

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF COLORADO

DOCKET NO. 02A-538T

IN THE MATTER OF THE APPLICATION FOR APPROVAL OF A PLAN TO
RESTRUCTURE REGULATED INTRASTATE SWITCHED ACCESS RATES AND
PETITION FOR DECLARATORY ORDER.

DECISION DISMISSING APPLICATION

Mailed Date: January 30, 2003

Adopted Date: January 22, 2003

I. BY THE COMMISSION

A. Statement

1. On October 4, 2002, the Applicants¹ filed their Joint Application and Petition for Declaratory Order. The Application requests that we approve their Stipulation Restructuring Intrastate Access Rates, and issue an order declaring that the terms of the Stipulation shall apply to all local exchange carriers in the state of Colorado. We issued public notice of the application.

2. Pursuant to that notice, the AARP, Rebecca J. Bennett, the Colorado Office of Consumer Counsel (OCC), and Commission Staff (staff) intervened. The Application proposes a new subscriber line charge (SLC) to be imposed on each residential and business line in the state

¹ The Applicants are AT&T Communications of the Mountain States Inc.; Qwest Corporation; WorldCom, Inc., on behalf of its regulated subsidiaries; Sprint Communications Company, L.P.; and the Colorado Telecommunications Association on behalf of the following members: Agate Mutual Telephone Cooperative Association; Big Sandy Telecom, Inc.; Blanca Telephone Company; CenturyTel; Columbine Telecom Company; Delta County Tele-Comm, Inc.; Dubois Telephone Exchange, Inc.; Eastern Slope Rural Telephone Association, Inc.; El Paso County Telephone Company; Farmer's Telephone Company, Inc.; Haxtun Telephone Company; Nucla-Naturita Telephone Company; Nunn Telephone Company; Peetz Cooperative Telephone Company; Phillips County Telephone Company; Pine Drive Telephone Company; Plains Cooperative Telephone Association, Inc.; Rico Telephone Company; Roggen Telephone Cooperative Company; Rye Telephone Company; South Park Telephone Company; Stoneham Cooperative Telephone Corporation; Strasburg Telephone Company; Sunflower Telephone Company, Inc.; Union Telephone Company; Wiggins Telephone Association; and Willard Telephone Company.

. In Decision No. C02-1313 (Mailed Date of November 22, 2002), we directed the parties to brief two questions: (1) whether a SLC imposed on residential access lines would violate the statutory cap on rates for residential local exchange service; and (2) in general, does the Commission possess the authority to permit local exchange carriers (LEC) in the state to charge a SLC.

3. The parties filed opening and reply briefs on those questions. The OCC also filed a Motion to Dismiss the Joint Application and Petition for Declaratory Order for Failure to State a Claim Upon Which Relief Can Be Granted. That motion requests dismissal of the Application for various reasons. The Joint Applicants filed their response opposing the motion to dismiss on January 3, 2003.

4. In their briefs filed in response to Decision No. C02-1313, the Applicants argue that imposition of a SLC on access lines, including residential access lines, does not violate any statute. Applicants therefore argue that the Commission is legally authorized to approve the Application. AARP, Rebecca Bennett, the OCC, and Staff contend that the proposed SLC is unlawful for various reasons.

5. Now being duly advised in the matter, we conclude that the SLC proposed in the Application would violate the statutory rate cap for residential basic local exchange service. Because the residential SLC is a fundamental component of the Application and in light of our determination that such a charge is forbidden by statute, we dismiss the Application on our own motion. We do not address other arguments made by the parties in opposition to the Application. Furthermore, given the dismissal of the Application on our own motion, the OCC's Motion to Dismiss for Failure to State a Claim is denied as moot.

