COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN INQUIRY INTO INTER- AND INTRALATA INTRASTATE COMPETITION IN TOLL AND RELATED SERVICES MARKETS IN KENTUCKY	))))	ADMINISTRATIVE CASE NO. 273

O R D E R

On May 25, 1984, the Commission issued an Order authorizing the introduction of interLATA, intrastate competition in Kentucky. On June 14, 1984, GTE Sprint Communications Corporation ("GTE Sprint") filed an application for rehearing, seeking modification of or further hearing with respect to the deferral of facilities-based intraLATA toll competition in Kentucky, and provisions requiring that Other Common Carriers ("OCCs") bill completed unauthorized intraLATA calls at the tariffed rate of the certificated intraLATA carrier. On this same date, MCI Telecommunications Corporation ("MCI") and Western Union Telegraph Company ("Western Union") filed an application for rehearing of the Commission's decision to defer the introduction of intraLATA competition. Also on June 14, 1984, AT&T Communications of the South Central States, Inc., ("ATTCOM") requested rehearing on the issues of the proper regulatory environment of ATTCOM, the differential operating authorization of Wide Area Telecommunications Services ("WATS") resellers vis-a-vis facilities-based interexchange carriers, and the requirements concerning advertising

the limitations on intraLATA competition. ATTCOM also proposed to file a supporting memorandum after the 20-day period allowed for rehearing applications had elapsed. On June 20, 1984, the Commission issued an Order denying ATTCOM permission to file this material late.

On June 22, 1984, ATTCOM filed a memorandum in response to the rehearing applications of MCI, Western Union and GTE Sprint (hereinafter "ATTCOM Memorandum") which, among other things, endorsed the requests of these applications for rehearing of the deferral of intraLATA competition and provisions relating to the restrictions of intraLATA calling. On June 28, 1984, MCI filed a Motion to Strike the ATTCOM Memorandum as an unauthorized pleading on the ground that the ATTCOM Memorandum was not a response but rather contained the substance of ATTCOM's anticipated memorandum in support of its Application for Rehearing.

On June 29, 1984, the Attorney General's Consumer Protection Division ("AG") filed responses to the ATTCOM, GTE Sprint and MCI and Western Union Applications for Rehearing. The AG's response urged the Commission to generally deny ATTCOM's application for rehearing, although agreeing with ATTCOM that enforcement of the prohibition against intraLATA toll calling required further study. Regarding the MCI and Western Union application, the AG posed no objection as long as a rehearing regarding the appropriate means to enforce the prohibition on intraLATA competition was not used as a vehicle to relitigate the issue of whether any restrictions should be imposed upon toll competition within Kentucky. Similarly, the AG opposed the GTE Sprint

application seeking rehearing on the issue of the deferral of facilities-based intraLATA toll competition while not opposing the granting of rehearing concerning the appropriate mechanism for prohibiting intraLATA calling.

Deferral of IntraLATA Competition

GTE Sprint has petitioned the Commission for modification or rehearing of the decision to defer the introduction of intraLATA competition. In its response memorandum, ATTCOM has supported GTE Sprint in this request, with the proviso that statewide authority be granted all interexchange carriers. After careful consideration of the arguments advanced in support of these requests, the Commission is of the opinion that rehearing on this issue should be denied.

GTE Sprint contends that the decision to defer facilities-based intraLATA competition was based primarily on the possible threat intraLATA competition would pose to universal service objectives and the revenues of local exchange carriers. GTE Sprint further contends no factual evidence exists in the record to warrant such concern. However, examination of the record reveals that no quantitative or "hard" evidence was introduced to demonstrate these adverse effects of allowing intraLATA competition would not occur. Indeed, since significant toll competition has not heretofore existed in this state, little or no factual evidence is available to support any position on this issue. Therefore, the Commission has had to rely in large measure on the statements of expert witnesses. Clearly, in these circumstances,

the Commission must use its informed judgment to carefully weigh the available evidence.

As emphasized in the Order of May 25, 1984, the lack of reliable evidence concerning the viability and consequences of toll competition in Kentucky was a factor in the decision to defer intraLATA competition while allowing interLATA competition. This will give the Commission and the telephone companies the opportunity to gain reliable experience with toll competition in Kentucky. GTE Sprint's petition contains nothing indicating the Commission erred in its conclusion that competition has yet to be shown to be an effective regulator of toll telecommunications markets in Kentucky. Further, the petition does not challenge the Commission's conclusion that only actual operating experience under an access charge environment with at least some equal access will adequately resolve this issue.

