(Decision No. C87-1347)

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

* * *

RE: THE REVIEW OF PRIVATE LINE SERVICES IN ACCORDANCE WITH §40-15-308, C.R.S. and §40-15-305, C.R.S.)	CASE NO. 6633
RE: THE APPLICATION OF THE MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY FOR ENTRY OF AN ORDER BY THE COMMISSION REFRAINING FROM REGULATING POINT TO POINT AND POINT TO MULTIPOINT DEDICATED TELECOMMUNICATIONS SERVICES; OR IN THE ALTERNATIVE, FOR A DECLARATION OF CONTINUED APPLICABILITY OF THE PUBLIC UTILITY LAW OF COLORADO TO OPERATING RIGHTS FOR THOSE SERVICES.)	APPLICATION NO. 37367 INITIAL COMMISSION DECISION

September 28, 1987

Appearances:

Russell P. Rowe, Esq., Raymond W. Martin, Esq., and Roy A. Adkins, Esq., Denver, Colorado, for The Mountain States Telephone and Telegraph Company;

T. Larry Barnes, Esq., and Rebecca B. DeCook, Esq., Denver, Colorado, for AT&T Communications of the Mountain States, Inc.;

Ann Hopfenbeck, Esq., Denver, Colorado, for the Office of Consumer Counsel;

George J. Cerrone, Esq., Denver, Colorado, for the City and County of Denver;

Paula M. Connelly, Esq., Denver, Colorado, for the Colorado Municipal League and the Colorado Association of Radio Common Carriers;

William Levis, Esq., and Robert Nichols, Esq., Denver, Colorado, for MCI Telecommunications Corporation;

Michael Glaser, Esq., Denver, Colorado, and James F. Fell, Esq., Portland, Oregon, for Eagle Telecommunications, Inc.;

Mark A. Davidson, Esq., Denver, Colorado, for Phillips County Telephone Co., Plains Telephone Coop., Peetz Telephone Coop., Rye Telephone Co., Universal Telephone Co., Haxton Telephone Co., Pine Drive Telephone Co., and Strasburg Telephone Co.;

Randall G. Alt, Esq., Denver, Colorado, for Agate Mutual Telephone Exchange Co., Big Sandy Telecommunications, Inc., The Bijou Telephone Coop. Assn., Columbine Telephone Co., Delta County Coop. Telephone Co., Eastern Slope Rural Telephone Assn., Inc., Farmers Mutual Telephone Co., Nucla-Naturita Telephone Co., Inc., Sunflower Telephone Co., Inc., and Wiggins Telephone Assn.;

Peter Edwards, Esq., Denver, Colorado, for Denver Burglar and Fire Alarm Company;

Terry Parrish, Berthoud, Colorado, pro se;

Martin Cahill, Lakewood, Colorado, pro se;

Herbert Lindsay, Northglenn, Colorado, pro se;

Arthur G. Staliwe, Esq., and Peter Stapp, Esq., for the Staff of the Public Utilities Commission, and

John E. Archibold, Esq., Denver, Colorado, for the Public Utilities Commission.

STATEMENT

Application No. 37367 was filed by The Mountain States Telephone and Telegraph Company (Mountain Bell) on November 26, 1985. After notice was issued by the Commission on December 19, 1985, protests or petitions to intervene were filed by AT&T Communications of the Mountain States, Inc. (AT&TCOMM), Colorado Municipal League (CML), Colorado Association of Radio Common Carriers (CARCC), Colorado Cable Television Association (CATV), Denver Burglar & Fire Alarm Company (DBA), the Office of Consumer Counsel (OCC), the City and County of Denver (Denver), MCI Telecommunications Corporation (MCI), Colorado Ski Country USA (CSCUSA), and the Staff of the Commission (Staff). The petitions for intervention were granted by the Commission. In addition, the Commission had ordered Mountain Bell to provide notice to affected customers on December 12, 1985.

Hearings in this application were scheduled to begin on December 1, 1986. When the matter was called for hearing, Mountain Bell moved to withdraw or, in the alternative, to delay hearing on its application. This request was taken under advisement. On December 15, 1986, Mountain Bell filed a letter with the Commission requesting that further hearing on this matter be continued until after June 1, 1987. This request was granted. Subsequently, in Decision Nos. C87-54, C87-221 and C87-427, the Commission ordered Mountain Bell to file monthly reports estimating the amount of revenue lost as a result of competitive activities in the private line market, beginning with data for December 1986. Exhibit No. 4D is a copy of Mountain Bell's only report filed prior to September 17, 1987.

On July 2, 1987, Governor Roy Romer signed HB 1336 into law, codified as Article 15, Title 40, C.R.S., which repealed HB 1264 enacted in 1984. As a result of this legislation, the Commission established Case No. 6633 and consolidated it with this application to allow the Commission to consider, in an efficient and expeditious fashion, treatment of private line services for all providers in the State of Colorado. The Commission issued notice of Case No. 6633 on July 2, 1987, and, as a result, additional petitions to intervene were filed and granted by the Commission for US Sprint (Sprint), Eagle Telecommunications, Inc., Phillips County Telephone Company, Plains Telephone Cooperative, Peetz Telephone Cooperative, Rye Telephone Company, Universal Telephone Company, Haxton Telephone Company, Pine River Telephone Company, Strasburg Telephone Company, Agate Mutual Telephone Exchange Company, Big Sandy Telecommunications, Inc., The Bijou Telephone Cooperative, Columbine Telephone Company, Delta County Cooperative Telephone Company, Eastern Slope Rural Telephone Association, Inc., Farmers Mutual Telephone Company, Inc., Nucla-Naturita Telephone Company, Sunflower Telephone Company, Inc., Wiggins Telephone Association, and American Television and Communications Corporation, (ATC) and by pro se intervenors Herbert A. Lindsay, Terry Parrish, Martin Cahill, Maggie Nachtscheim, and Rhonda Bryant. The Commission set these matters for hearing beginning September 1, 1987.