B. The Application

6. Applicants request that we approve their Stipulation restructuring the rates for intrastate switched access services.² The Stipulation proposes to substantially reduce intrastate switched access rates (now paid by interexchange providers), and, on a revenue neutral basis, implement an intrastate SLC for each residential and business line, to be paid by residential and business end-users.³ Specifically, the Applicants propose to offset the reduction in switched access charges by imposing a \$1.47 monthly charge on each access line within the state.⁴

7. For Qwest, the rate restructuring is intended to make its intrastate switched access rates mirror its interstate charges. For the rural ILECs, the Stipulation would result in setting their intrastate carrier common line rates to \$0.00, and offsetting that reduction, in part, with the proposed SLC. Any shortfall from these two adjustments would be recovered by the rural ILECs from the Colorado High Cost Support Mechanism. Under the Stipulation, the SLC would be charged to all access lines without regard to whether the end-user has pre-subscribed to an interexchange carrier. The reduction in switched access rates would reduce the costs for providing intrastate toll services for interexchange carriers. Nevertheless the Stipulation provides that these carriers shall *not* be required to reduce their toll rates.

² The rates for switched access services are those charges paid by interexchange or toll providers to LECs to enable those providers to originate and terminate toll calls by their customers.

³ The proposed SLC is a flat monthly charge imposed on each residential and business access line. As such, a SLC would be paid by each residential and business end-user having local telephone service regardless of their usage of particular telephone services such as toll services.

⁴ The Stipulation originally estimated the necessary revenue neutral SLC to be \$1.70. Based upon updated revenue information, the Applicants estimate the required SLC at \$1.47.

C. Briefs Regarding the Residential Rate Cap

8. As indicated above, the Commission on its own motion raised the question whether any SLC would violate the statutory rate cap for residential basic local service. Section 40-15-502(3)(b)(1), C.R.S. provides:

Consistent with the public interest goal of maintaining affordable and just and reasonably priced basic local telecommunications service for all citizens of the state, the commission shall structure telecommunications regulation to achieve a transition to a fully competitive telecommunications market with the policy that *prices for residential basic local exchange service, including zone charges, if any, do not rise above the levels in effect on May 24, 1995, for comparable service....*

(emphasis added). The statute provides for certain exceptions to the cap (*e.g.* to account for changes in the United States gross domestic product price index), but none of those exceptions is relevant to issues in this case.

9. The Applicants argue that the proposed SLC would not violate the rate cap for residential basic local service. According to the Applicants, the SLC does not constitute an increase in residential basic local service, because the SLC is not a basic local service rate element. The Applicants explain: The Application proposes to restructure switched access rates. In particular, the SLC replaces switched access charges. That is, the SLC would recover from end-users a portion of fixed loop costs now associated with the provision of intrastate access services. Therefore, Applicants argue that the proposed SLC is an access rate element, not a basic local service rate element. The rate cap in 40-15-502(3)(b)(I) does not apply to switched access rates, and, as such, the statutory cap is not violated by imposition of a SLC.

10. Applicants further contend that basic local exchange service and the associated rates do not presently cover the costs for originating and terminating access services for which the Application seeks to restructure rates in this docket. The Applicants conclude that no statute mandates recovery of access costs through per minute usage rates. The Application is simply a

rate restructuring, not a rate increase. Consequently, the Commission possesses the legal authority to approve a SLC for residential access lines.

11. AARP, Rebecca J. Bennett, the OCC, and Staff contend that the proposed SLC would violate the statutory rate cap for residential basic local service. These parties argue: Residential customers will be required to pay the \$1.47 monthly charge in order to obtain and maintain basic local exchange service. Thus, the proposed SLC will become part of the price for local service. That \$1.47 charge will raise the rates for residential local service above the levels in effect on May 24, 1995, and none of the exceptions to the rate cap apply here. Because the proposed SLC is an increase to residential basic local exchange service and the resulting rates are above the statutory cap, the SLC violates the statute. The Commission, regardless of its general discretion in setting rates, cannot approve a rate that is inconsistent with a statute.

12. The parties opposing the Application further contend that the proposed SLC is, in fact, a shift of costs from interexchange carriers to basic local exchange customers. That is, the proposed SLC is designed to recover some portion of loop costs now allocated to interexchange carriers and, ultimately, to toll service customers. As a flat monthly charge on all access lines, the SLC will force all customers to become toll customers, even if they make no toll calls. The parties argue that, in essence, the SLC is an additional charge *for access* to toll services (*i.e.* for the mere capability of placing a toll call), especially for those customers who do not place toll calls.

13. The opponents note that access to toll is already a component of residential basic local exchange service, and, as such, residential customers are already paying for access to toll in their current local service rates. The parties suggest that an additional charge without any change in basic local exchange service constitutes a rate increase in excess of the statutory cap.

