STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

OPINION NO. 98-10

CASE 94-C-0095 - Proceeding on Motion of the Commission to Examine Issues Related to the Continuing Provision of Universal Service and to Develop a Regulatory Framework for the Transition to Competition in the Local Exchange Market

CASE 28425 - Proceeding on Motion of the Commission as to the Impact of the Modification of Final Judgment and the Federal Communications Commission's Docket 78-72 on Provision of Toll Service in New York State

OPINION AND ORDER ESTABLISHING ACCESS CHARGES FOR NEW YORK TELEPHONE COMPANY AND INSTITUTING A TARGETED ACCESSIBILITY FUND

Issued and Effective: June 2, 1998

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BY THE COMMISSION:

INTRODUCTION

The core issue in this phase of these proceedings is the level of the carrier access charges[1] levied by New York Telephone Company d/b/a Bell Atlantic-New York (New York Telephone) on toll or interexchange carriers for origination and termination of calls upon its local network. Access to this network is essential for any long-distance carrier doing business in New York State. The genesis of this phase was the interexchange carriers' claim, supported by the Consumer Protection Board (CPB), that excessive access charges inflate intrastate toll rates, constrain toll growth, and give New York Telephone an unfair competitive advantage as it fully enters the

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[1] An access charge is a charge made by a local exchange carrier for use of its local exchange facilities for a purpose such as the origination or termination of traffic that is carried to or from a distant exchange by an interexchange carrier.

toll market. For its part, New York Telephone proposed a revenue-neutral rate redesign, eliminating time-of-day discounts and instituting a new presubscribed line charge.

Another core issue concerns the creation of a Targeted Accessibility Fund (TAF), to support Lifeline, E911, and Telecommunications Relay Service (for the hearing impaired), on an explicit, competitively neutral basis. Carriers propose to recover TAF outlays through a surcharge on customer bills.

Upon review of the evidence presented, the recommended decision and the parties' exceptions, we conclude that promoting competition and improving economic efficiency require an immediate reduction in New York Telephone's carrier access charges, in a manner that precludes any impact on basic local service rates, and that passes these savings on to toll customers as toll carriers have pledged to do.[1] As to design of New York Telephone's access charges, the time-of-day discounts will be retained and proposals to institute a presubscription charge are rejected. Finally, the Targeted Accessibility Fund will be established, without the surcharge.

BACKGROUND

The Competition II Proceeding

In the Competition II Opinion and Order,[2] we established principles for a universal service policy for residential customers. Among other things, we identified the following as attributes of basic local telephone service:

1. Single party access line
2. Access to local/toll calling
3. Local usage
4. Tone dialing
5. Access to emergency services
6. Access to assistance services
7. Access to telecommunications relay services

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[1] See Cases 96-C-0603 et al., Proposed Bell Atlantic/NYNEX Merger, Opinion No. 97-8 (issued May 30, 1997), p. 31.

[2] Case 94-C-0095, Opinion No. 96-13 (issued May 22, 1996).

8. Directory listing
9. Privacy protections.

We charged the parties with developing details to implement an explicit, competitively neutral, targeted funding mechanism to support programs such as Lifeline, emergency services (911), and the Telecommunications Relay Service. With regard to affordable rates, we reasserted the long-standing policy to ensure that basic services are affordably priced, noting that the incentive rate plans for New York Telephone and Rochester Telephone afforded such rates to 95% of the local telephone customers in the State. Finally, we initiated a further phase of that proceeding to consider the overall level of interexchange carrier access charges and universal service funding.

On June 10, 1996, we further charged the next phase of these proceedings to make recommendations related to the definition of basic service and its universal availability, and carrier access levels and rate design, in the context of the transition to competition. We also charged this phase with addressing whether basic service is priced below its cost and, if so, to what extent must it remain priced below cost to maintain universal service. Finally, the instituting order consolidated Cases 94-C-0095 and 28425, for the purposes of reaching a permanent solution to the designated carrier problem and of examining carrier access costs.

Procedural History

The interexchange carriers viewed the central issue as the level of intrastate carrier access charges levied by New York Telephone, and sought an immediate, substantial reduction of these charges to their incremental cost, proffering cost studies and testimony to bolster their allegations. New York Telephone, in contrast, asserted that its rates, including access charges, were determined on a company-wide basis, without regard to the cost of particular services; that the Commission had no authority to reduce access charges below the levels established in its Performance Regulatory Plan (PRP);[1] and, therefore, that there were no evidentiary issues. The Bell Atlantic/NYNEX merger and the state approval determinations, along with the continuing federal judicial and administrative litigation under the Telecommunications Act of 1996 (the Act), punctuated the schedule of this phase.

On November 26, 1996 Administrative Law Judge Eleanor Stein delineated four issues to be decided in this phase. The first, and most immediate, concerned an interim extension of the Designated Carrier Plan (DCP), regarding pooling and independent companies' access charges which had been arrived at by the parties and approved, with clarifications, in September 1996.[2] The second group of issues concerned universal service funding and comprised two distinct undertakings: the Targeted Accessibility Fund and a possible second fund, if necessary, to ensure affordable basic rates for companies not under long-term incentive plans. This inquiry implicated another issue, controversial among the parties at the time, as to whether any revenues from such a fund should be available to New York Telephone to indemnify it against any diminution of its interexchange access revenues. The third issue concerned the level and design of interexchange access charges; and the fourth entailed an examination of the discount rate the Commission was to establish, pursuant to the Act, for schools, libraries, and rural health care providers.[3] Working committees of the parties, facilitated by Staff, were formed to address

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[1] A seven-year performance-based incentive regulatory plan for New York Telephone was adopted in August 1995. Case 92-C-0665, Performance-Based Incentive Regulatory Plan, Opinion No. 95-13 (issued August 16, 1995).

[2] Cases 94-C-0095 et al., Order Adopting Agreement With Clarifications (issued September 18, 1996).

[3] 47 U.S.C. §254.

collaboratively the discounts for schools, libraries,[1] and rural health facilities, and the TAF.

In January 1997, parties filed comments concerning the impact of the Act and FCC regulations on interstate access charge issues. In February 1997, an effort was made to facilitate joinder of issue among the parties, in light of the complexity of the concerns before the group and the range of viewpoints, by having the parties offer off-the-record presentations of their general views on the advisability of reforming carrier access charges in the environment of full service and network element competition.

Parties indicated concern that our determination in Cases 95-C-0657 et al. (the Network Elements proceeding), regarding costs for network elements, would affect the testimony they intended to file in these proceedings and the method and outcome of the costing inquiry in the access charge context. Subsequently, the litigation schedule in this case was revised to accommodate the Network Elements proceeding decision schedule. Parties were informed that testimony should identify and assign costs to those aspects of any remaining network elements, if any, that, taken in conjunction with those already assigned a price by the Commission, constitute the package defined by the Commission as basic local exchange service. In June 1997, AT&T Communications of New York, Inc. (AT&T) moved for streamlining the litigation process by appointment of a special master to determine cost issues; New York Telephone and MCI Telecommunications Corporation (MCI) opposed the request,

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[1] The working group on schools and libraries discounts became the New York Committee for Schools and Libraries, which arrived at a consensus plan. Following several hundred comments upon the plan, and a final determination by the Federal Communications Commission (FCC) adopting a plan for universal service support for schools, libraries and rural health care providers, we adopted discounts for services for schools and libraries tracking the federal plan. (Cases 94-C-0095, et al. Opinion No. 97-11, issued June 25, 1997).

preferring the existing litigation process, and the AT&T request was denied.

