

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE TARIFF FILING OF SOUTH CENTRAL BELL )  
TELEPHONE COMPANY TO ESTABLISH PULSELINK ) CASE NO. 10321  
PUBLIC PACKET SWITCHING NETWORK SERVICE )  
AND DATA TRANSPORT ACCESS CHANNEL SERVICE )

O R D E R

Introduction

On June 20, 1989, South Central Bell Telephone Company ("South Central Bell") filed a motion for reconsideration and for rehearing of the Commission's May 26, 1989 Order in this proceeding. In that Order, the Commission rejected the proposed PulseLink Public Packet Switching Network Service and Data Transport Access Channel Service tariffs as filed and required that rates be supported using fully distributed cost allocation methods. The Commission's primary concern was to ensure that South Central Bell's regulated operations were adequately compensated for regulated services provided to its unregulated affiliate, BellSouth Advanced Network, Inc. ("BSAN").

On July 7, 1989, MCI Telecommunications Corporation ("MCI") filed its response to South Central Bell's motion for reconsideration objecting to South Central Bell's motion and strongly encouraging the Commission to stand by its May 26, 1989 Order.

In its motion, South Central Bell indicated that the Commission's concerns appeared to be based on a misunderstanding of how PulseLink service is constructed and upon an inappropriate application of Federal Communications Commission ("FCC") principles regarding protection against cross-subsidy. South Central Bell provided a discussion of how costs are allocated to its affiliate, BSAN, for the provision of enhanced services and concluded by stating:<sup>1</sup>

...costs for enhanced packet switching are already being separated from the costs for basic packet switching, and are being accounted for below-the-line. The Commission's Order rejects the PulseLink tariffs unless fully allocated cost allocation methods are also applied to basic packet switching rate elements. The Commission's Order would require the arbitrary application of fully allocated cost methodology in addition to the measures to protect against cross-subsidy already taken by South Central Bell.

South Central Bell disagreed with the Commission's determination that several of the rate elements will be used primarily, or solely, by BSAN. South Central Bell indicated that the tariff is not designed solely for BSAN and that the tariff contains significant elements for use by other customers and enhanced service providers.

South Central Bell also noted that the Commission's finding that "it is doubtful that other enhanced services providers would be able to compete with BSAN" failed to take into account the prefiled testimony of John F. Dorsch that PulseLink service would

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<sup>1</sup> Motion for Reconsideration of Order, page 4.

compete with other existing packet switched services.<sup>2</sup> South Central Bell stated that its response to Item 3 of the Commission's February 10, 1989 Order demonstrated that prices for PulseLink service are comparable to prices for service offered by packet switching service competitors.

South Central Bell also stated that the Order reflected several misconceptions concerning the relationship of BSAN and South Central Bell.<sup>3</sup> South Central Bell contended that at page 10 of the Order, the Commission stated that BSAN is collocating equipment in South Central Bell's central offices and is obtaining protocol conversion services at nominal cost. South Central Bell indicated that the equipment is owned by South Central Bell and that BSAN owns no equipment in South Central Bell's public packet switching network. South Central Bell also indicated that BSAN does not obtain protocol conversion services at nominal cost. South Central Bell indicated that the record demonstrated that in addition to the Network Utilization Rate Element, which is a 7 percent surcharge added to basic transport rates, BSAN is also being charged a non-zero cost, calculated per segment. This includes investments and expenses of central office equipment used in protocol conversions, customer billing, and installation and maintenance of equipment used to support enhanced services.

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<sup>2</sup> Ibid., page 7.

<sup>3</sup> Ibid., page 8.

South Central Bell reiterated that protocol conversion equipment has already been arranged and accounted for in such a way as to protect against cross-subsidization, and that the application of fully allocated costs to the tariffed, regulated aspects of PulseLink are unnecessary because protocol conversion costs have already been allocated and accounted for.

South Central Bell also re-emphasized its position that a fully allocated study is inappropriate for determining price levels for competitive services such as PulseLink and that the FCC recently recognized that incremental cost studies are the appropriate way to base and test prices for such services.

Finally, South Central Bell indicated that it was necessary to understand that part of the transport costs for the operation of PulseLink service include the cost of transporting data to central control centers in Atlanta and Birmingham.

#### Discussion

The May 26, 1989 Order did not question whether or not South Central Bell was appropriately applying cost allocation methods for apportioning costs related to enhanced or unregulated services.<sup>4</sup> As PulseLink service is a regulated service, the fact that the costs of providing unregulated services are allocated

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<sup>4</sup> South Central Bell's motion does raise the concern whether it is appropriately applying cost allocation principles, in that the motion suggests that common investments will be allocated based on relative usage, whereas a correct application of the allocation principles would allocate investments based on usage forecasts. However, this issue would be more appropriately addressed in Administrative Case No. 321, Separation of Costs of Regulated Telephone Service from Cost of Nonregulated Activities.

using fully allocated principles is irrelevant and does not preclude the application of fully allocated principles to the pricing of regulated services. The Commission's determination to price PulseLink based on fully allocated costs is not an attempt to reflect the costs of protocol conversion in the rates for basic services. It is to ensure that South Central Bell's regulated operations are adequately compensated for the use of basic, regulated services.

The Commission did not err in determining that several of the PulseLink rate elements would be used primarily, or solely, by BSAN. Item 12b of the Commission's February 10, 1989 Order requested South Central Bell to indicate the estimated percentage of usage of certain rate elements contained in the tariff filing. South Central Bell's response provided the following information:

<u>Item</u>	<u>Affiliate Percentage</u>
Dial Access Line	100
Data Sets, Dial Access Channel	100
Data Sets, Direct Access, Analog	78
Data Sets, Direct Access, Digital	0
Service Ordering, Dial Access Line	100
Basic Protocol Transport, Per Segment	67
Basic Protocol Transport, Fast Select	100
Asynchronous Transport, Per Segment (NURE)	100
Asynchronous Transport, Fast Select (NURE)	100
Basic Protocol Access Ports	0
Asynchronous Protocol Access Ports	100

South Central Bell noted that the first five items are available with other central office-based services besides PulseLink service and that its response only reflected their use with PulseLink service.