The Commission has elected to initially make the potential but unproven benefits of facilities-based toll competition available to the citizens of Kentucky in the market where viable competition is most likely to flourish--the interLATA market. In its petition, GTE Sprint expresses the opinion that, ". . .the same considerations which led the Commission to approve interLATA competition are applicable to the intraLATA market."[1] In its memorandum, ATTCOM concurs in this judgment. However, the evidence of record indicates these two markets are distinct, with important differences that lead to a differential likelihood of

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[1]Application for Rehearing of GTE Sprint, p. 5.

success of competition. According to Cincinnati Bell, "Logic suggests that the long haul traffic between major interLATA areas would be the primary target of competition for toll markets."[2] There is nothing in the record to refute such logic; indeed several of GTE Sprint's own statements support it.[3] The Commission therefore disagrees with the opinion expressed in GTE Sprint's petition, and remains convinced it is entirely appropriate to authorize full facilities-based competition first in the market generally acknowledged to be most conducive to a competitive structure.

GTE Sprint does not appear to challenge the Commission's finding that significant public benefits will not be lost as a result of deferring facilities-based intraLATA competition. However, GTE Sprint finds this position to be inconsistent with concerns regarding the impact of intraLATA competition on the revenues of local exchange carriers. It is the opinion of the Commission that the two conclusions are entirely consistent. Based on the evidence of record it is apparent that penetration of the intraLATA market by OCCs will initially be relatively limited in scope, largely due to the preponderance of lower density short haul traffic routes in this market. However, at the same time, it can be expected that the OCCs would very selectively operate on the most lucrative intraLATA routes, thus

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[2]Cincinnati Bell's response to Commission Order dated July 19, 1983, p. 14.

[3]See, for example, Application for Rehearing of GTE Sprint, the last sentence beginning on p. 4.

potentially diverting substantial revenues away from exchange carriers. From the standpoint of the body of Kentucky's telecommunication users as a whole, this type of selective competition is not desirable. One motivation for deferring intraLATA competition is to give the OCCs time to demonstrate that they will initiate facilities-based service on a widespread basis in the interLATA market, rather than serving select routes. As indicated in the May 25, 1984, Order, this is an important concern of the Commission, and the development of the route structure of the OCCs will be observed carefully. Competition will not be successful if the OCCs provide service solely on a small number of select routes. The Commission encourages the OCCs to concentrate their efforts on developing as complete a service offering in Kentucky's interLATA toll market as possible. By doing so it can be demonstrated that allegations of "cream skimming" in Kentucky's intrastate toll markets are unfounded.

The Commission would like to make it clear that, contrary to the assertions of GTE Sprint, the decision to defer intraLATA competition did not turn on the issue of whether the revenue streams of local carriers would be jeopardized by the introduction of intraLATA competition. The public interest issues involved are considerably broader than this. For example, the Commission has been required to make a judgment concerning whether or not toll is a natural monopoly. If the evidence had clearly indicated toll is a natural monopoly, it would not have been in the best interests of Kentucky's citizens to authorize any toll competition intrastate. This conclusion would hold true

even if it could be demonstrated competition would not pose a threat to the finances of any local exchange carrier.

Another major concern of the Commission, cited in the Order, is the differential impact the introduction of toll competition will likely have on various geographic regions and customer groups in Kentucky, irrespective of the impact on the revenues of exchange carriers. This point was succinctly and aptly summarized by Allied Telephone Company of Kentucky, Inc., in response to a question concerning the effects of permitting competition in intrastate markets:

> The net result is that the general body of ratepayers is usually disadvantaged, at least to some degree, while a relatively select group of users is definitely advantaged.[4]

It is a responsibility of this Commission to consider the interests of all citizens of the state in its decisions, particularly those groups or individuals that would be negatively affected by a Commission decision. The Commission has concluded that it must manage the transition to a more competitive telecommunications industry in a manner that will minimize negative consequences to any group of consumers. It will take time to observe the impact of competition, to determine what steps may be necessary to alleviate negative consequences, and to devise methods to do so. In sum, the issue of the impact of competition on exchange carriers has been a consideration in the Commission's

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[4]Comments of Allied Telephone Company of Kentucky, Inc., in response to Commission's July 19, 1983, Order in Case No. 8873, the record of which was incorporated by reference in this proceeding by Order dated January 10, 1984.

decision, but by no means is it the only one nor the most important one, as GTE Sprint apparently believes.