The parties proceeded to file testimony, responsive testimony, and pretrial briefs. An on-the-record evidentiary hearing was held in August 1997, producing a transcript consisting of 1,097 pages; 51 exhibits were admitted into evidence. Following the hearing, Staff[1] requested additional information from the parties concerning rate design, local exchange cost studies, and interexchange carrier flow-through of any carrier access charge reductions. Moreover, as a result of issues that came to light at the hearing, an August 27, 1997 ruling by Judge Stein required parties to modify their cost studies to reflect four concerns: exclusion of toll usage costs and revenues from basic service; inclusion of flat rate usage costs and revenues; modification of local usage costs resulting from identification of intrabuilding (central office) calls; and inclusion of retail costs associated with basic local service. Accordingly, revised cost studies, and comments on those studies, were filed in November 1997. Finally, comments, briefs, and reply briefs were filed by New York Telephone, AT&T, MCI, Sprint, ALLTEL New York (ALLTEL), CPB, Time Warner Communications Holdings, Inc. (Time Warner), Frontier Telephone of Rochester, Inc. (Frontier), WorldCom, Inc. (WorldCom), Empire Association of Long Distance Telephone Companies, Inc. (Empire/ALLTEL), Small Company Group, and Bell Atlantic Mobile, Inc. (Bell Atlantic Mobile).

On January 23, 1998, a Recommended Decision was issued. Initial and/or reply briefs on exception were filed by AT&T, Bell Atlantic, Bell Atlantic Mobile, CPB, Frontier, Taconic Telephone Corp., MCI, New York Clearing House Association (NYCHA), Small Company Group, Sprint, ALLTEL, and Time Warner.

[1] Department of Public Service Staff did not act as a party in this phase of the proceedings. An Advisory Staff team was coordinated by Daniel Martin and Angelo Rella.

<u>The FCC Access Charge Order</u>

The Telecommunications Act of 1996 (the Act) mandated that federal and state universal service support mechanisms should be "specific, predictable, and sufficient"[1] and that implicit subsidies had to be made explicit "to the extent possible."[2] In May 1997, the FCC reduced the level of access charges somewhat and, with perhaps greater impact, redesigned those rates, both to identify implicit universal service subsidies and to better align the charges with the way the costs are incurred.[3]

In its order, the FCC lowered total carrier access charges by $1.7 billion nationwide. Roughly one fifth of these access charge reductions, approximately $350 million, result from actual reductions to local exchange company access revenues, achieved by lowering those companies' price caps. The balance of the reduction is funded by increases to multiple line business and non-primary residential line rates, and through various other shifts of recovery of non-traffic sensitive costs from usage to flat rate charges. The FCC did not reduce interstate access charges to incremental cost; indeed, its reductions were, in absolute amounts, modest, to avoid feared disruptive effects on ratepayers and the affected local exchange companies. Instead, it adjusted interstate access rates to more closely align charges with costs, and relied on competition to further drive down the price of access in the marketplace.

The FCC recognized that states were initially responsible for identifying implicit intrastate subsidies.[4] As a practical matter, however, the FCC action imposed considerable pressure on states to act for, without reductions in intrastate

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[1] 47 U.S.C. §254(b)(5).

[2] 47 U.S.C. §254(e).

[3] CC Docket No. 96-262, First Report and Order (released May 16, 1997) (the Access Charge Order).

[4] <u>Ibid.</u>, ¶¶ 10-13.

access charges, a call from New York City to Buffalo might eventually cost more than a call from New York City to San Francisco.

NEW YORK TELEPHONE'S ACCESS CHARGE LEVELS

The Parties' Contentions

New York Telephone argued current carrier access charges were reasonable. In the eyes of the interexchange carriers, however, they are excessive in comparison to the cost of providing switched access; and the interexchange carriers and CPB urged us immediately to reduce them to incremental cost. More specifically, the interexchange carriers took the position that rates for carrier access should be reduced to the Total Element Long Run Incremental Cost (TELRIC) for local access, on the ground that the identical network elements provide the identical functions in providing these two services: they are distinguished only by their purpose, not by any technical difference.[1] This position was succinctly summed up by its proponents as: "A minute [of access] is a minute is a minute."

New York Telephone offered numerous indications that competition is vibrant in both the local or switched access and toll markets, and that mandated access charge reductions are unnecessary. Time Warner and ALLTEL concurred. MCI, AT&T, and Sprint refuted this showing with their own demonstrations that only a small fraction of switched access lines are offered by competitors of New York Telephone. Time Warner, on the other hand, asserted that the market forces should be relied on to put downward pressure on access charges.

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[1] The possible applicable statutory standards, costing approaches, and models were reviewed in Cases 95-C-0657 et al., Network Elements, Opinion No. 97-2 (issued April 1, 1997).

The Recommended Decision

In the recommended decision, the Judge found, with respect to New York Telephone, that (1) carrier access charges are at least three times the incremental cost of providing access; (2) on a forward-looking basis, the revenues associated with the provision of basic local service cover the costs of providing that service;[1] (3) under certain circumstances the disparity between the cost and price of carrier access can be anti-competitive; and (4) toll customers are unduly burdened by pricing access so far above cost.[2]

Based on these findings, the recommended decision called for a reduction in New York Telephone's access charges of $120 million annually. The recommended decision suggested that toll carriers be ordered to flow these savings through to the broad range of their residential and business customers and to so indicate on customers' bills.

The recommended decision identified certain revenues that could be made available to allow New York Telephone to recover some of this loss. First, the revenue impact under the recommended decision would be moderated by applying $23 million of revenues resulting from an increase in federal payments to New York Telephone in support of the Lifeline program; by our order, those revenues are now being deferred.[3] Second, the recommended decision suggested we approve the proposal of the industry

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[1] All cost studies were done on a forward-looking, not embedded, cost basis. On exceptions, New York Telephone and AT&T challenge some aspects of the analysis contained in the Staff Cost Report comparing basic local service costs and revenues. Although some of these exceptions will be granted, the net effect of these adjustments does not alter this finding.

[2] The recommended decision also recommended determinations concerning independent companies’ access revenues. Because revenue losses are at issue, and several of these companies have requested ice-storm related relief, these issues have been severed for consideration of those impacts.