14. As for the Applicants' argument that the proposed SLC is an access rate element instead of a local service rate element, the parties point out that switched access rates are charges paid by interexchange carriers to LECs for origination and termination of toll calls. A SLC, in contrast, is a charge paid by end-users directly to the LEC regardless of toll usage and as part of the monthly bill. Therefore, the proposed SLC is not an access rate element. For these reasons, AARP, Rebecca J. Bennett, the OCC, and Staff conclude that the Application should be dismissed.

D. Decision

15. We agree with the parties opposing the Application, and conclude that the proposed SLC would violate the statutory rate cap for residential basic local exchange service. In light of this conclusion and because the proposed SLC on residential customers is a fundamental part of the Application, we dismiss the Application on our own motion.

16. All parties to this case agree on the nature of the proposed SLC: First, the \$1.47 charge will be unavoidable for all customers of basic local exchange service. Any end-user wishing to obtain or maintain basic local exchange service will be required to pay the SLC; there will be no way to avoid this charge. The monthly charge will apply even to end-users who make no toll calls during the month and to end-users who are not served by applicants' companies.⁵ Second, the purpose of the flat \$1.47 monthly charge on all access lines is to allow LECs to recover directly from all end-users, not just toll users, costs now recovered in switched access rates paid by interexchange carriers and, ultimately, their toll customers.

⁵ This latter fact raises a question whether accepting this stipulation would raise a *Homebuilders* problem, see *Home Builders Ass'n of Metro. Denver v. Public Utils. Comm'n*, 720 P.2d 552, 564 (Colo.1986), because the stipulation purports to bind all local exchange carriers in Colorado, but is not being done through the normal rulemaking/ratemaking procedures.

17. We agree with the parties opposing the Application that the proposed SLC is, in effect, a local service rate element. As noted above, the monthly SLC will be an unavoidable charge imposed on all customers having an access line. Imposition of the charge is dependent on nothing other than being a basic local exchange service customer, and being a basic local exchange service customer requires that the charge be assessed. The proposed SLC, therefore, would be part of the price for basic local exchange service. And, as a new and additional charge, it would constitute a rate increase for residential basic local exchange service in excess of the statutory cap. This is so because the Commission has defined basic local exchange service as including access to intrastate toll. See 4 CCR 723-2-17.1.7. The only suggestion contravening this conclusion, that the SLC would be a local service rate element, is the Applicants' argument that the SLC is instead a switched access rate element. However, this argument is plainly unacceptable. Section 40-15-102(28), C.R.S., defines "switched access" as:

[T]he services or facilities furnished by a local exchange company to interexchange providers which allow them to use the basic exchange network for origination or termination of interexchange telecommunications services.

Switched access rates are those charges paid by interexchange providers to LECs to enable those providers to originate and terminate toll calls by their customers. The proposed SLC--a flat monthly charge imposed on each residential and business access line--is not a switched access rate element under the statutory definition.

18. Because the SLC would be a local service rate element, the price charged for residential basic local exchange service including the SLC cannot exceed the level specified in § 40-15-502(3)(b)(I). There is no dispute that this level will be exceeded with the proposed SLC once the determination is made that the \$1.47 charge is a local service rate element. Thus, the

rate for residential local service proposed in the Application would be unlawful, and cannot be approved by the Commission.

19. Moreover, we agree with the parties opposing the Application that the proposed SLC is unlawful as an additional charge to residential customers *for access* to toll services. "Basic local exchange service" includes services and features specified by the Commission. *See* § 40-15-102(3), C.R.S. Under existing Commission rule, "basic local exchange service" includes, in part, "access to toll services." *See* 4 CCR 723-2-17.1.7 (Rule 17.1.7). Our rules (4 CCR 723-2-2.2.2) define "access to toll service" as:

[T]he use of the wireline subscriber loop, as well as that portion of the switch, or the functional equivalent of these network elements in the case of a wireless carrier, *necessary to access an interexchange carrier's network*.

(emphasis added) This component of basic local exchange service does not give customers *actual toll usage*, but does give them the *capability* of making toll calls (for additional toll usage charges from an interexchange carrier). Notably, these provisions clarify that residential customers are already paying for access to toll services as part of their existing residential local service rates.

