exchange carriers.
NY.P.S.C. 1989

Local exchange telephone carriers (LECs) were authorized to implement a wider use of individual case-basis pricing for Centrex service; the commission agreed to remove current restrictions on line size and distance from the central office if, concurrently, the LECs would file rate stability options for private branch

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exchange trunk service; while the individual pricing arrangements will not be specified by tariff, the tariffs must include general provisions designed to allow nondiscriminatory access to such arrangements to similarly situated customers and appropriate cost data to support each arrangement must be filed with commission staff to ensure that no cross-subsidization by basic services occurs.

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10.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Private line service -- Local exchange access.
NY.P.S.C. 1989

Telecommunications service providers that collect traffic of large customers and transport it over dedicated, private lines between customer locations or to interexchange carriers' points of presence, should be allowed comparably efficient interconnections (or, in other words, virtual collocation) for the purpose of competing with the dominant local exchange carrier for the transport of private line and dedicated carrier access services in the New York metropolitan LATA; accordingly, the dominant local exchange telephone carrier was directed to establish comparably efficient interconnections at its local central offices with registered or certified carriers for the carriage of intrastate private line traffic in the New York metropolitan LATA.

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11.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Private line service -- Local exchange access.
NY.P.S.C. 1989

Because requiring the dominant local exchange telephone carrier (LEC) to establish comparably efficient interconnections at its local central offices with registered or certified carriers for the carriage of intrastate private line traffic could adversely affect ratepayers (due to the potential loss of contributions that are received by users of basic services from profits on the LEC's provision of dedicated, private line service), the commission stated that it may require an interconnector to bear some of the burdens concomitant with the new rights it receives by (1) implementing an "equal access" tariff structure which would produce a contribution to basic services that would be derived on a nondiscriminatory basis from both the dominant local exchange carrier and other carriers and (2) establishing a universal service fund to support services such as lifeline service, emergency service, the placement of pay telephones in uneconomic areas, and relay service for the deaf.

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12.

RATES

s553 -- Telephone rate design -- Private line service -- Pricing flexibility.
NY.P.S.C. 1989

Requiring the dominant local exchange carrier (LEC) to establish comparably efficient interconnections at its local central offices with registered or certified carriers for the carriage of intrastate private line traffic must be accompanied by a concomitant increase in the LEC's pricing flexibility; accordingly, when the interconnection tariffs of a LEC are approved, that LEC will be allowed pricing flexibility for high-capacity private line service and interoffice private line circuits.

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13.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Switched services -- Fiber optic facilities -- Local exchange access.

NY.P.S.C. 1989

The commission rejected a request by a provider of fiber optic telephone service for the ability to interconnect its fiber optic facilities with the central offices of a local exchange carrier (LEC) for the purpose of providing switched services; the commission found that inasmuch as the unbundling of switched access service elements necessary to accommodate such a competitive alternative would result in significant restructuring of access charges and the pricing flexibility of the LEC for switched access service is constrained until September 1991 by the Modification of Final Judgment (48 PUR4th 227, 552 F.Supp. 131), the request for collocation could not be granted; the commission stated that it would review its policy on the collocation issue after the Modified Final Judgment restrictions are removed.

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14.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Market dominance -- IntraLATA toll service.
NY.P.S.C. 1989

The local exchange telephone carrier (a subsidiary of a Bell System regional holding company) was held to exert market dominance in the intraLATA toll

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service market.

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P.U.R. Headnote and Classification

15.

PUBLIC UTILITIES

s117 -- Telecommunications -- IntraLATA toll service -- Competition -- Regulatory policy.

NY.P.S.C. 1989

A request by a local exchange telephone carrier (LEC) for the deregulation of its intraLATA toll services was denied where it was found that although the dominant interexchange carrier and other common carriers competed with the LEC for intraLATA toll business, the LEC remains the dominant provider.

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16.

RATES

s553 -- Telephone rate design -- Billing and collection services -- Competitive pricing -- Individual billing contracts -- Local exchange carriers.

NY.P.S.C. 1989

Local exchange telephone carriers (LECs) were authorized to offer billing and collection services through individual billing contracts; nevertheless, tariffs will still be required for those portions of billing and collection services which use bottleneck facilities and billing and collection functions will be monitored closely to ensure that pricing and operation policies are not used to suppress enhanced service providers or, in instances where LECs offer enhanced services, to skew competition.

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17.

RATES

s553 -- Telephone rate design -- Private line service -- Moratorium.

NY.P.S.C. 1989

In an opinion reviewing regulatory policies for intraLATA telecommunications services that were subject to competition, the commission stated that it was willing to modify an existing rate moratorium agreement with a local exchange carrier to adjust for the net impact of changes in the pricing policies for private line interconnection and Centrex service.

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i.

RATES

s532 -- Telephone rate design -- Competitive pricing -- Elasticity -- Bypass.
NY.P.S.C. 1989

Statement, by the commission, that because existing technology allows the largest users of telecommunications services to construct private systems, attempts to deny the benefits of competitive pricing to such users would only encourage them to drop off the public system, which would increase prices for captive customers.

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ii.

RATES

s543 -- Telephone rate design -- Customer classes -- Cross-subsidies.
NY.P.S.C. 1989

Statement, by the commission, that realigning residential subsidy dollars within the residential class so that they flow to only those customers who need them, rather than to all residential customers regardless of need, reduces the negative effects of competition on low-income customers.

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iii.

SERVICE

s433 -- Telecommunications -- Regulatory policies -- Universal service.
NY.P.S.C. 1989

Statement, by the commission, in an opinion reviewing regulatory policies for segments of the telecommunications industry that were subject to competition, that careful observance of the following would assure consumer protection while maximizing competitive benefits: (1) undiminished commitment to universal telephone service for all New Yorkers, (2) maintenance of high service quality, (3) continued existence of an adequate forum for resolving consumer concerns, (4) avoidance of rate shock to individual customer groups, (5) continued commission oversight to ensure that deregulation is not the first step toward unregulated monopoly or near monopoly, and (6) maintenance of the ability of the commission to regulate if any of the above conditions are not met.

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iv.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Regulatory policies.

NY.P.S.C. 1989

Statement, by the commission, in an opinion reviewing regulatory policies for segments of the telecommunications industry that are subject to competition, that the commission must continue to (1) encourage competition to the extent consistent with the maintenance of universal service, (2) monitor the status of the competitive telecommunications market, (3) monitor the market conditions to determine which companies are nondominant, (4) monitor price trends to ensure that deregulation generates neither predation nor anticompetitive cross-subsidies, (5) establish service requirements to ensure access to emergency service, (7) determine customer satisfaction with the quality of competitive services, (8) ensure that the quality of basic service does not diminish, (9) ensure that those services defined as basic continue to be provided at rates that are reasonable, (10) ensure that adequate complaint resolution mechanisms exist, either through department staff to the extent services continue to be provided pursuant to tariff or commission-approved contract, or through the service providers themselves in the case of deregulated services, and (11) obtain from companies any information necessary to make the foregoing determinations.

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v.

PUBLIC UTILITIES

s117 -- Telecommunications -- Resale service -- Regulatory policy.

NY.P.S.C. 1989

Discussion, by the commission, of the attributes of various types of telecommunications services provided by resellers and of the degree of regulatory oversight appropriate for each type of service; includes discussion of cellular service, toll service, alternative operator service, customer-owned, coin-operated telephone service, and shared tenant service.

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vi.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- InterLATA services -- Other common carriers (OCCs) -- Market power.

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NY.P.S.C. 1989

Statement, by the commission, that while the interLATA market share of other common carriers (OCCs) was steadily increasing, the market share is spread among an increasing number of competing entities, hence, the market power of individual carriers was unlikely to increase.

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vii.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- IntraLAT A services -- Contribution to basic services -- Regulatory policies.

NY.P.S.C. 1989

Statement, by the commission, in an opinion reviewing regulatory policies for intraLATA telecommunications services that were subject to competition, that careful monitoring was required to prevent adverse impacts on ratepayers that might result from the fact that the contribution to basic services would diminish as various services of dominant carriers became subject to price competition.