[3] Cases 94-C-0095 et al., Universal Service and Access Charges, Order Directing Deferral (issued December 24, 1997).

collaborative process to establish a Targeted Accessibility Fund to support Lifeline, E911, and other services, and to add a surcharge to end-user bills to match each company's payment into that Fund. All regulated carriers would pay into the fund, based on a percentage of their intrastate revenues. Carriers providing the services would recover their net costs from the fund. The surcharge would generate an additional $48 million in New York Telephone revenues. These payments would cover New York Telephone's TAF-related expenses which are currently being recovered through the company's rates, and offer the opportunity to reduce the company's access charges by that amount. The Judge recommended that New York Telephone could seek recovery for the balance of the access charge revenue reduction by demonstrating that it had complied with the standards established in the merger determinations.[1]

The Parties' Exceptions

1. Policy Exceptions

a. In General

New York Telephone excepts only to $49 million of the proposed $120 million reduction, while observing that the recommended decision does not account for associated toll revenue reductions resulting from the need to lower its toll and individual calling plan rates to compete with interexchange

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[1] Cases 96-C-0603 et al., NYNEX/Bell Atlantic Merger Petition, Order Approving Proposed Merger (issued March 21, 1997); Opinion No. 97-8 (issued May 30, 1997). The recommended decision also offered an alternative approach, pursuant to the two orders approving the Bell Atlantic/NYNEX merger: the reduction of access charges to forward-looking cost if New York Telephone failed to establish, in the near future, that its conduct has promoted competition, its customers have benefitted, and consumers have shared in the merger cost savings. Most parties take exception to this approach; MCI would read the alternative as proposing a subsequent access charge reduction in addition to that recommended by the Judge. On reply, New York Telephone urges rejection of this proposal. We decline to adopt it, as an immediate, partial reduction more appropriately addresses the need for economic efficiency and competitiveness.

carriers' reduced rates. It suggests new price ceilings should reflect any offset from the TAF, calculated as an exogenous revenue increase under the PRP. Time Warner excepts more broadly, asserting the record demonstrates that immediate reductions will disrupt competitor local carriers' revenues and business plans.

AT&T, Sprint, MCI, WorldCom, and CPB continue to urge an immediate full reduction to forward-looking cost. AT&T points out that the Judge recommended the $120 million reduction as a minimum and characterizes this recommendation as conservative, arguing that the record supports at least an additional $100 million reduction. Further, AT&T urges that the current access charge regime be replaced with a single, forward-looking, cost-based integrated rate structure, pricing carrier access and exchange access identically. Sprint views the recommended decision as a step in the right direction but believes the record and recommended decision findings support immediate full reduction to cost. It suggests, as an alternative, that we accept the recommended decision's reduction for now but set a schedule for a transition to access charges to forward-looking cost no later than the earlier of New York Telephone's interLATA entry or January 1, 2001.

In reply, New York Telephone reiterates its preference for a market-driven approach and asserts that no access charge reductions should be ordered until it is in the long distance market. In addition, it counters the views of AT&T and WorldCom that it would not be harmed financially by this loss of revenue.

b. <u>Competitive Impacts</u>

On exceptions, New York Telephone contends no party presented evidence to warrant any access charge reduction, and excepts to such proposed reduction as exceeds the revenues suggested for recovery.

New York Telephone also excepts to two of the findings supporting the recommended access charge reductions; in its view the record indicates market forces should be allowed to set access charges.[1] It excepts to the findings that current access rates burden toll customers and give New York Telephone an unfair market advantage. New York Telephone asserts that the discrepancy between incremental cost and service prices results from shared fixed costs and is not evidence of inefficient pricing. In support, it notes prices in the highly competitive toll market incorporate roughly a 400% markup over incremental cost. Additionally, New York Telephone contests whether moving only one price toward incremental cost maximizes efficiency for a regulated firm, with its interrelated service prices, each with its own associated incremental costs. Finally, New York Telephone argues that it is the toll markup, not the disproportion between price and cost for access, that prejudices toll customers. On reply, CPB counters that excessive carrier access charges distort investment decisions and harm efficient toll competition.

New York Telephone also excepts to the recommended decision’s finding that it may enjoy an anti-competitive advantage.[2] In support of its exception it adduces that the opportunity cost of selling access to toll carriers ensures it includes the contribution foregone from not selling access to a toll carrier in its profitability calculations for its intraLATA toll service.

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[1] New York Telephone also excepts to the absence of consideration of the impact on its toll rates of a $120 million access charge reduction (New York Telephone’s Brief on Exceptions, p. 5, n. 3), and urges that if it estimates toll revenue impacts in its compliance filing, it be permitted to do so in conformance with the PRP methodology.

[2] New York Telephone excepts to the recommended decision’s conclusion that the incumbent local exchange carrier is advantaged by the difficulties and delays inherent in policing imputation, asserting this conclusion is unsupported by the record and contrary to recent precedent.

c. The Merger Standards

The Administrative Law Judge found that the Commission, in the merger determinations, so modified the PRP as to allow reconsideration of New York Telephone's access charge levels to maximize competition and efficiency, and substituted a new standard for recovery for that agreed to by New York Telephone in the PRP. In agreeing to the terms and conditions attendant upon the Commission's approval of the merger, she continued, New York Telephone effectively waived its objection to consideration of its access charge levels in this phase of these proceedings. And while the Judge accepted New York Telephone’s view of the standards for modification of access charges--i.e., that access charge reductions may be required if necessary to promote competition or improve economic efficiency[1]--she rejected New York Telephone’s restrictive interpretation of the efficiency test, which limits it to the efficiency of New York Telephone. She found more reasonable and analytically useful the broader interpretation offered by the interexchange carriers: that we consider overall market efficiencies.

New York Telephone excepts to both the interpretation and the application of the merger standard. It excepts to the recommended decision interpretation of "improve efficiency" in the merger order to refer to market efficiency, reiterating its view that its own efficiency is what is at issue. In addition, it excepts to the conclusion that access charge reductions are necessary to improve market efficiency, the threshold under the merger orders. Sprint interprets the recommended decision to provide for reductions only if and when New York Telephone fails to meet the merger standards and, on reply, New York Telephone urges that interpretation.

[1] Cases 96-C-0603 et al., Proposed Bell Atlantic/NYNEX Merger, Opinion No. 97-8 (issued May 30, 1997).

d. Flow-through

CPB urges adoption of its proposal that all toll customers share in the flow-through of access charge reductions, and calls for monitoring of toll prices to prevent subsequent toll price increases. Sprint stands by its flow-through pledge, although asserting that the intensely competitive toll market will force flow-through even without regulatory oversight and seeking the latitude to decide where to apply reductions. But Sprint opposes the suggested requirement that access charge reduction flow-throughs be reflected on customers' bills, on the grounds that such bill entries are unnecessary, difficult to calculate under the various calling plans, expensive, and confusing to customers.

NYCHA and SIA assert, on reply, that their experience at the FCC indicates that only an explicit statement on end-user bills will ensure access charge reduction flow-through. CPB urges rejection of Sprint's request for discretion in directing the flow-through, reasserting the importance of flowing through reductions to all customers.

2. Exceptions as to the Staff Cost Report

a. Introduction

We have recognized that contribution from non-traffic sensitive access charges served the objective of keeping down monthly charges for subscriber access to the system and promoting universal subscription to telephone company networks. Indeed, there was little or no dispute in these proceedings that the common regulatory practice has been to encourage or require local telephone companies to price services other than basic local service at profit maximizing levels in order to exact contribution from those services to hold down the rates for basic service.

In the instituting order, we mandated this phase of these proceedings to address whether or not, in fact, basic local service was subsidized by access charges. In defining this inquiry for New York Telephone's costs and rates, the starting places were the definition of basic local service in the Competition II opinion and the costs assigned to the network elements considered in Cases 95-C-0657 et al.

New York Telephone argued consistently that the use of forward-looking cost studies for this purpose is an irrelevant exercise, inasmuch as it is entitled to recover in rates not only the forward-looking but the fully embedded costs of providing basic service, and it prepared the cost studies under protest. The interexchange carriers responded that the Act's requirement of explicit, competitively neutral universal service support compels the use of forward-looking cost models.

The Administrative Law Judge concluded that were the purpose of this exercise to set rates for New York Telephone's basic local service, its challenge to the use of TELRIC, as defined in the Network Elements proceedings, might be valid. But because we mandated this inquiry into the costs of basic local service in order to establish whether there is a subsidy for those costs, she considered forward-looking costs appropriate for this analysis.