GTE Sprint further contends the Commission failed to fully consider statements made by Dr. Michael Pelcovits, witness for MCI, and Dr. Ben Johnson, witness for the AG, in its deliberations concerning intraLATA competition. The Commission has, in fact, given adequate weight to the testimony of these two witnesses. It should be noted that in making this assertion, GTE Sprint is asking the Commission to rely solely upon the type of "unsubstantiated statements" it previously criticized the Commission for relying upon regarding the potential consequences upon local exchange carriers cited by the Independent Group. Both statements are opinions which are unsupported by any "factual evidence." It is clear neither witness made a categorical statement, and each was careful to avoid the impression of offering an unqualified answer.

GTE Sprint is also in error in the interpretation that has been placed upon the statements of these two witnesses. The statements referenced by GTE Sprint were made in response to questions concerning a possible or actual differential in the access charges paid by the OCCs and ATTCOM. The strongest construction that can reasonably be placed upon their testimony with regard to the impact of toll stimulation is that it could be sufficient to offset access charge revenue lost to exchange carriers due to discounted access charges paid by OCCs. Neither witness made statements that could be construed as testimony that toll stimulation would be of such a magnitude that resultant access

charge revenues would equal the toll revenues of exchange carriers lost to toll competitors. Only if this were true would revenue streams of exchange carriers not be adversely affected by competition.

In the petition for rehearing, GTE Sprint reasons that the lack of opposition by South Central Bell Telephone Company ("Bell") to intraLATA toll competition is evidence that such competition would not entail negative effects on exchange carriers. GTE Sprint's conclusion in this regard is in error. It does not follow from the fact that intraLATA competition might not impact negatively on the finances of Bell that other carriers would not be adversely affected. Additionally, with the exception of Bell, all other local exchange carriers participating in this proceeding opposed the introduction of intraLATA toll competition at this time.

Finally, GTE Sprint complains of the lack of a firm time frame for introducing facilities-based intraLATA competition, apparently citing the possible encouragement of bypass activity. However, GTE Sprint has not attempted to present arguments or evidence to alter the Commission's view that a deferral of reasonable length will not unduly encourage bypass activity, and has not provided a date certain by which the Commission will have sufficient information to decide whether or not to permit intraLATA competition. The Commission continues to agree with the statement of MCI witness, Dr. Pelcovits, that,

> . . .to the extent that there is. . .information like that [intraLATA competition being deferred rather than prohibited] available to people --

they'll make use of it and that will minimize potential harm [from bypass].[5]

Restriction of Unauthorized IntraLATA Calling

MCI and Western Union and GTE Sprint request modification or rehearing of provisions in the May 25, 1984, Order relating to the billing of unauthorized intraLATA toll calling. The major substantive arguments cited as justification for rehearing include issues of technical feasibility, cost considerations, the possible billing of interLATA and/or interstate toll calls at intraLATA rates, and the inability to precisely match the distance component of established carriers' intraLATA toll rates.

In a memorandum filed in response to the applications of MCI and Western Union and GTE Sprint, ATTCOM voiced several criticisms of the provisions dealing with unauthorized intraLATA calling. ATTCOM expressed the opinion that either blocking of such calls, or requiring the OCCs to terminate service to customers who persistently place unauthorized intraLATA calls, would be preferable.

ATTCOM initially petitioned the Commission for rehearing with respect to the requirement that ATTCOM advertise its lack of authorization to handle intraLATA traffic. This request was reiterated in ATTCOM's response to the applications of MCI and Western Union, and GTE Sprint. The Commission is of the opinion that the issues of advertising and customer information in this regard are related to the issue of restricting unauthorized

[5]Transcript of Evidence ("T.E."), March 8, 1984, p. 62.

intraLATA calling. Both arise from the simultaneous allowance of interLATA toll competition and deferral of intraLATA toll competition. These issues are closely interwoven, and decisions made in one can influence the outcome in the other. Therefore, the Commission finds that these should be treated as different aspects of a single general issue upon which rehearing will be granted.

The Commission is further of the opinion a formal conference should be held prior to rehearing. This will facilitate efficient investigation into the rather complex technical issues involved, and allow all parties ample opportunity to evaluate and present views on alternative solutions to this problem.