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viii. MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Private line service -- Local exchange access -- Interconnection.

NY.P.S.C. 1989

Statement, by the commission, that allowing liberal interconnection with the local exchange network generally fosters competition and will likely provide more effective and efficient carrier access service.

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ix.

MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Regulator y policies.

NY.P.S.C. 1989

Statement, in a concurring opinion issued in a decision reviewing regulatory policies for telecommunications services that are subject to competition, that no service -- basic or nonbasic, large or small -- should be considered permanently noncompetitive, and the commission should strive to break down barriers and eliminate bottlenecks whenever and wherever they occur.

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x.

TELEPHONES

s2 -- Construction and equipment -- Upgrades.

NY.P.S.C. 1989

Statement, in a concurring opinion issued in a decision reviewing regulatory policies for telecommunications services, that because the global competitiveness of the United States and New York economies was directly related to the telecommunications industry, the commission should encourage upgrades of the network system through incentive-based regulation, experimentation, innovation, infrastructure investment, and a more rapid pace of planning.

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xi.

PUBLIC UTILITIES

s117 -- Telecommunications -- Video transmission -- Regulatory policies.

NY.P.S.C. 1989

Statement, in a concurring opinion issued in a decision reviewing regulatory policies for telecommunications services, that the commission, in the near future, should deal with issues that arise as networks increasingly provide pathways for mass announcement services and move technologically towards video transmission.

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xii.

PUBLIC UTILITIES

s117 -- Telecommunications -- Interconnection and access -- Regulatory policies.

NY.P.S.C. 1989

Statement, in a concurring opinion issued in a decision reviewing regulatory policies for telecommunications services, that in the coming years policy makers must structure ways in which network interconnection is granted, defined, priced, and technically harmonized to provide mutual interaction among the increasingly large number of members of the network family.

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xiii. MONOPOLY AND COMPETITION

s83 -- Telecommunications -- Regulatory policies.

NY.P.S.C. 1989

Statement, in a concurring opinion issued in a decision reviewing regulatory policies for telecommunications services, that, to ensure that competition does not lead to cyclical price instability or oligopolistic price coordination, regulators must be vigilant to instances of price collusion and foster potential alternatives such as resellers as a means of reducing oligopsonist temptations. Re Regulatory Policies for Segments of the Telecommunications Industry Subject to Competition

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APPEARANCES: Saul M. Abrams, Esq., William Bouteiller, Esq., for Department of Public Service Staff, Three Empire State Plaza, Albany, New York 12223; Thomas M. Eichenberger, Esq., Katherine P. White, Esq., Elaine McHale, Esq., for AT&T Communications of New York, Inc., 32 Avenue of the Americas, New York, New York 10013; Sam Laniado, Esq., Read & Laniado, for New York State Telephone Association, Inc., 25 Eagle Street, Albany, New York 12207; Howard Read, Esq., Read & Laniado, for Cellular Telephone Co., Syracuse Telephone Co., and Utica Cellular Co., 25 Eagle Street, Albany, New York 12207; Lesley Douglass Webster, Deputy Commissioner and Counsel (by Anne F. Curtin, Esq.), for New York State Department of Economic Development, One Commerce Plaza, Albany, New York 12245; David R. Poe, Esq., H. Liza Moses, Esq., LeBoeuf, Lamb, Leiby & MacRae, for ALLTEL New York, Inc., 520 Madison Avenue, New York, New York 10022; Frank J. Miller, Esq., Huber, Lawrence & Abell, for Continental Telephone Co. of New York, Inc., 99 Park Avenue, New York, New York 10016; B.P. Oliverio, Esq., Kavinoky & Cook, for Albany Telephone Co., Buffalo Telephone Co., and Genesee Telephone Co., 120 Delaware Avenue, Buffalo, New York 14202; Edward R. Wholl, Esq., Alan Stein, Esq., for NYNEX Mobile Communications Co., One Blue Hill Plaza, Pearl River, New York 10965; Robert C. Atkinson, R.P. Romanelli, for Teleport Communications, One World Trade Center, Suite 2649, New York, New York 10048; William E. Erickson, Esq., S. Elizabeth Daigle, Esq., for MCI Telecommunications Corp., Five International Drive, Rye Brook, New York 10573; David A. Gross, Esq., Sutherland, Asbill & Brannan, for New York Clearing House Association, 1666 K Street, N.W., Washington, D.C. 20006; Henry D. Levine, Esq., Brant S. Karstetter, Esq., Morrison & Foerster, for New York Clearing House Association, Committee of Corporate Telecommunications Users, and MCI Telecommunications Corp., 2000 Pennsylvania Avenue, N.W., Suite 5500, Washington, D.C. 20006; Michael T. Tomaino, Esq., Nixon, Hargrave, Devans & Doyle, for Rochester Telephone Corporation, Lincoln First Tower, Rochester, New York 14603; Donald W. Boecke, for Rochester Telephone Corporation, 100 Midtown Plaza, Rochester, New York 14646; Josephine S. Trubek, Esq., Helen Zamboni, Esq., for Rochester Telephone Mobile Communications, and RCI Corporation, 100 Midtown Plaza, Rochester, New York 14646; Jack R. Lebowitz, Esq., Miller, Mannix, Lemery & Pratt, P.C., for United States Transmission Systems, Inc., American Mobile Communications, Inc., Cellcom Telephone Company, and Nationwide Cellular Services, Inc., Northway Plaza, P.O. Box 3300, Glens Falls, New York 12801; Robert L. Sills, Esq., Deborah A. DuPont, Esq., Reboul, MacMurray, Hewitt, Maynard & Kristol, for U.S. Sprint Communications Company, 45

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Rockefeller Plaza, New York, New York 10020; Stephen P. Bowen, Esq., for U.S. Sprint Communications Company, 1850 M Street, N.W. -- 11th Floor, Washington, D.C. 20036; Daniel W. Rosenblum, Esq., Ashok Gupta, Public Utility Law Project, for Universal Service Alliance, 2090 Seventh Avenue, Suite 2000, New York, New York 10027; Randolph J. May, Bishop, Cook, Purcell & Reynolds, for User Parties, 1400 L Street, N.W., Washington, D.C. 20005; Robert J. Cimino, Esq., for County of Suffolk, Building 158, North County Complex, Veterans Memorial Highway, Hauppauge, New York 11788; Glenn Richards, Esq., for New York City Energy and Telecommunications Office, 49 Chambers Street, Room 720, New York, New York 10007; Keith J. Roland, Esq., Roland & Fogel, for Empire Association of Long Distance Telephone Users, 1 Columbia Place, Albany, New York 12207; Richard H. Wagner, Esq., Colin Grannum, Esq., Gerald Oscar, Esq., for New York Telephone Company, 1095 Avenue of the Americas, New York, New York 10036; Kathleen Quinn Abernathy, Esq., Ellen S. Deutsch, Esq., Thelen, Marrin, Johnson & Bridges, for Taconic Telephone Corporation, 2300 N Street, N.W., Washington, D.C. 20037; James V. Troup, Esq., Ellen S. Deutsch, Esq., Kadison, Pfaelzer, Woodard, Quinn & Rossi, for Taconic Telephone Corporation, 2000 Pennsylvania Avenue, Suite 7500, Washington, D.C. 20006; Philip S. Shapiro, Esq., for NYS Consumer Protection Board, 99 Washington Avenue, Albany, New York 12210; Kathleen Hawkins Berkowe, Esq., for Rockefeller Center Telecommunications, 1230 Avenue of the Americas, New York, New York; Hal Lubow, for AMCOM, 600 Meadowland Parkway, Secaucus, New Jersey 17094; Matt Edwards, for Unicell, Inc., 177 East 87th Street, Suite 401, New York, New York 10128; Diana Forrest, for Cellcom Telephone Company, 34-36 Fornelius Avenue, Clifton, New Jersey 07012.