After passage of HB 1336, Mountain Bell requested the Commission to deregulate all private line services. AT&TCOMM also requested the Commission deregulate all of its private line services. On August 28, 1987, Mountain Bell filed a Modification to Trial Data Certificate which limited its request. AT&TCOMM also filed two alternative proposals concerning its request which were received into evidence as Exhibit No. 23.

The hearing began as scheduled. During the course of the hearing, 73 exhibits with numerous attachments were received into evidence. In addition, motions to strike the testimony of Larry Van Ruler, Robert F. Adkisson, and a motion to strike an Amicus Curiae Statement filed on behalf of the Colorado Chapter of the Telecommunications Association (TCA), filed during the hearing, were denied. A request to withdraw intervention filed by Martin Cahill was granted.

The hearing was presided over by Examiner Thomas F. Dixon. Members of the Commission attended the vast majority of the hearing as their schedules permitted, consistent with other Commission business. The Commission also asked questions of various witnesses when clarification was necessary and attended closing arguments held on September 17, 1987.

At the conclusion of the hearing, this matter was taken under advisement. In accordance with § 40-6-109(6), C.R.S., the Commission issues this Initial Commission Decision.

FINDINGS OF FACT and CONCLUSIONS THEREON

Based upon all of the evidence of record, the Commission finds the following facts and makes the following conclusions of law.

1. Under the requirements of § 40-15-308, C.R.S., due and timely execution of its functions imperatively and unavoidably requires the Commission to issue an Initial Commission Decision in these proceedings.

2. Mountain Bell, so far as relevant here, is a local exchange provider of basic, local-exchange service, other services under Title 40, Article 15, Part 2 (Part 2 services), private line service as defined in § 40-15-102(22), C.R.S. (private line service), and other emerging competitive telecommunications services under Title 40, Article 15, Part 3 (Part 3 services), and is subject to the jurisdiction of the Commission. AT&TCOMM and MCI, so far as relevant here, are providers of private line service and other Part 3 services and are subject to the jurisdiction of the Commission. All three of these providers, as well as any other person, firm or corporation, may provide telecommunications services under Title 40, Article 15, Part 4 (Part 4 services), which were deregulated under HB 1336.

3. Application No. 37367 was filed prior to the enactment of HB 1336, now codified as Article 15, Title 40, C.R.S. (HB 1336), when HB 1264, previously codified as Article 15, Title 40, C.R.S. (HB 1264), was in effect. Case No. 6633 was established by the Commission as a result of the enactment of HB 1336 in order to evaluate efficiently and expeditiously the degree of regulation necessary for the provision of both intraLATA and interLATA private line services provided in the State of Colorado.

4. Under § 40-15-305(1)(a), C.R.S., the Commission may deregulate Part 3 services in accordance with Part 4 upon a finding that effective competition exists in the relevant market for a particular service and that deregulation will promote the public interest and the provision of adequate and reliable service at just and reasonable rates.

Under § 40-15-101, C.R.S., in HB 1336, the General Assembly declared that it is the policy of the state to promote a competitive telecommunications marketplace while protecting and maintaining the

quality of telecommunications services, and to regulate telecommunications services in a manner that would guarantee the affordability of basic telephone service while fostering free market competition within the industry. It found that these policies would increase customer choices and enhance the state's economic development. The legislature recognized that the degree of competition varied between markets, products and services. It, therefore, passed HB 1336 to declare that flexible regulatory treatments were appropriate for different telecommunications services.

Section 40-15-308, C.R.S., requires the Commission to evaluate and issue a decision in Application No. 37367 by October 30, 1987. For good cause, the Commission may extend the time to issue a decision for an additional 30 days. With the establishment of Case No. 6633, and its consolidation with Application No. 37367, the Commission will also evaluate private line service available through other providers, although not required to do so under § 40-15-308, C.R.S.

5. The General Assembly gave specific criteria for the Commission to use in order to determine whether or not effective competition exists in the Part 3 services, including the private line service market, in § 40-15-305(1)(b), C.R.S., and required the Commission to consider and make findings concerning the following factors:

(I) The extent of economic, technological, or other barriers to market entry and exit;

(II) The number of other providers offering similar services;

(III) The ability of consumers to obtain the service from other providers at reasonable and comparable rates on comparable terms and under comparable conditions;

(IV) The ability of any other provider of such telecommunications service to affect prices or deter competition;

(V) Such other relevant and necessary factors, including but not limited to relevant geographic areas, as the commission deems appropriate.

6. If effective competition is established for private line services in the relevant markets, then the Commission must determine if deregulation will promote the public interest. Although no definition of the public interest was established in HB 1336, it can be presumed that the General Assembly's intent can be found primarily in Title 40, Article 15, Part 1, C.R.S. (Part 1). In furtherance of its legislative declaration, the General Assembly stated in Part 1 among other things that nothing in HB 1336 should be construed to supersede any existing powers

of a local government and that no local exchange provider should price or provide access to its system in a discriminatory manner nor advantage itself in its local exchange network to the prejudice or disadvantage of other providers. Part 4 services or products could not be cross-subsidized by revenues derived from regulated services and products under Parts 2 and 3. If a local exchange provider did not have interconnection with an interexchange provider, the Commission could order the interconnection. Any provider of regulated and unregulated telecommunications services must segregate its intrastate investments and expenses to ensure no cross-subsidization of deregulated services by regulated services. Finally, regulation must guarantee the affordability of basic telephone service and promote provision of adequate and reliable service at just and reasonable rates (universal service), while fostering free market competition.

The General Assembly also gave the Commission powers, in addition to those already available under §§ 40-6-106 & 107, C.R.S., to inspect books and documents of affiliates of local exchange providers and the power to develop and approve cost allocation methods which would prevent cross-subsidization.

7. Many of these terms used in HB 1336 are undefined, but guidance is available to the Commission in the general requirements of Part 1 proscribing cross-subsidization of unregulated services by regulated services and illegal restraint of trade, and in the requirements of §§ 40-3-102 & 106, C.R.S., against maintaining any unreasonable difference as to rates or services which are still specifically applicable to Part 3 services.

8. Finally, the Commission must find that deregulation will promote a competitive telecommunications marketplace as described in § 40-15-101, C.R.S.