At the Judge's request and in collaboration with her, Staff carried out an exhaustive review of the materials prepared by the parties, and the Judge adopted this Staff Cost Report. The principal conclusion of the Staff Cost Report was that the examination of New York Telephone's basic local service costs and revenues on a forward-looking basis reveals that revenues roughly equal costs.

b. General Exceptions

New York Telephone excepts to the use of TELRIC for identifying the cost of basic local service, asserting that while the recommended decision purports to use TELRIC only to determine universal service funding needs, it bases a rate reduction on TELRIC findings.

Further, New York Telephone excepts to drawing the conclusion that if there is no basic local service subsidy, there is no universal service justification for access charges above incremental cost. It argues that if basic local service does not contribute proportionately to shared fixed and common costs, that shortfall must be made up by other services.

As to the general exceptions concerning the use of TELRIC, New York Telephone notes that "[n]o disagreement exists in the case concerning the proper economic test for a subsidy: a service receives a subsidy if the additional revenue the firm receives because it supplies the service fails to cover the additional costs that the firm incurs to provide the service."[1] But it asserts its rates must be set based on total costs, not only forward-looking but embedded, and that the recommended decision in fact used TELRIC analysis not for universal service purposes but for setting rates. MCI replies that the recommended decision properly used forward-looking costs to determine whether local service needs a future subsidy from other services.

The exception regarding the use of TELRIC is denied. The Staff Cost Report is not the basis for the recommended rate reduction, but illustrates the long-standing subsidy debate. New York Telephone does not claim it cannot cover TELRIC costs at the rate recommended here. Nor do the data indicate otherwise. Indeed, as to the specific Staff Cost Report cost and revenue inclusions and exclusions, these determinations on exceptions result in increasing the adjusted contribution to local service from a positive $8 million to a positive $85 million, approximately 3% of local service revenues.

c. Specific Exceptions

i. Inclusion of Interstate Access Charge Revenues

New York Telephone argues the Staff Cost Report improperly included $218.5 million of interstate access charge revenues from the carrier common line (CCL) charge. In its view, attributing revenues from a non-local service, that is,

[1] New York Telephone’s Brief on Exceptions, p. 10.

interstate toll, to basic local service is inappropriate because (1) the revenues are uncertain; (2) the CCL charge is associated causally with interstate, not local service; and (3) only the revenue associated with supplying basic local service should be considered in measuring incremental revenue from supplying an additional basic local service unit.

AT&T, supported by CPB, defends the Staff Cost Report's inclusion of these revenues on the grounds that Staff was required to include the revenues associated with the 25% of loop costs allocated to the interstate jurisdiction because it included 100% of the cost of the local loop, without recognizing jurisdictional separations.

The exception is denied. Although the CCL revenues are generated from a rate imposed on toll usage, and thus are derived from toll service, it is important to recognize that, in the long run, the level of revenues collected is tied to the level of basic service costs; these revenues are intended by the FCC to cover a portion of the cost of the local loop. Furthermore, even if the CCL revenues were ignored, basic service revenues would still roughly equal the cost of providing basic service, falling short of those costs by less than 5%.

ii. <u>Non-recurring Charges</u>

MCI claims Staff's analysis is erroneous in that it, like New York Telephone's cost studies, includes the expenses for non-recurring charges but fails to incorporate the revenues associated with the expenses. MCI is incorrect. New York Telephone filed revised cost studies with its Initial Brief that included $152 million of non-recurring revenues, which were included in Staff's adjusted local service contribution studies. MCI's exception is denied.

iii. <u>Cost Estimates for Local Switching</u>

New York Telephone excepts to Staff’s approach to estimating the cost of local switching, asserting that it violated the fundamental rule that rate computation must be consistent with rate application. New York Telephone also contends that the cost of an intraoffice call equals the cost for the originating plus terminating portions of an interoffice call; in Staff’s view, the relevant cost of an intraoffice call equals half the cost of an interoffice call.

On reply, AT&T asserts the only record data setting forth a specific method for calculating these costs is AT&T’s cost study documentation in the Resale/Network Elements Proceeding. It charges New York Telephone’s workpapers fail to support its claim that the minutes used to determine local switching unit costs were developed according to its exception, and it argues that New York Telephone’s method is unsound.

New York Telephone has not supported its contention that the cost of an intraoffice call is the same as the cost for the originating plus terminating portions of an interoffice call. Also, we reject its contention that the costs at issue only pertain to the line side of the switch because the trunk side functions are dealt with separately in its analysis. In fact, although the costs of ports on the trunk side of the switch are captured in other rate elements, the same holds true for the costs of the line side ports. What is at issue here is the cost of the switching components between two ports.

New York Telephone has not provided evidence to support its rate computation (i.e., that the minutes in the denominator of the calculation are the claimed total half call minutes). Absent such a showing, we have no assurance that a correction to the application of the rate will not exacerbate the error associated with the computation of the rate. Accordingly, New York Telephone’s exception is denied.

iv. Application of the Tandem Trunk Port Rate

AT&T does not appear to except to the recommendation to adopt New York Telephone’s proposed rate design charging separately for the trunk ports on either side of the tandem switch. AT&T excepts to Staff’s computation of the tandem trunk port rate approved in Opinion No. 97-2, consistent with New York Telephone’s claim that the minutes of use relied upon in the calculation be consistent only with the costs related to a single tandem trunk port. In AT&T’s view, the minutes of use implied by the traffic factors used to develop the unit costs from the switch investment were based upon "suspect" New York Telephone workpapers. In reply, New York Telephone asserts procedural issues: first, that issues litigated in its Resale/UNE proceeding cannot be relitigated here; and, second, that AT&T failed to raise the issue of tandem trunk traffic in the evidentiary phase and, therefore, may not raise it on exception. Substantively, New York Telephone counters that because tandem trunk traffic is a combination of primary tandem and overflow traffic from subtending end offices, there is no reason tandem and end office trunks should display similar traffic characteristics.

The application of the trunk port rate separately for the ports on either side of the tandem that New York Telephone proposed, and Staff recommended, is preferable, and the exception is denied. As explained in the Staff Cost Report, if AT&T’s proposal were to be adopted, the output generated by the Hatfield model would need to be restated on a per-individual-trunk basis before averaging with the New York Telephone cost figure. However, Staff concluded no adjustment was warranted to the trunk port rate approved in Opinion No. 97-2 because other factors, such as an understated per tandem investment figure in the Hatfield model, mitigated the resulting overstatement of costs.

AT&T’s exceptions entail resolutions adjusting the AT&T estimate upward to reflect a higher input for tandem switching costs, halving the resultant AT&T cost to reflect only the port on one side of the tandem, possibly adjusting the New York Telephone estimate downward to correct for an understated tandem minute annualization factor (if AT&T's argument is correct), and finally averaging the resultant AT&T and New York Telephone estimates. Even if the sum of all these adjustments were to change the final port costs by a factor of two, applying the trunk port rate only once would change the total level of annual local usage costs by roughly $18 million. Therefore, AT&T's exceptions are denied.

v. Inclusion of Special Pension Enhancement Costs

New York Telephone alleges on exceptions that Staff improperly excluded from its calculations $139.5 million of special pension enhancement (SPE) expenses. In the wholesale discount phase of Case 95-C-0657,[1] New York Telephone had urged that these costs, related to retail service, be excluded from the calculation (thereby reducing retail costs and, correspondingly, lowering the wholesale discount) because they were non-recurring; we rejected that proposal. Here, New York Telephone applied an adjustment to include those costs, and it maintains that Staff failed to adopt that adjustment.