Before Bradford, chairman, and Jerry, Schwartz (concurring), Noam (concurring), McFarland, Kresky, and Williams, commissioners.

By the COMMISSION:

OPINION AND ORDER CONCERNING

REGULATORY RESPONSE TO COMPETITION

PROCEDURAL BACKGROUND

In light of the emergence of competition in some segments of the telecommunications industry, we instituted this case to review our regulatory policies. Our staff had reported recent substantial expansion in the number of firms operating in the toll, private line, and cellular markets and that each of those markets was exhibiting competitive characteristics. We therefore convened a formal proceeding [FN1] "to determine the degree to which effective competition currently exists within each of [those] markets and among the various companies operating in [those] markets."

The proceeding was conducted in two stages, with Administrative Law Judge J. Michael Harrison presiding. The first stage provided for the development of an analytical framework for defining and measuring the extent of competition and adduced evidence concerning that issue. The second stage provided for the development of regulatory policy issues raised in our initiating order, and was handled "on the papers as part of the post hearing briefs." Hearings were held

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in May, June, September, and October 1987, at which 30 witnesses testified on behalf of 20 parties. The record comprises 3,331 pages of testimony and 141 exhibits.

Judge Harrison's recommended decision was issued on May 9, 1988. The Judge analyzed each segment of the telecommunications market and recommended, on the basis of his analyses, varying degrees of regulation. He proposed that the present regulatory scheme be retained for the intra-LATA market, but otherwise generally endorsed staff's proposal to streamline regulation, finding that regulation could be made less burdensome in some instances. He noted as well that the record could have benefited from certain kinds of information, such as cost studies, but that it nevertheless revealed the broad outlines of market conditions. Parties filing briefs to the Commission concerning the Judge's recommendations are listed in Appendix A.

INTRODUCTION

[i-iv] The public interest is generally furthered by the emergence of competition wherever possible and prudent. The transition from regulation to competition is a critical challenge confronting utility regulators at this time. Done wisely, it offers potentially lower prices, higher service quality, broader consumer choice, more efficient industries, higher productivity, and a stimulus to economic growth, especially in the information-intensive service industries that provide the economic backbone of the New York economy.

Done too rapidly or with insufficient safeguards, it could lead to unregulated monopoly, price shocks, ratepayer subsidies for unregulated enterprises, and declines in service quality. Done too slowly, it will foster high prices, impede new service offerings, stagnate markets, and weaken the economy.

In most of the major regulated monopoly industries, this transition is underway. However, in the telecommunications sector -- where the technology itself has changed fundamentally in often procompetitive ways -- the pace has been especially fast. Since the breaking of the AT&T near-monopoly over telephone terminal equipment interconnection, the choices and prices in that market segment have improved immeasurably, and the forecasted evils (such as technical harm to the network) have not occurred.

The opening of the market for carrying calls is more complex than the opening of the market for customer premises equipment, but the potential customer benefit is still great. Because much of the benefit of transport competition occurs in the first instance to large volume users and has the potential to reduce existing residential subsidies, the introduction of competition that may eliminate the source of the subsidy is controversial, but it is conditioned by two important factors.

First, the existing technology allows the largest users to construct private systems. Attempts to deny the benefits of competitive pricing to these users can only encourage them to drop off the system altogether, which would increase prices to everyone else.

Second, existing residential subsidies went, before the Commission's lifeline program, to all customers, not just to those who needed them. The wealthiest residential customer received the same subsidy as a member of the middle class or the poorest customer. Realigning the subsidy dollars within the residential class so that they flow to those who need them reduces the negative effects of

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competition on low income customers. [FN2]

Six other basic principles will assure consumer protection while maximizing competitive benefits. We will move toward competition as rapidly as possible as long as -- but only as long as -- they are carefully observed:

- 1) Our commitment to universal affordable telephone service for all New Yorkers is undiminished.
- 2) High service quality must be maintained.
- 3) An adequate forum for resolving consumer concerns must continue to exist.
- 4) Rate shock to individual customer classes or groups must be avoided.
- 5) Deregulation is not to be the first step toward unregulated monopoly or near monopoly.
- 6) The ability to reregulate if any of the above conditions are not met must be maintained.

Emerging competition requires altered regulation. Some of the changes may be accomplished administratively; others require revisions to the Public Service Law. To that end, we will propose legislation that would largely deregulate competitive providers or services and permit us to deregulate other providers or services upon a finding that they are competitive. At the same time, the statute permits reregulation of deregulated services or providers when necessary, and allows us to ensure that customer satisfaction is maintained at a reasonable level. We must continue to

- encourage competition to the extent consistent with the maintenance of universal service;
- monitor the status of the competitive telecommunications market and the quality of its service;
- monitor market conditions to determine which companies are nondominant;
- monitor price trends to insure that deregulation generates neither predation nor anti-competitive cross-subsidies;
- establish service requirements to insure access to emergency service;
- determine customer satisfaction with the quality of competitive services;
- insure that the quality of basic service does not diminish;
- insure that those services defined as basic continue to be provided at rates that are reasonable;
- insure that adequate complaint resolution mechanisms exist, either through department staff to the extent services continue to be provided pursuant to tariff or Commission-approved contract, or through the service providers themselves in the case of deregulated services; and
- obtain from companies any information necessary to make the foregoing determinations.

CELLULAR TELEPHONE SERVICE

[1][2] Cellular telephone services, which use radio frequencies, are provided under a market structure determined by federal, rather than state, agencies. The Federal Communications Commission (FCC) licenses up to two carriers (one associated with the local exchange company and one not so associated) to provide cellular service in a given cellular geographic service area. The FCC has established 17 cellular service areas in the state: 11 metropolitan service areas and six rural service areas. All metropolitan areas are served by two competing carriers. The FCC has yet to authorize operators for the rural areas.

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Resellers are also permitted to purchase bulk capacity from licensed carriers for repackaging and resale to the public.

Since these carriers provide services that are not now considered essential to most telephone users, and since there are or will be at least two competitors in each territory in which the service is provided, we do not regulate them extensively. Although carriers must be certified, must file tariffs and must report financial information, the processes have been simplified. Our complaint jurisdiction extends to ordering resolution of disputes, although, as with any other tariffed service, we encourage carriers to make efforts to resolve complaints on their own.

In this case, the cellular telephone companies associated with local exchange telephone companies (Rochester Mobile and NYNEX Mobile) argued for the deregulation of cellular service; arguments also were made by other parties for more or less regulation than now exists.

Judge Harrison determined that if the service were considered a non-essential luxury, deregulation would be appropriate. Alternatively, if the service were essential, he would recommend a staff proposal that regulatory requirements be streamlined to the extent possible.

If the service is furnished competitively, we need not decide whether it is a luxury. We conclude that the service is furnished competitively, for the market structure is one that has been designed by the FCC to be competitive. Additionally, the existence of resellers -- compounded by the existence of significant excess capacity -- operates to check monopoly abuses of the facilities-based carriers and reduce the potential for a duopoly. Our experience, which shows that these carriers do not need to be regulated, as well as that of more than half the states, which have deregulated or vastly reduced regulation of cellular service, also supports our conclusion that this market is competitive.

We therefore will seek legislation that suspends the application of most aspects of the Public Service Law, including certification and rate regulation, to the provision of cellular service. The Legislature took such action with respect to one-way paging and two-way mobile communication services in 1984, similar action is justified here. [FN3]

The legislation would authorize us to monitor market conditions to insure that the basic principles discussed above will be satisfied. [FN4] Our proposal would exempt cellular telephone service from Articles V and VI of the Public Service Law but would establish minimal registration, service and reporting requirements. It would also provide that we could reinstitute regulation if necessary. We would retain authority to obtain from the company market information involving market share, number of providers, price levels, such other indices of competition that we shall specify, and such other service and rate information that we feel is necessary. We will direct our staff to develop requirements for periodic reports that are designed to provide this information.