9. In the event deregulation is not appropriate, the Commission shall regulate Part 3 services, including private line services, considering alternatives to traditional rate-of-return regulation such as flexible pricing, detariffing, and other methods consistent with the legislative intent expressed in § 40-15-101, C.R.S. In § 40-15-302(1), C.R.S., the Commission can consider rate base regulation and rate-of-return regulation, but shall not use them as the sole factors considered when regulating Part 3 services.

10. The General Assembly reduced legal barriers to entry into the Part 3 services or products market, and included nothing in Part 3 to require mandatory certification of providers of Part 3 services or products under § 40-15-302(2), C.R.S.

11. With this statutory framework in mind, neither Mountain Bell, AT&TCOMM nor any other provider demonstrated that effective competition presently exists in Colorado or within any submarket of the state for private line services. While Mountain Bell and AT&TCOMM demonstrated

that competitors exist for some private line services, the level of competition generated by these competitors is not effective. While many competitors potentially are capable of providing some private line services using alternative technologies, few are, in fact, providing private line service. AT&TCOMM provided no Colorado-specific evidence to support a finding of effective competition within Colorado's interLATA market, which is the relevant market for evaluating the competition it faces in the provision of private line services. Mountain Bell's evidence included several studies of competition. A microwave study (Exhibit No. 43) previously submitted to the Commission in Investigation and Suspension Docket No. 1720 (I&S 1720), then sponsored by Gordon Blankenship, was again submitted here. In Decision No. C87-364 (Exhibit No. 18) the Commission criticized this study as follows:

> We find that Mountain Bell Witness Blankenship's microwave study failed to demonstrate the existence of significant bypass of Mountain Bell's system. It should be pointed out that Mr. Blankenship's study far overstates the alleged inroads into Mountain Bell's customer base made by private microwave systems. This study also overstates the potential inroads of bypass into Mountain Bell's customer base. We find Mr. Blankenship's microwave study contains the following errors or misrepresentations:
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> 1. The study does not make a distinction between economic and uneconomic bypass. Mountain Bell has stated that its only concern is economic bypass.
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> 2. Public utilities, railroads, state and local governments, and oil companies make up 97 percent of the reported revenue losses. Each of these entities has particular quality and security requirements which Mountain Bell has difficulty fulfilling. In addition, these entities (except oil companies) have right-of-way paths unavailable to the general public which will tend to place them in the category of economic bypassers.
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> 3. Most of the private microwave capacity was installed prior to 1980. The largest users of private microwave systems, such as Public Service Company, the State of Colorado, K N Energy, Inc., and Colorado-Ute Electric Association, Inc., began construction of their private microwave systems in 1953, 1953, 1957, and 1977, respectively.

> 4. The largest users of private microwave systems also tend to be the largest users of Mountain Bell switched services....
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> 5. Reliability was a major concern for the largest private microwave users....
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> 6. Eight of the private microwave systems make up 82 percent of the alleged revenue loss, of which two of the systems make up 41 percent of the alleged revenue loss.
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> ...[T]he Commission recognizes that the private line market where it involves high speed data transfer (sometimes called the high end of the private line market) is a market which is becoming more competitive.
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> * * *
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> This market has its own special issues and its transition should be tailored to those issues.

It is unclear to the Commission why Mountain Bell would submit a study which was already found to fail to demonstrate the existence of significant bypass. This Commission took pains, in Decision No. C87-364, to point out the weaknesses it found in Mountain Bell's studies. It is hoped that in the future Mountain Bell will read our orders carefully and correct the failings we find in studies, rather than resubmitting valueless studies from past cases. Although HB 1336 has become law since the decision in I&S 1720 was issued, the conclusions concerning this study, standing alone, are still applicable.

12. Mountain Bell also offered additional evidence to support its original request that the Commission deregulate all, and as it amended its request, only certain private line services. This additional evidence, however, does not support a finding of effective competition for any private line services.

13. Specifically, Mountain Bell argued from Proprietary Exhibit No. 4D that certain revenues were lost to Mountain Bell as a result of competition. We find that argument is worthy of no weight based on Staff Witness Langland's analysis in Exhibit No. 59 of the information contained in Exhibit No. 4D. First, there is no showing that the data used from 1982 through December 31, 1983, to develop a trend line is representative of Mountain Bell's present position, since divestiture occurred on January 1, 1984. Data existed for the subsequent years of 1984 through 1987 which should have been considered and incorporated, as acknowledged by Mountain Bell's own witness, Mr. Guth. He stated it was not reasonable to ignore data available after January 1, 1984, to develop the trend

line. The Commission could infer that the complete data, if incorporated in the trend line, would have caused a different trend line from which less favorable conclusions could be drawn from Mountain Bell's perspective. We find that the omitted data invalidate the report and the conclusions which might be derived from it in its present state since the data is out-of-date. In addition to being out-of-date, the study is extraordinarily simplistic. As Mr. Langland testified, the study made no adjustment for any other factor than time, omitting a variety of important economic influences and statistical techniques such as back-casting.

In Decision Nos. C87-54, C87-221 and C87-427, the Commission directed Mountain Bell to a quantify its lost revenues for private line services on a monthly basis, which Mountain Bell has repeatedly asserted is occurring in other proceedings before the Commission. Exhibit 4D was its response to these Commission orders, a response we find to be inadequate. As business managers facing a more competitive environment, responsible officials in Mountain Bell should know whether they are losing private line business or not, and be able to quantify any lost revenues. We will later order Mountain Bell to develop an adequate method, in conjunction with staff, to track losses.

14. In Exhibit No. 3, Mary Kaye Sharp discussed an analysis of the monthly billing of the top 100 revenue-generating customers for all services of Mountain Bell. Mountain Bell staff compared these customers' private line monthly billing for January 1, 1985, and May 1, 1986. Twenty-seven customers had significant decreases in private line billing. Mountain Bell concluded that the decline in revenues for 14 of these customers was related to competition. From this, Mountain Bell drew certain conclusions, which it acknowledged depended on whether this sample was representative of the total customer base. It is this very assumption which must be proven before the conclusions provided can be probative. There was no evidence to support the basic assumption. Presumably, this is a summary of voluminous records, yet Mountain Bell offered no underlying records to support the conclusions which could have made its results probative under Rule 1006, Colorado Rules of Evidence.