In reply, AT&T correctly notes that Staff's retail costs did consider the SPE expenses. Attachment B of the Staff Cost Report, which contains Staff's determination of retail costs, used the indirect expenses the Commission allocated to retail activities in Opinion No. 96-30. Thus, Staff's adjusted retail costs fully consider the SPE costs, consistent with Opinion No. 96-30. New York Telephone's exception is denied.

[1] Cases 95-C-0657 et al., Wholesale Discount Rates, Opinion No. 96-30 (issued November 27, 1996).

vi. Local Service Allocation Percentages

AT&T excepts to Staff's use of New York Telephone's claimed "local service percentages" for determining retail costs. For example, New York Telephone's 88% allocation of customer accounting expense was based upon access lines, which only removes non-local service lines and assumes all customer accounting expense for local service access lines is related to basic local service. According to AT&T, that is not the case; for example, toll and vertical services have customer accounting. Also, AT&T asserts, New York Telephone never provided evidence that 85% of its service orders will be for bare bones basic local service in a forward-looking marketplace in which services will be packaged.

AT&T's arguments have some merit. The Report adopted New York Telephone's adjustment, excluding vertical features costs and revenues. However, like basic service, vertical feature services have retail activity associated with them. New York Telephone's adjustment did not consider the related costs. We therefore determine the costs eliminated for features be increased by $77 million as follows:

Vertical Feature Revenues	$ 405 million
NYT's Current Wholesale Discount Rate	19.1%
Vertical Features Retail Costs	$ 77 million

vii. Productivity Factor

AT&T excepts to Staff's use of a 10% productivity adjustment, pointing to additional savings resulting from the Bell Atlantic/NYNEX merger. In reply, New York Telephone notes that our decision relied upon in the Staff Cost Report was issued one month after the completion of the merger and took it into consideration. In addition, New York Telephone asserts that it faces competitive factors driving its retail costs upward, ignored by AT&T. The exception is denied, based upon the Resale/UNE determination.

Conclusions

1. Access Charge Levels

The institution of a surcharge to fund the TAF, although unanimously supported by the industry, can still be seen as an inadvisable local rate increase. Although toll customers as a group would presumably benefit from toll reductions in at least the same amount as the surcharge increase, these reductions would not flow through dollar-for-dollar to individual customers, and those using little toll would only experience the local rate increase, not the toll reduction.

Without the TAF surcharge, $48 million applied by the Recommended Decision to reduce access charges becomes unavailable.[1] Accordingly, we have examined varying levels of reductions.[2]

One possibility is to mandate no reduction below PRP levels in New York Telephone’s access charges at this time, as New York Telephone and facilities-based CLECs urge. New York Telephone argues that if there is sufficient development of competition in the market for local exchange or carrier access services, significant market share loss may force New York Telephone to reduce its carrier access charges of its own volition. And the facilities-based CLECs maintain that a reduction in New York Telephone's carrier access charges, while advantaging competitors in the toll market, disadvantages local

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[1] Because the establishment of a TAF spreads the costs of local providers' Lifeline, E911, and Telecommunications Relay Services (for the hearing impaired) over all telecommunications carriers, New York Telephone will realize some positive balance of revenues above costs even without a surcharge; that balance can be applied to access charge reduction.

[2] New York Telephone offers that if access charges are not driven down by competition, $50 million will be available for rate reductions in the later PRP years (New York Telephone Reply Brief on Exceptions, p. 4, n. 5). The PRP provides for $25 million rate reductions in the years 2000 and 2001, to be determined (PRP, IV(B)(1)); we agree with New York Telephone that this might be an appropriate application of those reductions, but will not reach that issue at this time.

exchange competitors that have flourished in the generous margin afforded them between the cost and the price of providing carrier access. These parties favor allowing local exchange market competition to put downward pressure on access charges, and urge us to follow the example of the FCC which, while redesigning carrier access rates, did little to reduce them in absolute terms, preferring to rely on market forces. But we are persuaded by the interexchange carrier showing that current rates are uneconomic; accordingly, some reduction is required to promote competition and improve efficiency.

The $120 million rate reduction recommended in the Recommended Decision, with collateral effects and without the $48 million offset afforded by the TAF surcharge revenues, leaves New York Telephone the opportunity to seek recovery of considerable revenues by the end of Year 7 of the PRP. In light of the burden this might place on ratepayers, we reject this option.

On balance, we will adopt a substantial reduction in carrier access charges, but at a level below that of the recommended decision. A reduction of approximately $85 million will be sufficient to conform intrastate intra- and interLATA access charges; would have no collateral rate effects inasmuch as New York Telephone does not compete for in-region interLATA customers; would leave the ratepayers with far less rate recovery exposure should New York Telephone establish it has met the merger standards; and would still afford considerable relief to the toll carriers. This level of reduction also still leaves room for a competitive local exchange market, as it develops, to drive access charges farther down.

2. Recovery Under the Merger Standards

The merger determinations established that we could reduce New York Telephone's access charges based on a finding that a reduction was necessary to promote competition or improve efficiency; and that New York Telephone could seek to recover the resulting revenue loss by showing that: (1) its conduct has promoted competition; (2) customers have benefitted from competition, including price reductions beyond those mandated by the PRP; and (3) consumers have shared in the merger cost savings.[1]

AT&T asserts, on exceptions, that consideration of recovery is premature and, ultimately, bounded: it agrees New York Telephone may seek to recover some portion of the revenue loss upon demonstrating its customers have shared in the merger cost savings; however, it asserts, it will not be entitled to dollar-for-dollar recovery, and the extent of the recovery lies in the future discretion of the Commission.

New York Telephone concedes it is exposed to access charge losses by reason of competitive inroads over time. A decision that it is necessary to expedite the customers' benefits from competition should not have the effect of indemnifying New York Telephone against these losses. Moreover, it is difficult to predict the competitive circumstances New York Telephone will face at the time it seeks recovery. Accordingly, we are ordering the reduction with the proviso that New York Telephone may seek recovery for revenue losses pursuant to the merger determinations; neither the conditions nor the probability of such recovery is addressed here.

New York Telephone's carrier access charge will be reduced by $85 million. This is a reduction sufficient to give some relief to toll carriers and customers and to conform inter-

[1] Cases 96-C-0603 et al., supra, Order Approving Merger (issued May 30, 1997).

and intraLATA access charges.[1] Moreover, at this figure there are no cognizable associated net revenue losses.[2]

3. Competitive Local Exchange Carriers' Access Charges

Under our existing policy, competitive local exchange carriers are authorized to levy access charges subject to the constraint that their rates not exceed those of the largest carrier in the LATA without a showing that higher rates are cost-based and in the public interest.[3] Accordingly, absent further action, the access charges of competitive local exchange carriers in New York Telephone's LATAs, and new entrants, must be reduced along with New York Telephone's. This link should be maintained. In what is an increasingly vertically integrated environment, with companies competing to provide both local and long distance service, access charges should be symmetrical.