As for our consumer protection function, we no longer would act as the customer's forum of last resort for resolution of complaints. Rather, our job would be to insure that the companies are making adequate complaint resolution mechanisms available and are taking steps necessary to provide customers with sufficient information to make informed choices about their service options.

Pending action on our legislative proposal, we shall not alter the manner in which cellular telephone service is regulated. We shall require that a local

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exchange company that provides cellular service do so through a separate subsidiary. [FN5] Although we usually rely on cost accounting procedures to protect against outsiders when regulated and non-regulated services are provided by the same business, it is more effective to simply separate the businesses. Because cellular service is provided over a network that is physically independent of landline telephone facilities, that approach -- which is not practicable in instances where both services use the landline network -- is the one we shall use here.

RESELLERS

[3][4] [v] The resale of telephone services occurs when a firm orders services from a regulated supplier and repackages those services in a way that provides consumers benefits of pricing and/or additional service and feature availability. [FN6] Resellers can exist due to the differential between the wholesale and retail rates of facilities-based carriers or because this service offers advantages not available from the wholesaler. They operate in a number of telecommunications markets. Cellular resellers, for example, can buy up blocks of cellular capacity and resell them to end users. Resellers have no telecommunications facilities themselves, [FN7] and are most often entities that sell and install the cellular instruments (such as automobile dealers). The FCC has allowed only two facilities-based cellular carriers in each service area and has therefore required cellular telephone carriers to offer non-discriminatory resale of their services to facilitate the development of a resale market.

A reseller of toll services buys service from a facilities-based carrier and supplies service on a retail basis to its own customers. Frequently, such resellers also employ network equipment to switch or transport traffic and so take on, to some extent, the attributes of a facilities-based carrier. These resellers tend to enhance the competitiveness of toll markets.

A variant of toll resale has come to be known as alternative operator services (AOS). These providers resell long distance service for operator assisted calls. They package the resale of toll with the operator assistance function, which they provide themselves. These firms contract with institutions, such as hotels and hospitals, where large volumes of demand for operator assisted calls are concentrated. The fundamental service AOS providers offer these institutions is their capability for remote billing. Of course, dominant regulated carriers also have this capability. Where a hotel or a hospital has a contract with an AOS provider to carry all its operator assisted traffic, the hotel's customers or hospital's patients have no alternative means (or perhaps only a poorly described and inconvenient one) of carrier selection. These captive users are thus vulnerable to high rates and poor service.

Two other special resale situations also involve potential bottlenecks which require special attention. These involve the provision of customer owned, coin operated telephones (COCOTs) and the provision of shared tenant service (STS). The latter service results, for example, when the owner of a building directly or through a service operator provides switching equipment and some telephone service -- such as inter-tenant calling and direct connection to interexchange -- to the tenants without necessarily using the facilities of the local exchange company.

Resellers (except for COCOTs) are required to be certified and to file tariffs.

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They are subject to our resolution of customer disputes as well as limited financial reporting and accounting rules. In this proceeding, resellers sought to have their services at least detariffed, and preferably deregulated.

Judge Harrison concluded that the level of regulation of telephone resellers could be significantly reduced. He reasoned that because resellers cannot influence the wholesale price of the service they resell, regulation has little role to play.

With the noted exceptions, resale activity tends to exhibit the characteristics of effective competition and tends to foster competition in the markets in which resellers participate. There are no significant, effective barriers to entry and resellers generally do not have the ability to control prices or exercise market power. Accordingly, we will propose legislation for resellers similar to that being proposed for cellular service. However, because of the potential for market failure, the legislation will provide for minimum service, rate, and interconnection requirements for AOS, **COCOTs** and STS.

Pending adoption of the legislation, we will continue light regulation of most resellers (e.g., we will continue to certify new carriers and require tariff filings and will continue to apply certain minimum service requirements). We will also continue our complaint resolution function as long as these services continue to be provided pursuant to tariff. Cellular resellers enhance the competitiveness of that market; and it must be clear that the facilities-based carriers should treat all competitors -- including their subsidiaries -- equally. We are also concerned that regulated companies not use resale to avoid their underlying common carrier obligation.

The exceptions to these interim arrangements occur where a reseller can constitute a bottleneck. Such bottlenecks can be harmful because they may create market power that can result in non-market based decisions on pricing, quality, and content or user discrimination. **COCOTs** and alternative operator services are two instances where resellers may wield significant market power. We are concerned about the impact on consumers who use these services and we have recently established a proceeding that will consider the resale of service through **COCOTs**, [FN8] and another proceeding is evaluating alternative operator services. [FN9] We shall retain authority to deal with such problems if and when they occur.

Shared tenant services providers may also become bottlenecks. Those providers resell, in effect, both local and toll service, and could prevent or substantially deter a tenant from obtaining service from other providers, such as the local exchange company. Accordingly, our legislative proposal would require STS providers to permit reasonable access to the services of the local exchange company and interexchange carriers for tenants who desire service directly from that company and interexchange carriers. STS providers must permit exchange company access to their intra-building facilities at fair and reasonable rates.

INTER-LATA SERVICES

Other Common Carriers

[5][6] [vi] The record in this proceeding shows that the other common carriers (OCCs) -- carriers other than ATTCOM, such as MCI and Sprint -- exert little

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market power. In the inter-LATA market, for example, they had 11% of the revenues and 14% of the subscribers in 1986, the latest year for which the record contained data. These proportions represent a significant increase from the period immediately following divestiture, and the trend of this increasing share should continue. While the OCCs' aggregate share is steadily increasing, it will be spread among a greater number of competing entities. An individual company's market share -- and, hence, market power -- is unlikely to increase significantly.

We currently exercise only limited regulation of the OCCs. They are required to be certified, and to file tariffs, but are subjected to minimal service quality and financial reporting standards as well as our complaint jurisdiction. In this case, staff proposed further loosening of the regulation of these firms and Judge Harrison recommends staff's proposals.

Given the status of the market, we will continue the light regulation of the non-dominant OCCs. Reporting requirements, however, will be reduced by requiring only basic financial statements, market share information, and the tabulation of complaints.

Our legislative proposal for these companies will be similar to those discussed above for the cellular and reseller market segments.

ATTCOM

[7][8] ATTCOM is currently subject to the full panoply of regulation; [FN10] Judge Harrison recommends that because of its market share it continue to be so regulated.

The OCCs have relatively little market power as evidenced by their individually small market shares; conversely, ATTCOM continues to have substantial, though steadily declining, market power in the inter-LATA market. It has earned high profits in recent years while controlling, in the period immediately following divestiture, up to 90% of the New York inter-LATA market. (The existence of high profits immediately after divestiture is, of course, not dispositive of market power. These profits, in any event, may have been more attributable to uncertain access costs than to monopoly power.) Moreover, ATTCOM's national market share is declining, and there is no reason to expect a different result in New York. Still, given its dominant position, continued regulation, at least for a transition period, is advisable for ATTCOM's provision of inter-LATA service. Therefore, regulation of ATTCOM shall not now be relaxed to the extent that it is being relaxed for the other long distance companies.