15. Finally, the specific examples of reselling and sharing of microwave capacity demonstrated that resale was limited. For example, the Mountain Top system developed technical problems and is being upgraded to meet the needs of the primary user. Moreover, Mountain Top is not even attempting to solicit new customers. The amount of competition available from the five microwave systems identified in Exhibit 4E is virtually unknown, if indeed it exists. Although Mrs. Sharp discussed some resale and sharing of some of these systems, which had been related to her and other Mountain Bell staff, this evidence and the attempts to refute it by Mr. Langland were hearsay evidence unsupported by a residuum of competent evidence, and, therefore, entitled to no weight.

16. Mountain Bell acknowledges that its primary source of competition is from those telecommunications users who bypass virtually all of the Mountain Bell network by constructing their own private telecommunications networks, such as Martin-Marietta and the State of Colorado.

Mountain Bell contends that these customers are lost to the network whether or not they resell or share their excess capacity. There is no question that the loss of a customer potentially results in lost revenues to Mountain Bell to the extent former customers do not use the network and plant is stranded, at least temporarily. Private system competition to Mountain Bell comes not from entities such as Martin-Marietta and the State which build private systems for their own use (unless they resell or share with others), but from equipment vendors who sell the private telecommunications systems. Under HB 1264, in § 40-15-108(1) through (7), C.R.S., the General Assembly provided a mechanism for intraLATA providers to negotiate a contract with potential purchasers of private telecommunications networks. The mechanism has been used by some providers. Most of these applications have been approved by the Commission within 15 days. This mechanism is also available under HB 1336 (see § 40-15-203[3] through [8], C.R.S.) and is the statutory mechanism provided by the General Assembly for response to competition for private telecommunication networks. (Exhibit No. 70)

17. Mountain Bell also presented evidence that competition is prevalent via coaxial cable available from cable television providers. The City of Longmont has employed the use of this technology to provide traffic signalization, data and voice transmission under its franchise agreement with a cable television provider. While this is provided at no charge, the cable provider was allowed to use the necessary rights-of-way at no charge, while such use normally is charged at the rate of 4 or 5 percent of the gross revenues of the authorized user.

Coaxial cable also was used by ATC to provide home security in the Littleton/Highlands Ranch area in the southwest Denver metropolitan area. Initially, ATC wired Highlands Ranch with coaxial cable and used the cable to provide the home security service. However, it found that use of cable, alone, was not reliable or satisfactory. It began substituting autodialers and telephone line services as the primary means to provide security. It used the coaxial cable as a back-up system. The autodialers used in the Littleton area require the use of the Mountain Bell public switched-network rather than private lines. The net effect is that the coaxial cable is no longer used to a significant degree to replace Mountain Bell private line service. While this use of coaxial cable originally was touted by the cable television industry as a medium for home security, it has not proven itself in Colorado, as described by Witness Frank Pickard, Jr. The competitive potential is diminishing for that purpose.

Moreover, this technology requires the acquisition of rights-of-way which generally are quite costly or unavailable. While Mountain Bell discounts the importance of the need for rights-of-way and its ability to obtain it through the use of eminent domain, the fact remains that for anyone who intends to use coaxial cable or any other type of wire, including fiber optic, the cable must be physically placed somewhere, either in the ground or in the air, which necessarily involves the need for right-of-way. Mountain Bell also contends that anyone who can't obtain the necessary rights-of-way can use switched access or special

access (as defined in § 40-15-102[25] & [28]) to Mountain Bell's telephone system which Mountain Bell must provide. While it is true that such access must be provided, it is also true that for those users or customers who wish to build their own private telecommunications network, the acquisition of rights-of-way is critical in the event wireline technology is used to provide service end to end. This, perhaps, explains why most private telecommunications networks use microwave rather than other technologies, since rights-of-way are not so large an issue with microwave technology, generally. Even microwave technology is limited because of line-of-sight obstructions or difficult topography. Finally, the capital costs necessary to construct these private networks are substantial and operate as an economic inpediment. While lease-purchase options may ameliorate the up-front costs, many governments cannot exercise this option.

18. Mountain Bell presented evidence that satellite technology also has been used to generate competition within its private line market. However, it is clear from the evidence in these proceedings that the use of satellites to replace private line service is primarily for long distances and frequently on an interstate basis. Moreover, satellites are less desirable for applications requiring high degrees of security, such as use within the banking industry or for security systems. Mountain Bell's evidence that satellites are being used by the City of Colorado Springs for telemetry to monitor dams west of the city is not a sufficient indication that the use of this technology is widespread in Colorado. Other evidence of intraLATA usage of satellite technology within Colorado was lacking.

19. Additional forms of technology may be available to users who wish to bypass all or a part of the private line service market, but evidence of their actual use in Colorado was virtually nonexistent on the record in these proceedings. While AT&TCOMM, MCI, Sprint and other interLATA carriers may be poised to enter the intraLATA private line market, evidence of current, effective competition from them was nonexistent, primarily because HB 1336 only became effective on July 2, 1987, and secondarily because there is still some question as to whether they can legally enter this market without Commission approval. House Bill 1336 did not mandate certification of providers of Part 3 services, but the Commission is required to adopt rules concerning certification. It is likely that if certificates are issued, it will be in a very simplified manner. The Commission has already established Case No. 6636 to adopt certification rules, has held a public hearing, and has taken that case under advisement. It was argued in that case that the Commission should certificate some providers of Part 3 services, such as AT&TCOMM, MCI or Sprint, and not certificate others, particularly those who have not been subject to the Commission's jurisdiction historically, such as resellers.