Although the Commission is not, and never was, of the opinion that the PulseLink tariff was designed solely for BSAN, it is clear that at least initially, BSAN will be the major user of PulseLink services. The Commission does recognize the probability that this may change in the future and that other enhanced services providers or other customers may become major users of the service. However, considering the Commission's policy with respect to the pricing of services intended primarily for resale, such as access services, it is doubtful that this would result in significant changes in PulseLink pricing methods. The Commission does recognize that competitive pressures may require changes in PulseLink pricing; however, there is no evidence that this situation exists now.

The Commission took Mr. Dorsch's testimony into account when making its finding that other enhanced services providers would be able to compete. However, South Central Bell's response to Item 3 of the February 10, 1989 Order clearly showed that PulseLink rates are significantly below the rates charged by competitors. The Commission did recognize that South Central Bell failed to include BSAN's rates in this analysis and that the services offered by competitors are primarily intended for the interstate market, whereas PulseLink is intended for the intrastate, intraLATA market. The difference in targeted markets between BSAN and the other providers of enhanced packet switching services, shows that at the present time, BSAN has very little competition in the intrastate, intraLATA market. BSAN's entry

into this market may encourage other providers to compete in this market; however, South Central Bell has provided no new evidence to suggest that full competition currently exists. Furthermore, in order to support market-based pricing for PulseLink service, it would be necessary to include BSAN's rates and costs in any analysis. Although the Commission is of the opinion that BSAN's costs, as they relate to services provided by South Central Bell, are matters that are fully within this Commission's jurisdiction, it is recognized that BSAN may also have costs for services and equipment that are not related to services provided by jurisdictional utilities. In the absence of data to support market-based pricing, the use of fully allocated procedures is a reasonable and appropriate means of pricing regulated services to any customer, not only to affiliates of South Central Bell.

The Commission did not state that BSAN is collocating equipment in South Central Bell's central offices. The Order at page 10 states, in part, that "...not only is BSAN the only enhanced services provider that can locate equipment in South Central Bell's central offices...." (Emphasis Added.) At page 9 of the Order, the Commission stated that "South Central Bell estimates that over 70 percent of the PulseLink market will require protocol conversion services. These services will occur in the regulated packet switching equipment; however, as these services are unregulated...." (Emphasis Added.) Clearly, the Commission was not confused over the ownership of the equipment. However, even if the Commission had believed that BSAN owned this equipment, it would not have impacted the Commission's decisions

in this proceeding. The Commission's discussions with respect to the collocation of equipment were in the context of BSAN's competitive advantage over other enhanced services providers. The fact that BSAN is not collocating equipment in South Central Bell's central offices, but is instead using South Central Bell's equipment, increases its competitive advantage.

The Commission is of the opinion that there is no misunderstanding of how PulseLink service is constructed. Furthermore, the Commission's determination to base PulseLink rates on fully allocated costs did not reflect an "inappropriate application of FCC principles," but rather reflected the appropriate application of this Commission's principles regarding protection against cross-subsidy. South Central Bell has argued against the use of fully allocated cost methods in this proceeding, and its motion neither presents new arguments, nor suggests that there are any, for reconsideration. Therefore, the Commission is of the opinion that South Central Bell's motion should be denied.

However, with respect to transport costs, the point that these costs reflect transport costs to Atlanta and Birmingham is well-taken, inasmuch as South Central Bell's decision to locate central control centers in these cities should not have an adverse impact on the rates charged to Kentucky users. Furthermore, as transport costs reflect only a small portion of PulseLink costs, it is doubtful that there would be much difference between a rate developed using Kentucky-specific transport costs and an average region-wide cost. Therefore, the



Commission will grant South Central Bell's request for reconsideration on this matter. The Commission will allow South Central Bell to base transport costs using a region-wide average cost.

The Commission, having considered the motion and being sufficiently advised,

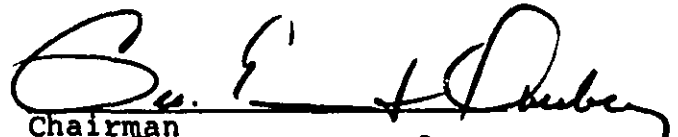
IT IS THEREFORE ORDERED that:

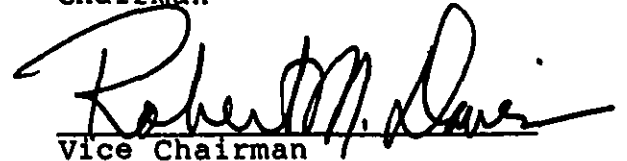
1. South Central Bell shall be allowed to base transport costs using a region-wide average.

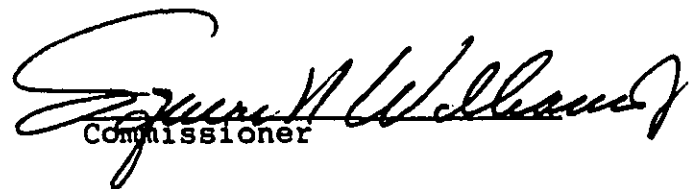
2. South Central Bell's motion for reconsideration shall be denied, except as ordered herein.

Done at Frankfort, Kentucky, this 10th day of July, 1989.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

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Executive Director