Additional pricing flexibility, however, is justified, especially in ATTCOM's more competitive services. Thus, for the two and one half year period after the current rate moratorium (until January 1, 1992), ATTCOM shall be offered as an alternative to traditional rate base regulation, an incentive regulation plan. The plan would freeze ATTCOM's message toll service prices [FN11] at current levels as a price ceiling and provide for substantial pricing flexibility for its other, more competitive services. That flexibility will be subject to two constraints; that no rate element be increased by more than 25% per year and that the annual revenue increase from price increases, without hearings, be limited to 2.5%. (This latter limitation is required by the Public Service Law.) We would also allow for the rapid introduction of new services without prior analysis of cost support and provide that changes in access charges,

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separations, and any regulatory costs imposed due to regulatory requirements be flowed through to customers. Similarly, we would provide that the effects of federal, state, or local tax law changes would also be flowed through to customers. ATTCOM would be required to continue to offer universal service at geographically averaged prices [FN12] and, over the period, to share equally with ratepayers earnings in excess of a predetermined level. The sharing level will be determined after receipt of comments on an ATTCOM filing implementing this proposal. [FN13]

In the longer run, we intend to deregulate ATTCOM. Its market share is likely to decline further, and it has made a reasonable case that it is subject to increasingly significant competition. Competitive pressures are likely to grow as more customers get equal access and ATTCOM's competitors mature. We conclude, therefore, that unless there is a material change in circumstances, ATTCOM should be deregulated by January 1, 1992. We shall seek legislation to accomplish that end. The legislative authority we plan to seek now would permit us to provide ATTCOM with full pricing flexibility starting in 1992 and make the treatment of ATTCOM symmetric with that of the OCCs. Any deregulation proposal would emphatically confirm ATTCOM's universal service and nondiscriminatory common carrier obligations, would include the consumer protection monitoring procedures discussed earlier, and would provide us with authority to reregulate.

INTRA-LATA SERVICES

Introduction

[vii] The issues considered in this section cover a broad range, from residential access lines to a variety of business services. The status of competition varies in each market as well. As we explain in each of the subsections that follow, we will tailor regulation to fit the competitive characteristics of each market. As a general matter, competition is more advanced downstate, and a greater degree of deregulation is warranted there. When and if competition emerges upstate, we will be receptive to proposals for similar deregulation.

One problem, resulting from the way certain services have traditionally been priced, involves several services and thus bears discussion at the outset. As various services of dominant carriers become competitive, the market drives prices to cost, and the contribution made by those services in support of basic service diminishes. We will carefully monitor this situation in order to mitigate adverse impacts on ratepayers.

As part of that review, we will attempt to spread fairly the costs of local exchange service, in order to avoid having that burden borne solely by the local exchange companies. Where interconnectors, such as Teleport, receive new rights, it may be reasonable to require that they bear some new burdens. Moreover, we anticipate that technology and competition will drive costs down and therefore address concerns in this area.

Dedicated Switching

[9] Centrex services provided by the local exchange company involve customized central office switching that provides the business customer with station-to-

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station intercom-like service and special features. Alternatively, a customer may purchase, from a non-regulated company, a Private Branch Exchange (PBX), which provides for switching between stations on the customer's premises. PBXs must be linked to the public network via trunk lines, so local exchange company control of those lines could provide monopoly power.

In this case, New York Telephone presented evidence concerning the competitiveness of Centrex and sought additional pricing flexibility for that service. Judge Harrison determined that while PBXs are a thriving alternative to Centrex, New York Telephone still possessed inordinate power because no competitor could provide an alternative to the PBX access trunk. The Judge noted as well that New York Telephone already had some pricing flexibility.

It is possible to provide greater flexibility without allowing the monopoly abuses feared by the Judge. The local exchange companies will be allowed a wider use of individual case base pricing arrangements by removing the current restrictions on line size and distance from the central office if, concurrently, the local exchange companies file rate stability options for PBX trunk service. While the individual billing arrangement prices will not be specified by tariff, the tariffs shall include general provisions designed to allow non-discriminatory access to such arrangements for similarly situated customers. Additionally, appropriate cost data to support each arrangement must be filed with staff so that no cross subsidization by basic services occurs.

The larger issue of whether the rates for Centrex and PBX exchange access service should be unbundled is being examined in two ongoing proceedings, the Intellipath case [FN14] and the open network architecture proceeding, [FN15] and the issue will be resolved there.

We will also propose that the Legislature amend the Public Service Law to allow the approval of the deregulation not only of nondominant firms, but also the selective deregulation of competitive services provided by dominant firms. Dominant firms may face competition in the provision of some services -- Centrex is a good example -- and it may be reasonable to deregulate such services when adoption of cost allocation rules makes it possible to protect against cross-subsidies. The FCC and several states already have most of this capability and we will recommend a similar approach for New York.

Private Line, Collocation, and Interconnection

[10][11][12] [viii] In the New York Metropolitan Area, New York Telephone Company faces growing competition from providers such as Teleport, which collect traffic of large customers and transport it over dedicated, private lines between customer locations or to interexchange carriers' points of presence. In this case, Teleport sought to collocate its fiber optic facilities inside New York Telephone central offices in order to duplicate the local exchange company's ability to aggregate low volume traffic.

Teleport asserted that it had improperly been prohibited from competing with New York Telephone by New York Telephone's refusal to allow it to interconnect. It claimed we should require New York Telephone to collocate Teleport facilities at the local exchange companies' central offices, and to offer transport and switching services separately.

New York Telephone opposed Teleport's request.

Judge Harrison found no basis for adopting Teleport's proposal. He determined

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that its presentation reflected an "artificial perspective" [FN16] on competition in telecommunications and recommended that it be rejected.

The Judge's view of competition is too restrictive, and it clashes with emerging open network architecture concepts that encourage unbundling the network into elemental components and offering them on a non-discriminatory basis. With some limitations, therefore, Teleport's proposal is acceptable. Allowing liberal interconnections with the local exchange network generally fosters competition and will likely provide more effective and efficient carrier access service.

Teleport, as well as other interconnectors and similar networks of large users, should be allowed comparably efficient interconnections (or, in other words, virtual collocation) for the purpose of competing with New York Telephone for the transport portion of private line and dedicated carrier access services. If Teleport (or others) can offer better service, better terms, or lower prices, the public interest will be enhanced.

Therefore, New York Telephone will be required to establish comparably efficient interconnections at its local central offices with registered or certified carriers for the carriage of intrastate private line traffic in the New York metropolitan LATA. New York Telephone shall file, within 60 days, tariffs providing for non-switched collocation/interconnection. The physical location of the interconnection point may be outside of a New York Telephone building, but the interconnection must be technically and economically comparable to actual collocation and the terms must be reasonable. A prima facie definition of reasonableness would be the prior acceptance of the terms by the connecting party, as long as the same terms are available to others seeking collocation/interconnection. We are aware that such arrangements may be complicated, and we will work to insure that any arrangements are fair to all.

Our action is designed to foster competition while minimizing unreasonable or extraordinary adverse impacts on other ratepayers. To do so it must be evenhanded and must consider mitigating demonstrated losses of existing contribution that would result from this action. Accordingly, we may require that an interconnector, such as Teleport, bear some of the burdens concomitant to the new rights it receives. This proposal could be implemented for example, by requiring an "equal access" tariff structure, which produces a contribution in support of basic services that is derived on a non-discriminatory basis from both New York Telephone and other carriers. The purpose of any such proposal should not be to increase available contribution but only to mitigate projected contribution losses. On a broader scale, we are evaluating myriad issues concerning the establishment of a universal service fund to support services, such as lifeline service, emergency service, the placement of coin telephones in uneconomic areas, and relay service for the deaf.

Teleport must also allow similar access to its facilities by New York Telephone or other carriers. As we note below, we shall allow New York Telephone to petition to be made whole for these changes, which were not contemplated by the current moratorium.

The removal of this barrier to the entry of private line competitors must be accompanied by a concomitant increase in the existing carriers' pricing flexibility. Accordingly, when the New York Telephone interconnection tariffs are approved, that company will be allowed pricing flexibility for its high capacity private line service and interoffice private line circuits.

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Specifically, New York Telephone will be granted the authority to increase rates for high capacity and interoffice private line services by 25% annually, and to decrease them without limitation, so long as rates cover their relevant incremental costs. This tariff flexibility, designed to further spur competition, will apply throughout the New York Metropolitan LATA (where we are authorizing further competition), but New York Telephone will also be permitted to offer individual case billing arrangements on a non-discriminatory basis for these services in the New York Metropolitan LATA in response to competitive requests for proposals. In order to prevent cross-subsidization by basic services, New York Telephone shall file with our staff cost support for price changes to competitive private line rate elements and individual case billing arrangements. The rates may become effective immediately upon such a filing, unless staff brings concerns to our attention. New York Telephone may elect to attempt to justify, separately, a private line rate restructuring of some of these services on cost grounds.