20. From the probative evidence presented, those customers who employ the high-end or high-speed technology, which was discussed in I&S 1720, have the most alternatives available and represent the greatest threat of competition to Mountain Bell. Most witnesses agreed that com-

petition existed to varying degrees in this submarket. Moreover, most witnesses agreed that the potential for competition was also greatest in this submarket for the future. Concern was expressed, however, over the piecemeal deregulation of portions of the overall private line market if the Commission chose to deregulate this submarket. As previously noted, the Commission does not find sufficient competition exists to deregulate this submarket at present; however, its decision not to deregulate is not based on a fear of piecemeal deregulation. Piecemeal deregulation is already a fact in HB 1336 with the deregulation of Part 4 services. Segregation of investments and expenses is also a fact of life for this Commission, no matter how difficult that may be.

21. The high-end or high-speed private line service is defined as providing to a single customer the capacity of 24 or more circuits over a single path, point to point, for analog transmission; or the use of T-1, DS-1 or above, or its data-service equivalent at or in excess of 1.544 megabits per second for digital transmission by a single customer over a single path, point to point. It is this segment of the intraLATA private line market served by Mountain Bell that is most competitive and deserves maximum flexible treatment, but this portion of the market is, at best, a patchwork of competition as described by Dr. Mark Correll for the OCC.

To respond to this situation, the Commission will develop a minimal regulatory scheme under which it will retain jurisdiction over this submarket of private line service. The Commission intends to exercise only its complaint jurisdiction and its audit powers to monitor this submarket unless unexpected problems arise. The Commission intends for Mountain Bell to operate as if these high-end private line services were virtually deregulated. Mountain Bell will not be required by this decision to file any price lists with the Commission for these services. However, staff will audit the provision of these services based on records to be developed and maintained by Mountain Bell which will contain only that information competent business managers would require to adequately manage the private line business.

In the event the rates set by Mountain Bell are challenged, Mountain Bell will have the burden of proving its rates are reasonable in future rate cases. Under Case No. 6634, the investments and expenses associated with these services will be segregated as if these services were deregulated in this decision. The Commission also will review the continued regulation of these services in approximately one year, as was recommended by <u>pro se</u> intervenor, Mr. Terry Parrish, to evaluate the impact of this action and to determine if these high-end services should be deregulated then, as more fully described in paragraph 37. At that time, Mountain Bell may supplement the evidence it provided in the hearing held from September 1 through 17, 1987.

22. With respect to all other intraLATA private line services, banded pricing with packaging flexibility is an appropriate form of flexible regulation. Again, virtually all witnesses who commented on this issue expressed the need for Mountain Bell to have pricing flexibility in

order for it to compete with potential competitors. The Commission recognizes that a loss of customers from the Mountain Bell network may result in lost revenues and stranded plant which could result in increased rates for the inelastic customers of Mountain Bell, normally residential and small business users. All parties agreed and the Commission finds that the ceiling for the banded rates should be the present tariff rates ordered in I&S 1720.

Disagreement arose with respect to the appropriate floor. The economists, Mr. Guth, Mr. Langland, Dr. Zepp and Dr. Correll, provided several alternatives. Mr. Guth, on behalf of Mountain Bell, recommended the floor be based upon the long-run incremental costs (LRIC) to produce the service or product, a concept that is difficult in application. Dr. Correll, on behalf of the OCC, recommended a floor derived by reducing the tariff rate by a varying percentage depending upon the amount of competition existing for the service or product. Mr. Langland, on behalf of the Staff, recommended that the ceiling be discounted by volume of use, using an inverted block rate. Dr. Zepp, on behalf of MCI, recommended that the floor could be set either with the proper use of LRIC or by narrowing the band similar to the recommendations of Dr. Correll or Mr. Langland.

23. No evidence was presented as to what the floor rates would be using any of the alternatives. Mountain Bell requested the Commission adopt the LRIC rates which it proposed in I&S 1720. When the Commission considered the use of LRIC to set rates in I&S 1720, it did so for broader purposes, and was justifiably skeptical of that method.[1]

Since the I&S 1720 decision, HB 1336 has become law and mandates consideration of flexible regulation of Part 3 services. Unlike I&S 1720, the application of LRIC in the private line market below 24 circuits or the DS-1 equivalent has less pervasive impact. The Commission finds that LRIC can be used in the private line market with less impact upon ratepayers, in general, than if LRIC had been used for all fixed, tariffed rates. For banded rates, LRIC-based prices will be used as a floor, whereas, in I&S 1720 Mountain Bell asked the Commission to use LRIC to establish fixed rates which would be the only rate Mountain Bell would have charged had LRIC pricing been adopted. The present tariff rates are based on fully distributed costs and, if used as a ceiling price, protect private line users. Those rates were derived primarily by using historical data with adjustments made for known and measurable future events. The LRIC method does require predicting future events and involves the use of projections.

The methods proposed by Dr. Correll, Dr. Zepp or Mr. Langland for setting the floor rates, indirectly rely on the use of historical information, i.e., hindsight. In competitive markets, projecting and anticipating the future, as well as hindsight, are the norm. Therefore, the

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1. Investigation and Suspension Docket No. 1720, Decision No. C87-364, March 20, 1987, pages 18 and 19.

Commission will allow Mountain Bell to establish banded prices using the present tariff rates as a cap and LRIC as a floor for private line services. This allows Mountain Bell flexibility to meet expected competition in the intraLATA market but protects both the general body of ratepayers and the users of private line services.

24. The Commission will use its audit powers to evaluate the rates derived using LRIC. The concerns the Commission expressed in I&S 1720 are known and Mountain Bell should be prepared to address them during audits of the LRIC rates. The rates derived using LRIC will not be published and will be treated as confidential information in order to minimize leverage that might be exercised by Mountain Bell customers and competitors. However, the LRIC prices will be available to staff and parties to these proceedings who comply with previously issued protective orders. Mountain Bell will maintain all records it uses to determine LRIC prices for staff inspection. In the event the LRIC prices are challenged by any party, Mountain Bell will always have the burden of demonstrating the LRIC rates are reasonable in any rate proceeding.