4. Average Revenue Per Minute and Flow Through

Currently New York Telephone is realizing an average revenue per minute (ARPM) of $0.0201 for its intraLATA carrier access charges, and an ARPM of $0.0359 for its interLATA carrier

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[1] By conforming intra- and interLATA access under this scenario, rates would average $0.0201 per minute. Currently, however, the average rate per minute for intraLATA access in the upstate area is approximately $0.0170 as a result of imputation failure of one of the company's optional calling plans, and a subsequent Commission order to reduce access charges further than provided for in the PRP. In order to avoid an additional imputation problem, upstate access rates should remain unchanged until the imputation deficiency is resolved.

[2] This level of reduction only reduces interLATA access charges. Because New York Telephone does not currently provide interLATA service in New York State, this reduction has no competitive effect on its toll charges. InterLATA service is not addressed in the PRP.

[3] Case 94-C-0095, Universal Service (Competition II), Opinion No. 96-13 (issued May 22, 1996), p. 26.

access charges. Evening and night/weekend discounts differ in both the percentages and the time periods in which they apply. The ordered reduction will result in one carrier access rate and realize an average ARPM of $0.0201, with the existing discount levels associated with downstate intraLATA access service and existing time periods associated with upstate intraLATA access now also applying to interLATA and downstate intraLATA access services. The rate elements will mirror the elements charged at the federal level, to the extent discussed herein. Additionally, we will continue to allow the upstate intraLATA ARPM to remain at current levels (approximately $.017). This lower ARPM resulted from an imputation failure of one of New York Telephone’s optional calling plans, and should remain at this level until the plan passes imputation. These changes will result in an estimated annualized revenue loss of $85 million. The ARPM of $0.0201 will replace the rate targets contained in the Plan.

AT&T, MCI and Sprint, in this proceeding, stated their intentions to flow through the carrier access charge reductions to their customers. We will require that these companies reflect their commitments by filing revised tariffs concurrent with New York Telephone’s carrier access reduction, along with supporting documentation which shows that 100% of the reduction applicable to each company is being flowed through. We expect that these toll reduction proposals will benefit most customers, both business and residential.

NEW YORK TELEPHONE ACCESS CHARGE RATE DESIGN

Introduction

New York’s intrastate access charge structure contains three elements: common line, local switching, and local transport. These categories roughly represent the different elements or functionalities of the network used to provide different aspects of what constitutes access. The common line charge represents the relevant portion of the cost of the local loop, considered non-traffic sensitive. Common line charges are paid by interexchange carriers based on minutes of use, and subject to two time-of-day discount plans: for interLATA calling (15% for evening, 30% for night) and intraLATA calling (40% for evening, 65% for night).[1] Local switching rates are currently levied by minutes of use, with discounts for interLATA calling of 15% for evening and 30% for night use, and discounts for intraLATA calling of 40% for evening and 65% for night use. Local transport intrastate rates are a complex hybrid of minutes-of-use and flat-rated components, with time-of-day discounts applying to the minutes-of-use portion of the charges.

New York Telephone proposed rebalancing carrier access charges to conform to the interstate rate design.[2] The proposal entailed elimination of all time-of-day discounts; and, for common line charges, New York Telephone proposed establishing a flat-rated charge to interexchange carriers for each presubscribed line, comparable to the new FCC presubscribed interexchange carrier or PICC.

MCI, Sprint, and AT&T proposed an incremental-cost-driven access rate structure. They concurred in urging that the carrier common line charge be eliminated; that local switching and transport be priced at the rates established in the Network Elements Proceeding; that the intrastate access charge structure be conformed to the interstate; and that the time-of-day discount be ended. Time Warner proposed that intrastate access charges should complement the federal access charge reform efforts and urged that any changes be competitively neutral, decrease administrative burdens, and allow for an orderly transition to competition.

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[1] In contrast, the interstate access charge structure has levied common line charges on end-users through the Subscriber Line Charge (SLC), with interexchange carriers paying the balance of the interstate common line charge based on minutes of use, without any time-of-day adjustment.

[2] New York Telephone noted that the PRP provides for it to request revenue neutral carrier access rate restructuring. PRP §IV(D)(6).

The Recommended Decision

The Administrative Law Judge’s recommendations were first, to reduce the interLATA average revenue per minute (ARPM) to the intraLATA level and conform time-of-day discounts statewide and, second, to reject the proposals for a federal-style PICC or presubscription line charge. The net effect of these recommendations was to avoid incentives to increase off-peak toll prices; conform intra- and interLATA access charges; and spare end-use customers any new state-mandated presubscription charge.

The judge concluded as well that time-of-day discounts should be retained on the grounds that they were cost-based, as shown in the access cost studies filed by New York Telephone, AT&T, Sprint, and MCI, and that any rate restructure that would increase existing night and weekend carrier access rates could ultimately result in increases in end-user rates for those time periods.

The Parties’ Exceptions

Generally, New York Telephone excepts to the rate design recommendations as contrary to the PRP provision allowing it to request revenue neutral rate restructuring subject to our approval but not, in its view, allowing us to impose an alternative proposal on it. It also raises specific objections, as do other parties.

1. The Presubscription Charge

New York Telephone proposed a flat-rated per-line charge to interexchange carriers for both intra- and interLATA presubscription, comparable to the federal PICC; it did not expect interexchange carriers to pass through this charge directly to their customers. With the exception of AT&T, which took no position, all other carrier parties supported the institution of a presubscribed line charge, in part to mirror the federal access charge structure. The recommended decision noted that a presubscribed line charge would lead over time to a decline in access charges, inasmuch as access minutes are increasing faster than presubscribed lines. The Judge nevertheless recommended rejecting the proposal, on the grounds that it could be passed on directly to end-users and might burden mass market toll providers, as well as residential and small business end-users.

Sprint excepts to the recommended rejection of a presubscription charge, on the grounds that such a charge would promote consistency between state and federal mechanisms. In reply, NYCHA opposes Sprint’s position, asserting customers should not have to pay an additional fixed charge absent deeper access charge cuts.

Sprint’s exception is denied. The institution of a new flat rate increase, in addition to recent new FCC flat charges, would unduly burden customers, as the Judge found.

2. Time-of-Day Discounts

New York Telephone excepts to the time-of-day recommendations, citing unintended consequences resulting from the access price reductions. New York Telephone asserts the recommendations would actually increase evening and night intraLATA access charges in the upstate LATAs and the night intraLATA access charge in the Metro LATA; moreover, its upstate personalized rate plan would fail the imputation test. New York Telephone seeks sufficient pricing flexibility to maintain different inter- and intraLATA rates and different upstate and downstate discounts.

The exceptions are denied, leaving time-of-day discounts in place. To address the asserted imputation concern, upstate intraLATA access rates will be maintained as necessary to pass imputation. If New York Telephone chooses to voluntarily further reduce downstate access charges to maintain competitive flexibility, it may certainly do so.

3. Originating and Terminating Access

Although several parties urged that any access charge reductions should target terminating access, on the ground that these charges were less susceptible to competitive pressures, the recommended decision suggested evenly dividing the proposed reductions between originating and terminating charges, out of concern about unintended consequences of asymmetry.

On exceptions, MCI and WorldCom urge priority for reducing terminating access charges to economic costs, claiming no competitive alternatives exist for terminating access. In reply, New York Telephone adduces evidence of alternatives, including dedicated access, and unbundled network elements, an alternative for reaching all customers. New York Telephone also reiterates that originating and terminating access have the same costs.

