

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

THE SALE AND DETARIFFING OF )  
EMBEDDED CUSTOMER PREMISES ) ADMINISTRATIVE  
EQUIPMENT ) CASE NO. 269

O R D E R

Introduction

This Order concerns the deregulation and detariffing of embedded mobile telephone and paging equipment. Such action is the result of various decisions made by the Federal Communications Commission ("FCC") with which this Commission must concur.

Discussion

Mobile Telephone Equipment

On April 28, 1983, the FCC released a Notice of Proposed Rulemaking ("NPRM") in CC Docket No. 83-372, Deregulation of Mobile Customer Premises Equipment ("Mobile Telephone Inquiry"), proposing to deregulate mobile telephone equipment. The FCC suggested that deregulation of mobile telephone equipment would be consistent with the deregulation of customer premises equipment initiated in CC Docket No. 81-893, Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services ("Second Computer Inquiry"), and would encourage the development of competition in the mobile telephone equipment market.

Subsequently, on November 7, 1983, the FCC released an Order in the Mobile Telephone Inquiry that deregulated mobile telephone equipment on a bifurcated basis and preempted state regulation of mobile telephone equipment. New mobile telephone equipment was deregulated effective January 1, 1984, and defined to include mobile telephone equipment "acquired by a carrier or manufactured by an affiliated entity after January 1, 1984...."<sup>1</sup> Embedded mobile telephone equipment was not deregulated, pending development of a detariffing plan.<sup>2</sup>

Concurrent with the deregulation Order in the Mobile Telephone Inquiry, the FCC issued a further NPRM requesting comment on whether the procedures outlined in the Second Computer Inquiry should apply to the detariffing of embedded mobile telephone equipment.<sup>3</sup>

On December 29, 1983, the FCC released another Order in the Mobile Telephone Inquiry that addressed an emergency petition filed by the American Telephone and Telegraph Company ("AT&T") and

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<sup>1</sup> CC Docket No. 83-372, Mobile Telephone Inquiry, Federal Register, December 6, 1983, page 54620, at paragraph 9.

<sup>2</sup> Embedded mobile telephone equipment was defined to include "existing in-place equipment or inventory which is tariffed or otherwise subject to the jurisdictional separations process'..." Ibid.

<sup>3</sup> CC Docket No. 81-893, Second Computer Inquiry, Federal Register, June 29, 1983, pages 29891-29917. In this NPRM, the FCC outlined procedures for detariffing embedded customer premises equipment and ordered that embedded customer premises equipment be detariffed no later than December 31, 1987.

required AT&T to transfer to AT&T Information Systems embedded mobile telephone equipment.<sup>4</sup>

Subsequently, on June 29, 1984, the FCC released an Order in the Second Computer Inquiry establishing requirements for the detariffing of embedded mobile telephone equipment. The Order established a transition plan involving AT&T in which state commissions have no role. In the case of independent telephone companies and radio common carriers, the Order specified that embedded mobile telephone equipment "owned by the Independent telephone companies or the radio common carriers shall be removed from tariff regulation not later than January 1, 1985....,"<sup>5</sup> and that "state commissions shall have authority to establish the rules under which the installed mobile CPE [customer premises equipment] owned by the Independent telephone companies or the radio common carriers shall be valued for purposes of its removal from regulated service."<sup>6</sup>

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<sup>4</sup> CC Docket 83-372, Mobile Telephone Inquiry, Federal Register, January 6, 1984, pages 882-886.

<sup>5</sup> CC Docket 81-893, Second Computer Inquiry, Federal Register, July 6, 1984, page 27754, Summary. As indicated at footnote 3, the FCC had proposed that embedded customer premises equipment be detariffed no later than December 31, 1987. However, in the case of embedded mobile telephone equipment, the FCC concluded that sufficient competition exists in the mobile telephone equipment market to justify an earlier detariffing date. Ibid., pages 27759-27760, at paragraphs 27-30.

<sup>6</sup> Ibid., page 27754, Summary, and pages 27760-27761, at paragraphs 32-34.

### Paging Equipment

Also, in the deregulation Order in the Mobile Telephone Inquiry, the FCC addressed the issue of whether paging equipment had been deregulated as part of its action in the Second Computer Inquiry. The FCC affirmed that paging equipment had been deregulated. However, as a result of apparent uncertainty among radio common carriers, the FCC indicated that it would not impose sanctions on those radio common carriers who had not detariffed new paging equipment and modified its definition of embedded paging equipment to allow some new paging equipment to be classified as embedded paging equipment.