25. Mountain Bell shall continue to publish tariffs reflecting the current rates established in I&S 1720, until changed with the approval of the Commission. These rates shall always be available to a customer who does not wish to obtain services or products under the banded rates, as was suggested by public witness Mr. Martin Cahill. The Commission recognizes that the present tariff rates will be, by definition, the highest price a customer would pay, but the continued publication of the current tariff rates may present less confusion to customers during the transition period. Moreover, the current tariff rates and the ceiling of the banded rates may be adjusted in the future by the Commission based on FDC.

Mountain Bell proposed that the price within the banded rates might be different for various exchanges, which would be the equivalent of geographic deaveraging. It could also be inferred that Mountain Bell proposed to price the same services or products differently for similar customers. Mountain Bell's representatives did agree later in these proceedings that Mountain Bell would treat similar customers in a similar fashion; however, the Commission finds that these proposals should be rejected. Banded rates shall be set on a service-by-service or product-by-product basis, statewide, so that similar customers are treated in a similar manner and so there is no undue discrimination.

26. The Commission wants customers to have maximum choices. To foster this goal, Mountain Bell should have packaging flexibility, allowing it to package its services and products to give customers additional choices. However, if Mountain Bell offers private line services together with other regulated services, it shall unbundle the prices of each component of its packages by stating these prices separately in order to allow competitors the ability to offer similar packages as was suggested by CML witness, Mrs. Rigg. Competitors should be able to use some of Mountain Bell's services and products on an unbundled basis to complete their own package offerings as was discussed by Mountain Bell witness,

Mrs. Sharp. Customer choices should not be limited to Mountain Bell packages. Rather, customers must also be able to choose packages from other providers. Where a competitor offers only a portion of the Mountain Bell package, it must be able to complete a similar package offer, using those Mountain Bell services and products necessary at the unbundled prices, which should be reflected in tariffs for regulated services or on price lists for flexibly or unregulated services.[2] In other words, Mountain Bell shall not use its ability to provide one-stop shopping to a customer, to the disadvantage of a competitor.

27. The Commission will also adopt Mountain Bell's revenue treatment proposal in its Clarification of Modification to Trial Data Certificate concerning packaging flexibility. To resolve the subsidization concerns, revenues for services and products will be credited to categories as follows:

A. Revenues equal to the tariff rate shall be assigned to Part 2 services of the package first.

B. For Part 3 services that are flexibly priced, the prices stated in the price list shall be recovered and assigned. Finally, and residually, the remaining revenues will be assigned to the unregulated service categories.

28. In addition to the flexibility allowed through the use of banded rates, Mountain Bell shall be permitted to enter into contracts with customers for private line services. Like banded pricing, the floor for the prices of service and products subject to a contract shall be based on LRIC which, at least in theory, unambiguously prevents predatory pricing. Conceptually, a primary reason for a customer to enter into a contract with Mountain Bell for services or products might be to obtain long-term prices and contract conditions. Conversely, Mountain Bell also obtains long-term revenue stability with which to determine probable revenue, and allocation of costs, particularly for unique needs which are not special assemblies, special arrangements, or other Part 4 services. The use of LRIC pricing is based on the same reasons here as it was for banded rates. Since tariffs will continue to exist, customers need no other ceiling protection since they can always rely on tariff rates rather entering into contracts. In addition, a customer may choose to contract for services at rates higher than existing tariff rates in order to obtain price stability or for any other sound business reason.

However, the plant used to provide contract services will not be deregulated as requested by Mountain Bell. While piecemeal deregulation

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2. It is the Commission's understanding, although not part of the record in this proceeding, that this approach corresponds with the open network architecture concept endorsed by US West before the Federal Communications Commission.

is a fact of life, there is no need to make the situation any more difficult than it is, nor did Mountain Bell produce any evidence to suggest that mere entry into a contract meets the statutory criteria of finding effective competition, let alone the public interest.

29. There is no need to file the contracts with the Commission; rather they should be maintained at Mountain Bell for investigation by the staff of the Commission. At this time, no special reports on the contracts should be required of Mountain Bell since the contracts should speak for themselves. Realistically, any effort to file an abbreviated summary of the contracts would surely be audited by the staff, comparing the summary with the actual contracts. Once the staff has reviewed some of the contracts, a summary may be more appropriate. We assume that with this grant of authority, Mountain Bell will enter into contracts. Thus, it is not necessary to inform the Commission of each and every contract. The staff's investigatory power should be adequate to ensure compliance. Mountain Bell stated that it would treat similar customers in a similar fashion, and the Commission expects Mountain Bell to do this since this is consistent with the statutory proscription against undue discrimination found in § 40-3-106, C.R.S. which is applicable to Part 3 services, including private line services, in addition to all other sections of Article 3, Title 40.

30. Finally, there is no evidence to support an automatic deregulation of a service or product based upon an artificial percentage of the number of customers entering into contracts or the number of circuits under contract. The Commission cannot provide Mountain Bell an automatic threshhold where deregulation could occur, since such a threshhold would be contrary to the statutory requirement that the Commission make a finding of effective competition pursuant to § 40-15-305(1)(b), C.R.S. Thus, that portion of Mountain Bell's proposal specifically is rejected. However, it is believed that the Commission's rules in Case No. 6636 will assist Mountain Bell with procedures and standards for seeking deregulation of Part 3 services in the future.

31. The Commission recognizes that it has not granted Mountain Bell deregulation as it requested in its Modification to Trial Data Certificate, but the Commission is granting Mountain Bell economic and competitive freedom and relief from traditional rate-of-return regulation in the private line market so it can operate in a competitive environment. With limited use of the Commission's jurisdiction, the difference between deregulation as viewed by Mountain Bell and the flexible regulatory treatment contained in this order may be one of semantics from a practical standpoint. The Commission must evaluate any additional progress which can be made toward effective competition before it can make the required findings and deregulate specific services.