The reduction should apply evenly to originating and terminating access, as any New York Telephone market share loss will affect both services; and there is no cost differential.

THE TARGETED ACCESSIBILITY FUND

In the Competition II opinion, we generally adopted the targeted accessibility fund (TAF) concept, designed to fund programs such as Lifeline, emergency services (E911), and Telecommunications Relay Service for the hearing impaired (TRS), on an explicit, competitively neutral basis.[1] In this phase of these proceedings, a collaborative working group (Working Group) of parties was formed, comprising incumbent and competitive local exchange carriers, interexchange carriers, and the Public Utility Law Project (PULP). The Working Group's meetings were facilitated by Staff, and it filed a report with the Judge.

[1] Case 94-C-0095, Opinion No. 96-13 (issued May 22, 1996).

The Working Group Report

Based on carrier responses to data requests and information provided by the Pool, the Working Group estimated TAF-eligible costs or foregone revenues at $50 million for Lifeline, $7.6 million for E911, and $16.9 million for TRS. The total projected cost was estimated at $74.6 million; however, subsequent additional federal Lifeline support reduced the state funding necessary by approximately $25 million. Accordingly, the overall size of the TAF is reduced by that amount, to a total of approximately $50 million.

The Working Group recommended that Lifeline funding be made available, for both the incumbent local exchange carrier and a facilities-based competitor, equal to the difference between the incumbent’s non-Lifeline and Lifeline rate.[1]

As to E911, the Working Group concluded that funded costs should include the costs incurred by the database administrator associated with the initial loading of data to its database, as well as the initial loading and recurring costs for other local carriers for collecting, processing, and submitting data to the database operator.[2] The trunking costs from the serving central office to the E911 tandem and the costs of provisioning up to two free trunks from the E911 tandem to the Public Safety Answering Points (PSAPs) will be recoverable through the TAF. The Working Group agreed that, for carriers unable to perform their own studies, the costs of the dominant incumbent local exchange carrier serving the LATA could be used as a proxy.

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[1] If a competitor does not offer a service comparable to the incumbent local exchange carrier, its recovery would equal that of the predominant incumbent local exchange carrier in the LATA for a comparable service.

[2] New York Telephone, Frontier, and ALLTEL currently assess a $0.03 per access line per month charge to counties to recover the ongoing costs associated with updating and maintaining their ALI databases. Therefore, ALI database operators will only be allowed TAF recovery for the initial loading costs associated with the operation of their databases.

As to the Telecommunications Relay System, the Working Group recommended that the costs of the operating center, currently operated by Sprint, as well as those associated with TRS Board meetings, auditing of provider data, and other Commission-authorized TRS functions, qualify for recovery.

The Working Group agreed that all regulated telecommunications carriers operating in New York State should be responsible for contributing to the fund. This included all local exchange providers, long distance companies, and cellular and Personal Communication Service (PCS) companies providing service on a facilities or resale basis. The Working Group reached a consensus regarding the basis for contribution to the TAF, conditioned upon the carriers being allowed to recover their assessments via an explicit surcharge on the end-users' bill. Each company contribution was to be based upon a percentage surcharge applied to its regulated, intrastate retail end-user revenues (excluding any revenues derived from services provided to other carriers, such as access, bottleneck billing and collection elements, wholesale services, or wholesale network elements).[1]

In the absence of a Commission determination allowing carriers the ability to generate TAF contributions through an explicit surcharge on the customer's bill, the carriers were divided as to an alternative basis for assessment. New York Telephone urged assessment based on all net intrastate revenue; AT&T and Frontier proposed netting intercarrier access payments against that figure.

Upon implementation of the TAF, all carriers providing the targeted services would be eligible to receive payments from the TAF as reimbursement for their costs. Adjustments would be made to current revenue streams to offset any new TAF surcharge

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[1] For administrative and cost savings reasons, the Working Group recommended that mandatory participation in the TAF be waived for extremely small carriers (under $10,000 in assessable intrastate retail end user revenues), and no party objects to this threshold.

revenues. All parties agreed that every new dollar of TAF payment should result in a dollar decrease in existing rates, to the extent that the costs of the targeted programs are currently being recovered in existing rates.[1]

The Working Group unanimously endorsed and recommended the New York Intrastate Access Settlement Pool, Inc. (Pool) as administrator of the TAF. The TAF administrator would be responsible for creating and distributing reporting forms, reviewing submitted data, issuing invoices to TAF participants, collecting TAF contributions, distributing TAF payments, and reporting to Staff and the Commission. The Working Group concluded that the TAF should be governed by an advisory board, consisting of a representative cross-section of telecommunications industry members and consumer representative organizations.

The Recommended Decision

The Judge's recommendation, generally, was to adopt the Report. However, since preparation of the Report by the Working Group, amendments to the Public Service Law were enacted concerning deregulation of cellular services. Parties were requested to address the effects of this change in their briefs on exceptions.

More specifically, the recommended decision adopted the surcharge (roughly .6% on a customer's total bill), and deemed the costs to be currently recovered through companies' rates, making approximately $50 million available for rate decreases. Further, the recommended decision suggested that New York

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[1] The concept of revenue neutrality was not extended to the competitive local exchange carriers. The Working Group concluded that a competitive local exchange carrier should be free to reduce its existing rates in response to any new inflow of revenue from TAF payments if it desires, but no requirement for such reductions should be imposed. The Working Group indicated that the competitive environment should be sufficient to control the need for competitive local exchange carriers to realign their rates in response to incumbent local exchange carrier reductions.

Telephone's portion of that $50 million, approximately $47 million, be applied to reduce carrier access charges.

The Judge also recommended conditioning the adoption of the surcharge upon also including the reflection, on the toll portion of customers' bills, of the rate decrease afforded customers as a result of flowing through access charge reductions.

The Parties' Exceptions

1. Application to Cellular Services

During the course of this phase of these proceedings, Bell Atlantic Mobile opposed requiring cellular and PCS carriers to participate in the TAF, on the grounds (1) that federal law preempted any such state commission action;[1] (2) requiring TAF funding by cellular alone, rather than all commercial mobile radio service (CMRS)[2] providers was both discriminatory and not competitively neutral; and (3) the TAF is an impermissible tax. The recommended decision adopted the Working Group proposal to assess all regulated telecommunications carriers for TAF contributions by dividing the statewide costs by total regulated intrastate retail end-user revenues generated by all carriers operating in New York. However, the recommended decision did not analyze the questions raised by the cellular carriers, instead requesting the parties to comment on recent amendments to the Public Service Law concerning cellular services.

On exceptions, Bell Atlantic Mobile reiterates its arguments, and asserts that the recent amendments suspend PSC jurisdiction, precluding the imposition on cellular services of

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[1] See 47 U.S.C. §§332(c)(3)(A), Omnibus Budget Reconciliation Act, and amendments in the Telecommunications Act of 1996, specifying preemption of state rate regulation of mobile carriers, and the exceptions thereto where those carriers substitute for landline carriers.

[2] The FCC defines CMRS to include private paging, business radio services, land mobile systems, cellular, offshore radio services, some mobile satellite services, PCS, and others. 47 CFR §20.9.

TAF assessments. Chapter 684 of the Laws of 1997, signed into law on December 1, 1997, added to the PSL §5(6)(A), providing:

> Application of the provisions of this chapter to cellular telephone services is suspended unless the commission, no sooner than one year after the effective date of this subdivision, makes a determination, after notice and hearing, that suspension of the application of the provisions of this chapter shall cease to the extent found necessary to protect the public interest.