Proposals for specific services in the New York Metropolitan LATA need not be conditioned upon completion of the case record in the ongoing private line generic rate structure case. This in no way abrogates our overall concern that rates for private line services in total -- or for individual non-competitive private line services -- are neither cross-subsidized by basic services nor over-priced, an issue that is being considered in the generic private line case. New York Telephone shall file such studies as may be determined in that proceeding to support their revenue requirements in its future rate proceedings.

Some of the larger independents, such as Rochester Telephone Corporation and ALLTEL, have made similar arguments with respect to the need for private line pricing flexibility. However, the record does not reveal that these companies face the degree of competition that New York Telephone is exposed to in the New York Metropolitan LATA. Nevertheless, these companies may receive flexibility on their private line services where there is a showing that such flexibility is required, and where appropriate interconnection arrangements, if sought by would-be competitors, are provided. New York Telephone will be afforded the same opportunity for its upstate LATAs. Further, where competitors provide dedicated circuits directly to a customer's premise, and a showing can be made that flexibility is needed, we would be willing to consider granting pricing flexibility for central office private line loop facilities.

Switched Carrier Access Services

[13] In this case, Teleport requested the ability to interconnect its fiber optic facilities with New York Telephone central offices through collocation. By this order, this request has been granted for unswitched (private line) services. Teleport's request for switched service will not be granted now. The unbundling of switched access service elements necessary to accommodate such a competitive alternative would result in a significant restructuring of access charges, and NYT's pricing flexibility for switched access is constrained until September 1991 by provisions of the Modification of Final Judgment (48 PUR4th 227, 552 F.Supp. 131). These considerations dictate that we not unbundle switched carrier access charges now. The cost basis for access charges is being reviewed in the generic access charge proceeding, and the issue will be considered further there. After the Modification of Final Judgment restrictions

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are removed in 1991, this market will likely become competitive. We will expand the ongoing access charge proceeding to review our policies for this market.

Local Exchange Company Carrier Access Issues

Local exchange companies are required to provide access to their network to interexchange carriers. In this proceeding, New York Telephone asserted its access service is faced with significant competition. It said that extensive bypass would reduce the usage of its network and that those who continued to use the network would inevitably have to pay higher prices in order to allow New York Telephone to recover its costs.

The threat of uneconomic bypass exists where access rates exceed the actual costs of access in order to provide a contribution to basic exchange service.

Judge Harrison found a need only to price carrier access charges at cost, so that uneconomic bypass would not be fostered. He determined that the local exchange companies continue to have a dominant market share, and that it is thus difficult to justify greater flexibility in setting carrier access rates. This issue has been considered in the access charge proceeding, where we directed the performance of cost studies. It will be reviewed there, after the results of the cost studies become known.

Intra-LATA Toll

[14] [15] The record in this case shows that there is little competition at present, although ATTCOM and the OCCs are permitted to compete with the local exchange companies for intra-LATA toll business. New York Telephone asserted that the intra-LATA toll market is competitive. Judge Harrison was not persuaded. New York Telephone is now by far the dominant provider of service. Therefore, we shall reject New York Telephone's request that the local exchange companies be relieved of regulatory oversight.

Also at issue here is MCI's assertion that competition should be fostered by requiring that New York Telephone impute access charges to itself and offer customers a choice of the intra-LATA carrier to be accessed by "1+" dialing.

The costs and benefits of that action are not developed on this record. Inasmuch as these issues are directly related to our ongoing examination of access charges and intra-LATA toll rates, they will be considered there. In the interim, regulatory procedures in the area of intra-LATA toll services will remain unchanged.

PUBLIC TELEPHONE SERVICE

In 1985, we allowed **COCOTs** to be connected to the network. The Public Service Law limits our authority over **COCOT** providers to the establishment and enforcement of operating rules.

New York Telephone contended that its public telephones face competition from **COCOT** providers. It stated that about 15,000 telephones were furnished by **COCOT** providers in its service territory and that because there were minimal entry barriers, it faced a serious competitive threat.

Judge Harrison found that although the record was not well developed, **COCOT** providers appear to be a competitive force. But he found that New York Telephone

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made no effort to explain how regulation of its telephone service should be reduced in the face of that competition. More broadly, he noted that the public debate that raged for years over the ten-cent coin rate shows that the public has come to regard public telephone service as an important aspect of this system and that, despite lower barriers to entry, there are undoubtedly locations where the public interest is served by the provision of public telephone service but where COCOT providers are not tempted to locate. Thus, the Judge recommended exploring how New York Telephone would act before reducing regulation of public telephone service.

The record here is not well developed. [FN17] A separate proceeding has been instituted to examine these issues in greater detail, with particular concern to insuring both choice and quality of service to end users. [FN18] The regulatory treatment of New York Telephone's own coin service may be considered in another proceeding to be established.

BILLING AND COLLECTION

SERVICES

[16] In our access charge opinion, [FN19] we noted that the Federal Communications Commission had recently detariffed billing and collection service offered to interexchange carriers by local exchange companies. We evaluated their arguments alleging discrimination and the need for a competitive response to other services and concluded that the deaveraging of billing and collection service should await the general deaveraging of access charges.

The issue has been raised again in this case. New York Telephone asserted again the viability of competition and asserted that the service should be deregulated.

Judge Harrison noted that the circumstances appeared not to have changed from the time the access charge opinion was issued and that the record in this proceeding is no more or less compelling than the case for deaveraging made there.

The deregulation of these services does not necessarily serve the public interest. The local exchange companies have a particularly effective and broad reaching billing and collection capability, which has been developed for and funded by ratepayers. That service now has monopoly attributes, such as the bill recording function, and the continually updated customer information data base, which are significant bottlenecks. Therefore, local exchange company provision of billing and collection services will continue to be regulated. We foresee, however, that new network signalling technologies, such as SS-7 and Automatic Number Identification, may broaden the availability of other billing services, and that policy may need to be reevaluated as the market becomes more competitive.

In the meantime, however, greater flexibility may be provided by allowing the local exchange companies to offer billing and collection services through individual billing contracts. Tariffs will still be required to be offered for those portions of billing collection services which use bottleneck facilities. These tariffs may be filed by each local exchange company. If a company introduces a billing and collection service that does not require access to either the monopoly recording function or the use of local exchange company

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customer records, we will entertain a petition to allow it to treat the costs below the line. Costs and revenues of such services shall be recorded as determined in the pending cost allocation proceeding. [FN20] We shall, in any event, review the proposals to insure our responsibilities under the Public Service Law are met. Billing and collection functions will be monitored closely to insure that pricing and operation policies are not used to suppress enhanced service providers or, in instances where local exchange companies offer enhanced services, to skew competition.

OTHER MATTERS

Moratorium Impact

[17] The changes in private line interconnection and pricing policies adopted here were not contemplated when the current New York Telephone rate moratorium was negotiated. Similarly, the reduction of PBX rates through the offering of rate stability plans and the offsetting additional pricing flexibility of Centrex also will change the environment contemplated by the moratorium. We are willing, therefore, to adjust the moratorium for the net impact of these changes. New York Telephone may petition us to recover those amounts. It shall bear the attendant burden of proof.

Procedural Objections

In their briefs on exceptions, several parties raised various objections to the manner in which Judge Harrison conducted the proceeding. The exceptions relate primarily to procedural issues and the Judge's analytical framework.

Although the exceptions are not all recited in this Opinion, we have considered them all and find them uniformly unpersuasive. The Judge conducted the proceeding efficiently and effectively, and the excepting parties' arguments are rejected.

CONCLUSION

The public interest is enhanced by the emergence of competition in the telecommunications industry. The policies articulated above are intended to insure that the transition to competition is done wisely.