32. Within the interLATA private line service market, it generally was agreed that a different situation exists. AT&TCOMM proposed either deregulation or "maximum reduced regulation". As previously noted, effective competition has not been proven with competent evidence for the interLATA market. However, because some competition does exist,

maximum reduced regulation is appropriate in the interLATA market for all providers. The Commission will adopt a scheme identical to that it has discussed for the regulation of the high-end or high-speed intraLATA private line market. It will retain jurisdiction over all private line services or products, but intends only to exercise its complaint jurisdiction and its audit powers to monitor the effects. All providers of interLATA private line services will retain the burden of proving their rates are reasonable in any rate cases filed with the Commission. Moreover, the Commission notes that there are already several competitors in this market, namely, MCI and Sprint, as well as AT&TCOMM. The Commission does not believe AT&TCOMM's advantage in this market requires unique treatment for AT&TCOMM. The Commission also will review these services in approximately one year to evaluate progress and determine if deregulation is appropriate as more fully described in paragraph 37.

33. As the Commission views HB 1336, interLATA carriers can enter the intraLATA private line market following approval, if required, by the Commission. In Case No. 6636, the Commission will determine if any certification is required, and, if so, to what extent. However, it is clear that the doctrines of regulated monopoly and of regulated competi- tion do not control the issuance of certificates in the event they are required. Should interLATA carriers, with any required Commission approval, enter the intraLATA private line service market, they will do so under conditions set forth in paragraph 32.

34. Obviously, the Commission is treating Mountain Bell differently from the interLATA carriers, particularly if those carriers enter the intraLATA market. The most significant reason is that Mountain Bell controls the monopoly, public switched-network and many bottleneck facilities. Although Mountain Bell contends that provisions of HB 1336 are enough to prevent it from unfairly using these facilities, the Commission will, through investigations by staff, review the use of these facilities. The Commission believes that HB 1336 contains numerous proscriptions which Mountain Bell is required to follow. Because the statute is clear, the Commission will not impose protective measures in anticipation of unlawful action as argued by several intervenors at this time. The Commission presumes Mountain Bell will follow the law.

Finally, to the extent Mountain Bell has treated certain offerings as special arrangements or special assemblies, the Commission will investigate the specific services and will make no ruling with respect to Lightway I, or Digicom I and Digicom III at this time. If these services involve the bona fide use of special arrangements or special assemblies, then they are deregulated as a Part 4 service. However, if not, they will be regulated within the scheme described in this order.

35. The Commission is aware of the concerns of the independent telephone companies with respect to FX and FCO services. However, the fact that Mountain Bell or any other provider can serve within an independent's territory, creating a potential for a large customer to bypass the independent, is a result of HB 1336 and the opening of the private

line market, not this order. Article 5 of Title 40 concerning certification is not applicable to Part 3 services. The Commission must foster beneficial competition in the rural areas, not inhibit it. The scenario painted by the independents of a large customer leaving an independent system to obtain FX or FCO service may be real, but neither the independents or Mountain Bell provided an example. Moreover, Mountain Bell asserted it would continue to provide FX and FCO services as it has in the past. Until Mountain Bell operates differently than it has, there is no need to take protective action now. Finally, to deny beneficial competition in rural areas would perpetuate unnecessarily the fact that currently the rural areas of Colorado do not benefit generally from competition.

36. The Commission staff will monitor the effects of this order, and, if necessary, may request providers to develop new computer programs for recordkeeping. The Commission recognizes that this may impose a burden, but agrees with *pro se* intervenor Parrish that the burden should only arise when developing the initial programs, and not continue after programs have been developed.

37. Mountain Bell's attorney stated that Mountain Bell has never had a need to prepare records necessary for the evaluation of the private line market. However, we find that basic financial and market information will be even more important in the future as a result of increasing competition and the flexible regulation described in this order. Therefore, the Commission anticipates that Mountain Bell and other providers of private line services will develop records and reports which would be necessary for them to monitor the success of their private line offerings in the normal course of business. At the conclusion of Case No. 6634, the Commission and its staff will be better equipped to determine if additional records are necessary for the staff to monitor the effects of this order. Minimal reporting is anticipated, and it is the intent of the Commission that the reports that are generated in the normal course of business, (such as, but not limited to, price lists, quantities of services sold, revenues, LRIC and other cost data as appropriate, and reports that may be required by the Federal Communications Commission) will be sufficient.

For the high-end or high-speed private line services, Mountain Bell should anticipate the need to separate the revenues, expenses, and investments associated with providing these high-end private services from the revenues, expenses and investments associated with all remaining private line services and all other services, in general. This separation is in anticipation that these high-end services may be first to be deregulated by the Commission. These services will not be subject to rate-of-return regulation. Mountain Bell will be allowed to earn whatever rate of return the marketplace allows for these services. These services will stand alone and not be included in the revenue requirement for all other regulated services offered by Mountain Bell. Mountain Bell should develop data which will reflect revenues, expenses, and investments associated with these high-end services, such as, but not limited

to, price lists, quantities of services or products sold, income statements and balance sheets specific to these high-end services. After March 1, 1988, these data shall be made available by Mountain Bell for staff audit on a quarterly basis, beginning with the period ending December 31, 1987, consistent with directives in Case No. 6634 to the extent it is completed.

As Mountain Bell noted in its closing argument, imputation of revenues, expenses and investments for Part 3 services, including private line services, may be appropriate when revenue requirements for Part 2 services are being determined.

These proceedings will be set for further hearing to supplement this record beginning August 29, 1988. It is the intent of the Commission that providers can present additional evidence without repeating the evidence which is already of record in these proceedings. This approach preserves the record already established while complying with the intent of the General Assembly to issue a final decision by October 30, 1987. After one year, the effects of this order may be evaluated, since the consumers of private line services will have had some time to adjust to the conditions, and the providers should be able to offer more substantial, empirical, and Colorado-specific evidence of effective competition within the relevant markets.

SUMMARY OF FINDINGS AND CONCLUSIONS OF LAW

In addition to those matters discussed previously, the Commission finds and concludes as follows:

1. Mountain Bell has failed to establish with competent evidence that effective competition exists for any private line services or any submarket within the private line service market.

A. There are significant economic and technological barriers to market entry and exit, specifically right-of-way costs for wireline services, security problems for microwave and satellite transmissions, and for coaxial cable used by the cable TV industry, line-of-sight problems for microwave systems, and capital and financing requirements for all entrants.