The FCC had intended that new paging equipment be deregulated effective January 1, 1983, concurrent with the deregulation of other customer premises equipment. Embedded paging equipment was not deregulated, pending development of a detariffing plan. The FCC allowed paging equipment acquired between January 1, 1983, and January 1, 1984, that had not been detariffed effective January 1, 1983, to be rated as embedded paging equipment<sup>7</sup> and, later, made the detariffing of embedded paging equipment subject to the same guidelines as apply to the detariffing of embedded mobile telephone equipment.<sup>8</sup>

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<sup>7</sup> That is: "All paging equipment that is acquired or put into service now through January 1, 1984, may be treated as new or embedded CPE, at the discretion of the carrier." CC Docket No. 83-372, Mobile Telephone Inquiry, Federal Register, December 6, 1983, page 54621, at footnote 10.

<sup>8</sup> CC Docket No. 81-893, Second Computer Inquiry, Federal Register, July 6, 1984, page 27754, at footnote 1.

On January 30, 1985, the Commission entered an Order in this case detariffing embedded mobile telephone and paging equipment, effective January 1, 1985, and establishing a valuation standard for removing embedded mobile telephone and paging equipment from regulated books of account.

On February 19, 1985, General Telephone Company of Kentucky ("General") filed with the Commission a Petition for Reconsideration and Stay of Order and Request for Hearing ("Petition").

General's petition cited as reason for reconsideration, stay, and hearing that the Commission had provided no notice that it had instituted a proceeding to address the issue of a valuation standard for removing embedded mobile telephone and paging equipment from regulated books of account prior to its Order of January 30, 1985. Futhermore, General stated that it could show by legal brief and presentation of evidence that the Commission's adoption of a net book valuation standard was inappropriate for General and should be changed to a market valuation standard.

On April 25, 1985, a hearing was conducted at the offices of the Commission in Frankfort, Kentucky.

#### Valuation Method

The FCC in its Third Report and Order required the states to use economic value in the detariffing of embedded CPE and

presented four alternatives for measuring or developing a surrogate for economic value:<sup>9</sup>

- (1) Imitating the process a firm would pursue in its capital budgeting process to estimate the economic value;
- (2) Using net book value as a proxy for economic value;
- (3) Relying on asset appraisal by independent appraisers; and
- (4) Conducting auctions

General proposed using the asset appraisal approach to determine economic value. Also presented by General was the capital budgeting approach.

The Commission was left with the task of deciding which of the approaches best met the criteria in the Third Report and Order for Kentucky. The approaches presented by General fluctuate widely depending on the assumptions and inputs unique to the specific approach. On the other hand, net book value is a more certain method of valuation than either the asset appraisal or the capital budgeting approach. Thus, the Commission is of the opinion that the transfer at net book value coupled with the opportunity of the utility to recover its investment in CPE prior to detariffing, as General had through its rescription process for depreciation rates, provides the fairest balancing of interest between ratepayers and investors, as required by the FCC and the

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<sup>9</sup> Third Report and Order in CC 81-893, Released October 26, 1984, at 17 and 18.

principles of Democratic Central Committee v. Washington Metropolitan Area Transit Commission, 485 F.2d 786 (D.C. Cir. 1973) (hereinafter referred to as DCC). The FCC has found that net book value is a recognized valuation method and that it meets the DCC test.<sup>10</sup>

Moreover, General elected to enter the competitive and more risky environment when it chose to make its initial investment in mobile and paging equipment and this service was chosen by a relatively small number of customers. If General did not recover its investment in this equipment, it is the Commission's opinion that the cost of this service should not be borne by the general ratepayers as General's proposal would cause.

The Commission has therefore decided that net book value is the fairest measure of economic value for both investors and ratepayers.

#### SUMMARY

The Commission, after consideration of the evidence of record and being advised, is of the opinion and finds that:

1. General's request that the valuation standard be changed to market value for embedded mobile and paging equipment should be denied.

2. Net book value is the appropriate valuation method in determining the economic value of embedded mobile and paging equipment.

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<sup>10</sup> Ibid., at 3.

3. The findings and orders of the Order dated January 30, 1985, in this case should be applied by General and are affirmed by the Commission.

IT IS THEREFORE ORDERED that:

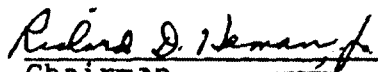
1. General's request that the valuation standard be changed to market value for embedded mobile and paging equipment is denied.

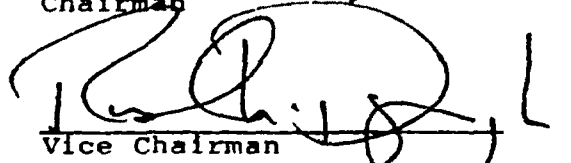
2. Net book value is the appropriate valuation method in determining the economic value of embedded mobile and paging equipment.

3. The findings and orders of the Order dated January 30, 1985, in this case shall be applied by General and are affirmed by the Commission.

Done at Frankfort, Kentucky, this 19th day of February, 1986.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Secretary