The Commission orders:

1. New York Telephone Company shall file, within 60 days of the issuance of this Opinion and Order, tariff leaves providing for non-switched virtual collocated interconnection, as described in the foregoing Opinion.
2. AT&T Communications of New York, Inc. is requested to file a response to the offer of an alternative regulatory plan within 60 days of the issuance of this Opinion and Order.
3. To the extent it is consistent with this Opinion and Order, the recommended decision of Administrative Law Judge J. Michael Harrison, issued May 9, 1988, is adopted as part of this order. Except as here granted, exceptions to the recommended decision are denied.

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4. New York Telephone Company may file revisions to its tariffs to effect the Commission's decisions concerning Private Branch Exchange rates, as described in the foregoing Opinion.

5. This proceeding is continued.

APPENDIX A, Parties Filing Briefs to the Commission, pp. 18-19.

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

APPENDIX B, ALTERNATIVE STATE SPECIFIC REGULATORY PLAN FOR ATTCOM-NY, (AFTER CURRENT MORATORIUM EXPIRES), pp. 20-21.

TABULAR OR GRAPHIC MATERIAL SET FORTH AT THIS POINT IS NOT DISPLAYABLE

SCHWARTZ, Commissioner, Concurring:

This highly significant opinion is, at one and the same time, ground-breaking and precedented. It breaks ground because it advances competition in the local exchange area, by "invading" the central office. It is precedented because it represents one more step in a series of decisions taken by the New York Public Service Commission to promote efficiency in the provision of telecommunications services, recognizing that the best way to achieve and preserve efficiency is through competition. [FN1]

Of course, conditions in New York State, owing to the concentration of large users in New York City, contrast markedly with those in other parts of the country. It is the very density of these users, combined with their high usage volume, that has made it possible for competitors to challenge New York Telephone Company in the provision of private line service, and has permitted the substantial growth of competition with Centrex. The minimum scale required for firms to contest the incumbent monopoly is not yet known, but by this opinion, the Commission is acknowledging contestability in other markets within the state as well.

[ix] Moreover, no service -- basic or non-basic, large or small user -- should be considered permanently non-competitive, and we should strive to break down barriers and eliminate bottlenecks as much as possible whenever and wherever they occur. Conceivably, some of the so-called non-competitive services could become competitive as rates now below cost rise to cost. The objective of regulation in communications, in my view, should be to follow where competition exists, to get out of the way where it might exist but doesn't, and even to lead competitors to the market if feasible and if in the public interest.

This does not mean, however, that the Commission should view its responsibility as that of unravelling the network that is now in place, simply because it may be technically feasible to do so. An enormous amount of sunk investment exists, much of which has a long useful life ahead of it. This plant and equipment purchased for monopoly service provision must be paid for, and if monopoly services are to utilize newer, more technologically advanced equipment along with competitive services, then ratepayers must contribute to recovering a fair share of those costs as well. Thus, cost allocation issues, which were not a principal focus of the instant proceeding, will become ever more critical in the future. Once rules have been set for allocating costs, it should be easier to

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determine what investments are economic, when they are to be jointly used by competitive and monopoly services. And that in turn should help to compensate the telcos for lost contribution, even as all costs are gradually translated into economic prices.

Regarding expectations for the future, it seems clear that the Commission must evaluate not only the structure of the industry, but also the behavior of the players. For example, should the telephone companies make wider use of market research techniques normally used by competitive firms, that itself will be an indicator that they do face robust competition. And we might make more sophisticated use of structural measures such as concentration, market share, etc. Not only do they give clues as to whether a firm can face effective competition; they also, when analyzed in conjunction with other industry variables, such as demand growth, tell us something about pace, and something about anomalies. It may be that an industry segment theoretically could be competitive but is not showing much change in these structural variables. Then we would ask why, and whether regulation is really the problem. In other words, this opinion by no means closes the competition issue, and the Commission should, in my judgment, initiate an ongoing effort to gauge the potential as it develops in many services and many geographical areas.

While it may well be that many intra-LATA services, owing to engineering and technical considerations, may never be subject to competition unless the LECs are grossly inefficient and incompetent, the jury is still out regarding the dimensions of the natural monopoly. Rather than consider which elements of the telephone company operations are subject to competition, the Commission should now focus on determining which elements are NOT subject to competition.

One way to advance this effort would be to encourage market tests. In such a volatile environment, it seems that only trials can enlighten us as to the potential for durable competition. We have ordered trials in other proceedings (such as the ISDN). I would like similar trials ordered for intra-LATA equal access. And I would like to see the Commission deliberately search for and assist in the design of other viable trials.

In numerous ways, the transitions from monopoly to competition and from rate-base, rate-of-return regulation to incentive regulation [FN2] mean that the Commission is engaging in a process of mediating among competitors. We are not enthusiastic about doing so, but it may not be possible to avoid it, if incumbents resist feasible proposals to make competition a reality, and if they want to see some of their services deregulated. However, we certainly have to watch out for gaming behavior on the part of the incumbent and the upstart.

The balancing that is required in moving towards competition involves an ongoing assessment of whether the risk of gains is larger than the risk of losses. In concurring in the caveats expressed in this opinion, I wish to make the economist's argument that the magnitude of hardship caused to any class of ratepayers receiving a subsidy under current regulatory practice must be considered in a comparative light. Moreover, short-term losses, such as customer confusion, should not be interpreted as long-term losses. Our primary goal with respect to consumers should be to educate them to the benefits of a system that is not really as foreign to them as they may at first believe.

A final point is worth noting. The practices of a state regulatory commission are defined by law and custom. But they are not conducted in a vacuum, and this Commission has played an exemplary role in helping to shape the national legal

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and policy framework within which the Federal Communications Commission, which also has congressionally mandated jurisdiction over regulation of common carriers, operates. But our role has been and should continue to be defined by priorities that derive from our fundamental jurisdiction and legal responsibilities, not, tempting as it may be, from more generalist concerns over which we have no authority.

This will be challenge enough, for the relevant environment is far from static, and even as this opinion is being written, the U.S. Congress has undertaken to explore once again the dimensions of its role in setting national policy. Among the issues it is considering legislating on are the restrictions against entering certain lines of business imposed on the Bell Operating Companies by the Modification of Final Judgment in 1982 (48 PUR4th 227, 552 F.Supp. 131). The New York Department of Public Service commented formally in the first triennial review of these restrictions, and is expected to comment once again in the second triennial review in 1990. I personally favor removal of the bans on information service content and manufacturing under a federal initiative allowing states to submit plans for control of monopoly abuses. Recognizing that this view may run into all sorts of obstacles, legal and political, and may not necessarily be supported by the Commission as a whole, I am sure all will agree that we must take note of and participate vigorously in this great national debate, which promises to radically change the context of state regulation. It is the states that have and should retain the major responsibility for implementing policy changes that primarily affect the bottleneck -- such as Open Network Architecture, the functional prerequisite for a full market test of the possibility of vigorous competition in information services.

This opinion, juxtaposed with previous orders enumerated above, our recent ONA order that invites enhanced service providers to seek acceleration of the unbundling planned by New York Telephone Company, our ISDN order, and our comments and filings before the FCC and the courts, comprise a holistic and anticipatory approach to regulation in this vital and essential communications arena, which, I trust, will not end here.

NOAM, Commissioner, Concurring:

I am pleased with our decision in this case, which should enhance competition in the provision of telecommunications services and benefit the people and economy of New York. Opening the market to new entrants and reducing regulatory restrictions should continue to be the Commission's policy direction, and hopefully in a fast-paced process. Having now lowered barriers to competition and encouraged network pluralism, we should focus on the next set of issues, continuing a process in which we are already engaged. Beyond the traditional and important goals that we must continue to pursue, such as consumer protection, universal service, and service quality, we must address new issues which include:

[x] 1. Telecommunications as economic competitiveness policy. The global competitiveness of U.S. and New York economy are directly related to the state of telecommunications. Other nations and financial centers are actively using telecommunications as a strategic tool. Given foreign firms' frequent advantages in mass production manufacturing, the only way to compete is to stay ahead in information content, process intelligence, and innovation. The upgrade of the

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network system is hence of major importance to the economic efficiency and growth of information intensive industries. ISDN, broadband networks, fiber in the loop, and intelligence in the network are building blocks in this upgrade. We should encourage experimentation, innovation, infrastructure investments, and a more rapid pace of planning. Our ISDN policy initiative and incentive-based regulation are examples.