B. Mountain Bell has demonstrated that there are a number of providers offering similar services, but that the majority of these providers are poised to enter the private line market as a result of the enactment of HB 1336, rather than providing significant competition today. However, with HB 1336, it can be expected that more providers may provide alternatives to Mountain Bell's private line services in the future.

C. A vast majority of the consumers who require high-end or high-speed private line services can obtain those services, primarily

using microwave technology, at reasonable and comparable rates on comparable terms and under comparable conditions; however, the evidence does not support a similar finding with respect to all other types of private line services. The Commission does not find that the General Assembly intended for every single consumer to have such alternatives available and will not require Mountain Bell to demonstrate that each and every consumer has reasonable alternatives in future proceedings.

D. While the Commission believes Mountain Bell has the ability to affect prices or deter competition, the Commission expects Mountain Bell to comply with HB 1336, particularly with respect to avoiding cross-subsidization and illegal restraint of trade. Therefore, the Commission requires that Mountain Bell not exercise its ability to affect prices or deter competition.

E. With respect to AT&TCOMM and any other providers of private line services in Colorado, the Commission finds that no Colorado-specific evidence was provided concerning the degree of competition within the state as a whole, or within the interLATA market, specifically. Therefore, the same findings contained in subparagraphs A through C apply to private line services offered by all providers other than Mountain Bell.

F. Because AT&TCOMM and other interLATA providers control neither bottleneck facilities nor the public switched network, the Commission finds it has fewer concerns about their abilities to adversely affect prices or deter competition. As a result, the Commission finds that maximum flexible regulation for these providers is appropriate, even if they enter the intraLATA market.

2. The Commission finds that the degree of regulation described in this order will promote competition and allow a reasonable transition period to evaluate the effect of this regulatory scheme. By allowing Mountain Bell, AT&TCOMM or any other providers to supplement this record with additional evidence concerning effective competition and the public interest, the Commission will minimize duplication of effort.

3. By promoting competition in this fashion, the Commission finds the public interest will best be served and that the competition it encourages by this order will lead to the provision of adequate and reliable private line services at just and reasonable rates. This order provides for minimal regulation by the Commission where appropriate, and flexible regulation for all other categories of private line services.

4. The Commission finds that the regulatory scheme described in this order permits Mountain Bell, AT&TCOMM and any other providers economic and competitive freedom to respond to competition, virtually eliminates the use of traditional rate-of-return regulation for private line services, provides flexible regulatory treatment for these services as contemplated by HB 1336, and promotes competition within the private line market, statewide.

O R D E R

THEREFORE THE COMMISSION ORDERS THAT:

1. Application No. 37367, filed by The Mountain States Telephone and Telegraph Company on November 26, 1985, and amended by a modification to trial data certificate, filed on August 28, 1987, is granted in accordance with this Decision and Order, and in all other respects is denied.

2. The request filed in Case No. 6633 by AT&T Communications of the Mountain States, Inc., for deregulation or flexible regulation of its private line services in Colorado is granted in accordance with this Decision and Order, and in all other respects is denied.

3. All requests to deregulate or flexibly regulate private line services made by other providers in Case No. 6633 are granted in accordance with this Decision and Order, and otherwise are denied. Upon its own motion, the Commission will order flexible regulation of private line services for interLATA providers in accordance with this Decision and Order.

4. All providers of private line services in Colorado, subject to the jurisdiction of this Commission, shall comply with the terms and conditions set forth in this Decision and Order and shall participate in Phase II of the proceedings in Case No. 6633 and Application No. 37367, established by Interim Order No. R87-1072-I, as appropriate, to implement the segregation of investments and expenses associated with the provision of private line services in Colorado. Phase II of these proceedings shall be consolidated with Case No. 6634, concerning segregation of investments and expenses.

5. For purposes of res judicata, collateral estoppel, and petitions for reconsideration, reargument, or rehearing, only those matters contained in the Findings of Fact and Conclusions Thereon in this Decision and Order are final. Any other matters raised in Case No. 6633 or Application No. 37367 which specifically have not been ruled upon by this Decision and Order subsequently may be raised in Phase II of proceedings in Case No. 6633 and Application No. 37367, or in other proceedings.

6. No declaratory order is issued with respect to Lightway I or Digicom I and Digicom III offerings in this proceeding at this time. These offerings will be considered in Case No. 6645, concerning Part 4 services, described in Title 40, Article 15, of the Colorado Revised Statutes.

7. Further orders with respect to Phase II in Case No. 6633 and Application No. 37367 will be issued by the Commission as necessary.

8. Case No. 6633 and Application no. 37367 shall remain open both for the purpose of Phase II, segregation of investments and expenses

associated with the provision of private line services in Colorado, and for further hearings in approximately one year for the further evaluation of the status of the private line markets and the impact of the flexible regulatory treatments provided for in this Decision and Order.

9. The Mountain States Telephone and Telegraph Company shall work with the staff of the Commission to develop a monthly report concerning lost revenues associated with the provision of private line services as a result of competitive activities, which was previously ordered by the Commission to be prepared by Mountain Bell only and which has been provided by Mountain Bell in an unsatisfactory manner in the past.

10. This Decision shall be considered as a final Decision, subject to the provisions of § 40-6-114 and § 40-6-115, C.R.S.

11. The 20-day time period provided by § 40-6-114(1), C.R.S., to file an application for rehearing, reargument, or reconsideration begins on the first day after the mailing or serving of this Decision and Order.

12. By Interim Order No. R87-1227-I, parties desiring a transcript of these proceedings were required to make an appropriate request by September 28, 1987. That order shall be modified to reflect that any requests for a transcript or portion of the transcript shall be made in writing and filed with the Commission and its Chief Court Reporter, Norman Reinholtz, no later than September 30, 1987, at 3:00 pm.

13. This Decision and Order shall be effective 30 days from this date.

DONE IN OPEN MEETINGS of September 25 and September 28, 1987.

THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF COLORADO

Arnold H. Cook

Andra Schmidt

Ronald L. Lehr

Commissioners

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