Bell Atlantic Mobile asserts that the PSL amendment severs any jurisdictional link the Commission may have had to impose TAF funding requirements on cellular services; it asserts that link was already restricted by federal legislation prohibiting state market entry and rate regulation of all CMRS services, including cellular. WorldCom, in contrast, asserts that cellular services should be assessed for the TAF, on the grounds that they compete with landline service, and are a premium service. WorldCom suggests the Commission impose an additional TAF charge on local carriers and allow them to recover it through their charges for service to cellulars. In reply, New York Telephone disagrees, viewing this proposal as an indirect violation of Chapter 684.

AT&T, meanwhile, recognizes that this Commission no longer has rate or certification of entry authority over cellular services, but asserts that CMRS providers must contribute to the fund in the same manner as wireline carriers. In its view, however, federal and state law require that providers of cellular services should have the discretion whether and how to recover TAF contributions from their subscribers. AT&T seeks clarification that all facilities-based carriers, including carriers that bundle local exchange carrier elements in order to provide Lifeline services, should be eligible to recover costs from the TAF.

2. Wireless E911

The Judge recommended that E911 wireline costs of database loading and trunking be recoverable from the TAF. AT&T urges, on exceptions, that CMRS providers' implementation of wireless E911 as required by the FCC also be recoverable from the TAF. AT&T cites recent FCC requirements that CMRS providers make E911 available concurrent with the establishment of a state funding mechanism to reimburse them for their costs. In AT&T's view, exclusion of these costs from TAF is not competitively neutral, and the TAF should be adjusted to accommodate these requirements as necessary in the future. In reply, New York Telephone asserts that funding for Wireless E911 services will not be necessary until an authorized agency requests wireless E911 capabilities. New York Telephone states that no such request has been made and, therefore, AT&T’s exception is premature.

Discussion

Although we reject the Working Group proposal for establishment of a surcharge to fund the TAF, it nevertheless remains advisable to establish the TAF at this time, as a necessary vehicle to ensure that new entrants both contribute to and provide universal service. This is so even though New York Telephone, in the short run, will be both paying into and taking the lion’s share out of the Fund. However, as the transition to competition in the local exchange market proceeds, the TAF will become increasingly significant. Accordingly, the Fund should be established as proposed by the Working Group, as modified by the recommended decision, with additional modifications.

First, as noted, the surcharge proposal is rejected, and carriers will be allowed to meet their TAF obligations through their current revenues. As to the alternative methods for assessing carriers’ contributions to the Fund, we adopt the scheme offered by AT&T and Frontier, that is, assessment will be based upon relative regulated intrastate gross revenue, net of payments made to other carriers. As agreed by the Working Group, these payments include carrier access charges, bottleneck billing and collection elements, wholesale service, wholesale network elements, and operator services when bundled with services purchased at wholesale. In our estimation, this funding assessment method most fairly represents the relative current burdens and benefits of the TAF. In order to implement this determination, Staff will reconvene the TAF Working Group to address the applicable mechanisms and governance issues.

Second, the exception as to recovery of E911 wireless costs from the TAF is denied. A stronger showing would have to be made to entitled wireless service providers to reimbursement from a fund into which they do not pay.

Third, we will grant the state law exception as to exemption of cellular services from any Fund charges; therefore there is no need to reach the federal law issues briefed by parties. Consistent with that determination, providers of cellular service at this time are also precluded from recovery from the Fund and from participating in its administration. It is expected that, should providers of cellular services choose to offer New York customers these services, they will want to avail themselves of the TAF and accept responsibility for their share of the TAF assessment. Moreover, we may review the necessity of assessing cellular services for universal service purposes, including the TAF, in such manner and at such time as complies with the Public Service Law.

CONCLUSION

As to the level of New York Telephone access charges, an immediate reduction of approximately $85 million is ordered, as necessary for competition and efficiency. At this level, there are no additional associated revenue reductions; and this reduction will be offset by the $23 million federal Lifeline increase. As to the New York Telephone access charge rate design, we generally adopt the Judge’s conclusions, retaining time-of-day discounts and rejecting institution of a presubscribed line charge, but allowing New York Telephone sufficient rate design flexibility to ensure it complies with imputation rules.

Finally, the TAF should be established, but it should not be funded through a surcharge and cellular services should not be assessed for it.

The Commission orders:

1. To the extent it is consistent with this opinion and order, the recommended decision of Administrative Law Judge Eleanor Stein, issued January 23, 1998, is adopted as part of this opinion and order. Except as here granted, all exceptions to that recommended decision are denied.

2. Within ten days of the date of this opinion and order, New York Telephone Company (New York Telephone) shall file tariff amendments consistent with this opinion and order, to become effective on July 1, 1998, to reduce its existing interLATA carrier access charges to a level that realizes an average revenue per minute of $0.0201; and that produces interLATA access charge time-of-day periods with effective discounts of 40% in the evening period and 65% in the night/weekend periods, conforming to the current downstate intraLATA time-of-day discounts and upstate intraLATA time-of-day time periods. Further, New York Telephone Company shall file tariffs, within ten days of the date of this opinion and order, to become effective on July 1, 1998 to reduce its existing New York Metro LATA intraLATA carrier access charges to a level that realizes an average revenue per minute of $0.0201, and that produces New York Metro intraLATA access charge time-of-day periods with effective discounts of 40% in the evening period and 65% in the night/weekend periods, conforming to the current downstate intraLATA time-of-day discounts and upstate intraLATA time-of-day time periods. Upon filing those tariff amendments, New York Telephone shall serve copies on all active parties to these proceedings. Any party wishing to comment on the tariff amendments may do so by submitting 10 copies of its comments to the Secretary within 15 days of the date the amendments are

filed. The tariff amendments shall not take effect on a permanent basis until approved by the Commission but may be put into effect on a temporary basis on one day's notice, subject to refund if found not to be in compliance with this opinion and order.

3. New York Telephone Company shall file tariffs, to become effective no later than October 1, 1998, that reflect the carrier access charge rate design discussed in this opinion and order.

4. AT&T Communications of New York, Inc., MCI Telecommunications Corporation and Sprint Communications Company, L.P., shall file tariffs within ten days of the date of this opinion and order, to become effective on July 1, 1998, to decrease their annual intrastate toll revenues by an amount equal to the reduction they will receive in intrastate carrier access charges to New York Telephone Company, with supporting documentation that the reduction applicable to each company will thereby flow through, in its entirety, to its respective business and residential customers.

5. The requirement of the Public Service Law and 16 NYCRR 630.70 that newspaper publication shall be completed prior to the effective date of the amendments is waived, but New York Telephone Company, AT&T Communications of New York, Inc., MCI Telecommunications Corporation, and Sprint Communications Company, L.P., are directed to file with the Commission, not later than August 14, 1998, proof that a notice of the changes set forth in the amendments and their effective date has been published for four consecutive weeks in a newspaper having general circulation in their service territories.

6. The Targeted Accessibility Fund will be established, in conformance with the modifications in this opinion and order to the proposals of the Targeted Accessibility Fund Working Group and the recommended decision; Department of Public Service Staff will commence the implementation of this determination with the parties.

7. These proceedings are continued.

By the Commission,

(SIGNED) JOHN C. CRARY
Secretary

APPENDIX

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