WATS Resale

ATTCOM has petitioned the Commission to reconsider authorization for statewide resale of WATS. In its application, ATTCOM stated, "WATS resellers should not be given the unwarranted competitive advantage of providing statewide service while other interexchange carriers, including AT&T Comunications, are limited to interLATA services only." However, ATTCOM in its petition failed to provide either new arguments and/or new evidence bearing on resale of WATS. ATTCOM has apparently attempted to rectify its original application deficiency with its June 22, 1984, filing. In fact, neither MCI nor GTE Sprint addressed the issue of Resale of WATS in their applications for rehearing. Therefore, it is the Commission's opinion that it is inappropriate for ATTCOM to supplement its application for rehearing on WATS resale with its June 22, 1984, filing. The Commission also

notes that MCI's Motion to Strike inaccurately states that this issue is the one exception to MCI's complaint that ATTCOM's Memorandum does not substantively address either the MCI or GTE Sprint applications. Thus, the Commission will only consider ATTCOM's original application on this issue.

In Administrative Case No. 261, An Inquiry into Resale of Intrastate Wide Area Telecommunications Services, the Commission authorized statewide resale of WATS effective September 2, 1983. The Commission found in that proceeding that the resale of WATS would provide positive benefits to the telecommunication consumers of Kentucky. There has been no new evidence introduced in this proceeding to show that the original Order permitting statewide resale of WATS is inappropriate, nor has ATTCOM provided new evidence to show that the Commission's resale decision is not consistent with the overall intent of this Order. The Commission concurs with the AG witness, Dr. Ben Johnson, that the development of an active resale market could serve to facilitate the growth of the facilities-based carriers.[6] Thus, the Commission is of the opinion that statewide resale of WATS will result in more effective competition in the telecommunications market, providing benefit to a greater number of Kentucky consumers. Therefore, the Commission rejects ATTCOM's petition to rehear the issue of statewide resale of WATS.

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[6] T.E., March 8, 1984, pp. 173-176.

Relaxation of Regulatory Oversight of AT&T Communications

ATTCOM has requested the Commission to allow rehearing in order to ". . .make some allowances to transition AT&T Communications to a more relaxed regulatory environment." ATTCOM proposes that regulation be reduced ". . .with regards, initially at least, to price reductions and new service offerings. . .." ATTCOM failed to fully specify why this issue should be reheard and did not produce any argument, new evidence, or raise questions of Commission error or misjudgment in support of its application. Instead, ATTCOM desired to file a memorandum in support of the application after the statutory period prescribed for seeking rehearing pursuant to KRS 278.400. The Commission declined permission to do so. Subsequently, in a response to GTE Sprint's request for rehearing of the deferral of intraLATA competition, ATTCOM attempted to elaborate upon its request for relaxation of regulation. This elaboration injects arguments concerning the desirability of altering Commission regulation of ATTCOM into a memorandum ostensibly addressed to the intraLATA deferral issue. This constitutes an improper use of the opportunity to respond to a party's rehearing application. Therefore, arguments contained in the response memorandum concerning regulation of ATTCOM have not been considered by the Commission. Based on ATTCOM's application filed June 14, 1984, the Commission finds that rehearing on the issue of relaxing regulation of ATTCOM at this time should be denied.

FINDINGS AND ORDERS

The Commission, having considered the evidence of record and being advised, is of the opinion and finds that:

1. In accordance with the above discussion, GTE Sprint's Application for Rehearing should be granted in part and denied in part as specified in the above sections of the Order.

2. In accordance with the above discussion, MCI and Western Union's Application for Rehearing should be granted as specified in previous sections of this Order.

3. In accordance with the above discussion, ATTCOM's Application for Rehearing should be granted in part and denied in part as specified in the previous sections of this Order.

4. In accordance with the above discussion, MCI's Motion to Strike Unauthorized Pleading should be granted to the extent previously described herein.

IT IS THEREFORE ORDERED that GTE Sprint's Application for Rehearing be and it hereby is granted in part and denied in part as previously indicated.

IT IS FURTHER ORDERED that MCI and Western Union's Application for Rehearing be and it hereby is granted.

IT IS FURTHER ORDERED that ATTCOM's Application for Rehearing be and it hereby is granted in part and denied in part as previously indicated.

IT IS FURTHER ORDERED that MCI's Motion to Strike Unauthorized Pleading should be granted to the extent previously indicated.

IT IS FURTHER ORDERED that the rehearing requests granted herein shall be heard at a hearing to be held on August 2, 1984, at 1:30 p.m., Eastern Daylight Time, at the Commission's offices in Frankfort, Kentucky, to be preceded by a formal technical conference to be held on July 20, 1984, at 9:00 a.m., Eastern Daylight Time, at the Commission's offices in Frankfort, Kentucky.

Done at Frankfort, Kentucky, this 5th day of July, 1984.

PUBLIC SERVICE COMMISSION

Chairman

Vice Chairman

Commissioner

ATTEST:

Secretary