20. It is apparent that the proposed SLC is an additional charge to end-users for the same access to toll services that is now included as a feature of basic local exchange service (*i.e.* the mere capability of placing a toll call).⁶ In the first place, the Applicants concede that the purpose of the proposed SLC is to require end-users to pay some of the originating and terminating access services costs now paid by interexchange carriers through access rates, and, ultimately, by toll users. Notably, payment of the SLC will not result in any change in service

⁶ The fact that the SLC is a charge for access to toll services, which is presently one of the components of basic local exchange service under Rule 17.1.7, is additional evidence that the proposed SLC is a local service rate element.

for any local service customers; for example, no additional services or features, such as a certain number of minutes of toll usage, will be provided to customers who will be required to pay the new charge. And, as stated above, the \$1.47 monthly charge will apply even to customers who make no toll calls during the month.

21. Since the proposed SLC is not a payment for the costs related to toll usage--end-users will get no toll usage even when they pay the \$1.47 monthly charge--it must be a payment for toll access (*i.e.* for the mere capability of placing a toll call). However, as explained above, basic local exchange service customers are already paying for that service as part of their local rates. We conclude that imposition of an additional charge, the SLC, without any change to residential local service is the equivalent of a rate increase, and is proscribed by § 40-15-502(3)(b)(I).

E. Conclusion

22. For the above-stated reasons, we conclude that Applicants' proposal to reduce switched access rates and the attendant proposal to assess a SLC on all access lines, including residential lines, would violate the rate cap set forth in § 40-15-502(3)(b)(I). Therefore, the Commission lacks the legal authority to approve the Application. Given this conclusion, we dismiss the Application on our own motion. Some of the parties in their briefs and the OCC in its Motion to Dismiss raised other legal challenges to the Application. Given our conclusions regarding § 40-15-502(3)(b)(I), it is unnecessary to address these other issues. The OCC's Motion to Dismiss is denied as moot.

II. ORDER**A. The Commission Orders That:**

1. The Joint Application and Petition for Declaratory Order filed on October 4, 2002 is dismissed.
2. The Motion to Dismiss the Joint Application for Failure to State a Claim Upon Which Relief Can Be Granted by the Colorado Office of Consumer Counsel is denied as moot.
3. The twenty day period provided for in § 40-6-114, C.R.S., within which to file applications for rehearing, reargument, or reconsideration begins on the first day following the Mailed Date of this decision.
4. This order is effective immediately on its Mailed Date.

B. Adopted in Commissioners' Weekly Meeting on January 22, 2003.

(S E A L)



ATTEST: A TRUE COPY

Bruce N. Smith
Director

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

POLLY PAGE

JIM DYER

Commissioners

CHAIRMAN RAYMOND L. GIFFORD
SPECIALLY CONCURRING.

III. CHAIRMAN RAYMOND L. GIFFORD SPECIALLY CONCURRING:

1. I reluctantly join the Commission's dismissal of this petition. I do so because the legal impediments to access reform erected by the legislature are formidable and dispositive of the proposal here. I am reluctant because the policy imperative for this Commission of reforming access remains. I urge the Commission—and the parties to this Stipulation—expeditiously work toward reforming this archaic and market-distorting rate mechanism.

2. The mechanics of § 40-15-502(3)(b)(1), C.R.S. are simply too formidable to overcome with the proposal here. Unfortunately, it seems to be that § 502(3)(b)(1) cements the current rate elements in place, and allows them to change only through a very painstaking, arduous choreography that is not accomplished by this Stipulation, and may not be able to be accomplished, in concert, at all. The attempt to classify the in-state SLC as a switched access rate element—and hence not a basic local exchange service rate element—is unavailing, particularly because the Commission has made access to toll service part of the definition of basic local exchange service in Rule 17.1.7.