[xi] 2. Treatment of telephone carriers in their expanding capacity as mass media providers. As networks provide pathways for mass announcement services and move technologically towards video transmission, it becomes essential to clarify their status. Should they operate as publishers and select programs under their own responsibility, or as common carriers that must be neutral as to lawful content, use, and users? Traditionally, common carrier principles have governed telephony, in contrast to cable television or broadcasting, and have served well as a foundation for an expansion of the telephone's scope and use, while insulating carriers from legal liability and threats by economic and political pressure groups. It would take strong arguments to overturn this principle for video transmission services. The Commission should, in the near future, deal with these issues.

[xii] 3. Protection of interconnection and access. In coming years policy makers must structure ways in which network interconnection is granted, defined, priced, and technically harmonized to provide mutual interaction among the increasingly large number of members of the network family. The open network architecture concept is a step in that direction, and one in which state regulators should play a constructive role. The PSC, in its own ONA proceeding, has begun to deal with this set of issues, with the aim of defining a constructive state policy that is not purely jurisdictional in focus.

4. Protection of a balance between technical standardization and diversity. As the number of members of the network family and their sophistication increases, the need for standards and protocols becomes ever more important if we wish to avoid a technical fragmentation of the American network just at a time when Europe is moving in the opposite direction, and just when our technical competitiveness is challenged as never before in this century. There is need for a system in which competitive diversity can be exercised within a defined technical compatibility. There is a need for government to assure -- though not necessarily set -- timely standards, protocols, and definitions, in collaboration with industry. Since there is a strong need for national compatibility, such leadership must be exercised in Washington, but in consultation with the states where local service is affected. In particular, it is necessary is [sic] to establish a blueprint for a modular concept of the network system, with well-defined interface points and standards. This would enhance compatibility, competitiveness, and flexibility in structuring new services by local exchange carriers, other network providers, manufacturers and users. It is necessary for a state like New York to establish expertise in this field and to encourage the federal level of government to become more active in standards issues than in the past.

5. Protection of the viability of the core network and establishment of alternative mechanisms of social support. The emerging pluralistic network system makes it increasingly difficult to maintain traditional internal transfers from one class of users to another. This does not spell the end of transfers as such. There are still reasons to support services for rural areas,

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the infirm, or for the truly needy. Keeping such subscribers on the network, in addition to meeting standards of fairness, also benefits the rest of society by providing greater value to its telephone service. A lifeline program such as the one established by the PSC permits a better targeting of the subsidy than in the past, and creates the ability to take greater deregulatory risks by providing a social safety net. Yet support should not come solely from the subscribers to the local exchange companies. A universal service fund could provide a mechanism to deal with this issue.

[xiii] 6. The prevention of oligopolistic behavior and of cyclical instability. A pluralistic network system is likely to have excess capacity. Given low marginal cost and high fixed costs, competition may cause either cyclical instability and/or oligopolistic price coordination by firms. This is most likely where the number of competitors is very small, such as in the provision of cellular telephone network services. It is therefore important for regulators, beyond being vigilant to instances of price collusion, to foster potential alternatives such as resellers which would reduce oligopolistic temptations.

7. Establishment of policy to match the global scope of networks. As national and state governments lower barriers in telecommunications, the emerging network system will not stop at the national frontier. Telecommunications will transcend the territorial concept and specialized international networks will become increasingly important. As the cost of international transmission drops dramatically and as the volume of international transaction rises, no country, and certainly no single U.S. state, can be a regulatory island anymore. The challenge for New York's regulation is how to frame rules in such a complex international environment, how to develop an understanding for the broader environment of telecommunications, and how to participate in an already complex process of international telecommunications policy. For a state with as vast an international level of activities as New York, it is imperative to ensure that policies in the international field maintain or enhance the role of New York as an international marketplace and center for the new types of international networks.

All of these issues will, no doubt, lead to significant regulatory controversies and will occupy us for a long time. None of these tasks is beyond our grasp in terms of complexity or political feasibility. But they require us to take the next steps in dealing with the new issues of a pluralistic network environment.

FOOTNOTES

FN1 Case 29469, Order Instituting Formal Proceedings, Oct. 22, 1986 (N.Y.P.S.C.).

FN2 Re Lifeline Rates, Cases 28961, et al., Opinion No. 85-12, May 9, 1985 (N.Y.P.S.C.).

FN3 The statute is codified at s5(3) of the Public Service Law.

FN4 For example, if licensed cellular companies engage in price squeezing tactics to eliminate or disadvantage cellular resellers, we will consider

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regulating them again to the extent necessary to maintain a competitive market.

FN5 The FCC has required Bell Operating Companies that provide cellular service to do so through a separate subsidiary.

FN6 All telephone corporations engage in resale to some extent; however, some of these firms provide no regulated telecommunications services other than the resold services. The term reseller, when used in this Opinion, refers to the latter circumstance. This serves to distinguish these firms from other non-dominant carriers that may also engage in resale activity to a certain extent.

FN7 A company operating as a reseller in one area could be a facilities-based carrier in another.

FN8 Case 27946, Order, Feb. 22, 1989 (N.Y.P.S.C.).

FN9 Case 88-C-102.

FN10 ATTCOM has agreed to a rate moratorium and has some pricing flexibility. It is also permitted to retain half of any profits it achieves over its target earnings, as an incentive to efficiency.

FN11 Including, among others, MTS, Cross State Service, directory assistance, and operator services. We intend to review at the plans' inception those prices to insure that they result in a reasonable return for ATTCOM.

FN12 We recognize that our decision in the access charge case contemplates the deaveraging of interexchange carrier access charges, if the cost studies to be performed by the local exchange companies so warrant. That action, in turn, may require ATTCOM to deaverage its intrastate toll rates.

FN13 The plan is outlined in Appendix B.

FN14 Case 88-C-063.

FN15 Case 88-C-004.

FN16 R.D., p. 167.

FN17 It is not clear, for example, how deregulation would affect the COCOT market and ratepayers. We are also concerned about maintaining coin service in some uneconomic locations and insuring access to 911 service.

FN18 Case 27946, Order, Feb. 22, 1989 (N.Y.P.S.C.).

FN19 Case 28425, Access Charges, Opinion No. 87-11, mimeo pp. 139 et seq., June 11, 1987 (N.Y.P.S.C.).

FN20 Case 88-C-136, Order Adopting Interim Cost Separation Standards and Requesting Comments on Proposed Standards, Sept. 28, 1988 (N.Y.P.S.C.).

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SCHWARTZ, Commissioner, Concurring

FN1 These decisions date back more than 15 years, beginning with the decision to allow interconnection of customers' own premise equipment, which antedated the federal action to do the same. There followed the deregulation of inside wire, the permission for intra-LATA toll competition, and flexible pricing under incentive regulation for both local exchange carriers and ATTCOM (the so-called moratoriums on general rate cases). And even in non-competitive areas, we have been moving towards cost-based pricing that contributes to efficient markets. To that end, we required removal of fixed costs from access charges, and brought about New York Telephone Company toll rate reductions thereby.

FN2 Our incentive regulation approach requires that profits above a prescribed level be shared 50%/50% between stockholders and ratepayers. Companies are now allowed to keep all profits up to and somewhat above a traditionally determined target rate of return. Whether experience will show either that this split is not necessary or that the indexed price cap with a predetermined productivity factor, a la the British and FCC model, is superior, it is too soon to say. Sharing is a fail-safe mechanism that ensures benefits to consumers should soaring profits result from this regulatory practice, and as such, is just and economically reasonable. It might not always be the best mechanism, and experience with incentive regulation will indicate whether it is.

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