3. I do believe that opponents of this Stipulation – sincere and correct though their legal arguments may be—ultimately have a crabbed and incorrect view about what is in consumers' best interest, particularly rural consumers.⁷ Access and its concomitant rate distortions act as an entry barrier into the local exchange market. Furthermore, as calls to regulate CLEC access charges show, the access charge regime distorts business plans, resulting

⁷ Robert W. Crandall and Leonard Waverman's monograph *Who Pays for Universal Service? When Telephone Subsidies Become Apparent* (Brookings 2000), shows that the current above-cost access regime results in large transfers from heavy rural long distance users to light long distance users. In other words, rural consumers would benefit from access reform, particularly intrastate access reform, the most. Crandall and Waverman argue that access reform, as part of a more efficient pricing regime, would greatly increase aggregate social welfare. The only losers from moving to such a pricing system would be rural consumers who do not use long distance. Political efforts should therefore be directed toward identifying and buying-off that group of consumers.

in arbitrage and incentives to park under an incumbent's access charge price umbrella. These are bad things, and impede any progress toward consumer welfare-enhancing competition in the local exchange market.

4. Finally, let me briefly sketch how the Commission might be able to accomplish the worthy, incremental goal of reforming intrastate switched access rates. First, the Commission will need to remove access to toll from the definition of basic local service. This service package change will, of course, cause cascading rate effects for the basic local service package, where, among other things, the Commission can address the common cost fallacies that underlie the current rate structure. Second, in concert with this basic local exchange package re-definition, the Commission should open a proceeding to investigate moving services from Part 2 regulation to Part 3 emerging competitive regulation and, ultimately, Part 4 deregulation. *See* §§ 40-15-207, 40-15-305, C.R.S. This will remove the entry barriers and distortions from the current rate requirements.

5. Moreover, I believe that "effective competition" will be found during that inquiry. The local exchange market has been made contestable by the federal wholesale unbundling, pricing and enforcement requirements. In addition, substitution of the wireline telephone service by wireless and cable telephony proceeds apace. Put simply, it is my belief that much of the retail rate regulation we do now—including access regulation—can and should be eliminated.

6. To return to this Stipulation, while it represents progress, it also retains and pays too much homage to those old rate elements. Consumers—and all carriers—would be better off if the Commission and the legislature set its mind on transcending these archaic rate elements, instead of perpetuating them. In my time on the Commission, there has yet to be an effective or convincing rebuttal to Kahn and Shew's pathbreaking article that defends what should be

commonplace: loop costs are not common costs and thus should be attributed to and recovered through subscriber access charges.⁸ Therefore, even this Stipulation was problematic, despite the residential statutory rate cap.

7. For one, the in-state SLC perpetuates the fiction born from political expediency that adds line-item charges to customers' bills in an effort to nudge toward recovering the loop costs through subscriber access charges. Consumers do not like this, and they should not like it. Second, the Stipulation perpetuates the rate elements that—particularly on a digital network—might not properly exist at all.

8. The goal is broad-based deregulation, not incremental and tediously slow retreat from rate structures we know to be wrong and harmful to consumers in the aggregate. This is by no means an easy feat. However, because regulatory change happens so haltingly, and there is so much work often for such paltry gains, I would urge the Commission to be bold; seek to abandon wholesale the current rate structure and its elements.⁹ The consumers of Colorado will benefit from such leadership.

⁸ Alfred E. Kahn & William B. Shew, "Current Issues in Telecommunications Regulation: Pricing" 4 Yale J. Reg. 191 (1987); *see also* Steve Parsons, "Seven Years after Kahn and Shew: Lingering Myths on Costs and Pricing Telephone Service" 11 Yale J. Reg. 149 (1994).

⁹ There is great cause for pessimism that this will ever happen. For one, there are formidable reliance interests built up around the current system—this Commission itself being one of those players with reliance interests and incentives to behave opportunistically. If there is no movement because of political inertia, the system will surely soon collapse under its own weight in any event, just as it rapidly is doing in the inter-state realm. Unlike the FCC, however, this Commission does not have the power to bail itself out by extending, say, access or universal service taxes onto data or Internet services. Because the inevitable will happen—wireless statewide calling areas are now the norm—and access will collapse, the short-term losers will be the incumbents, particularly access-dependent rural incumbents. In the meantime, however, Colorado consumers are cheated by overpriced in-state long distance, distorted incentives to enter the local exchange market and only the illusion of competition under damaging constraints.

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

CHAIRMAN RAYMOND L. GIFFORD

Commissioner

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