Kearsarge Telephone Company
Merrimack County Telephone Company
Docket No. DT 07-027
Company Responses
To Bailey Phase II, Set 1 Data Requests
PUBLIC
May 22, 2009

BAILEY 1.35: Please attach a copy of the New York state case referenced on page 13 of Reed Supplemental Testimony.

RESPONSE: See Attachment TDS 0192-0222 for a copy of the Order Adopting Framework in New York Public Service Commission Case 07-C-0349.

Michael C. Reed is responsible for this response.

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on February 13, 2008

COMMISSIONERS PRESENT:

Garry A. Brown, Chairman
Patricia L. Acampora
Robert E. Curry, Jr.
Cheryl A. Buley

CASE 07-C-0349 – In the Matter of Examining a Framework For Regulatory Relief.

ORDER ADOPTING FRAMEWORK

(Issued and Effective March 4, 2008)

BY THE COMMISSION:

INTRODUCTION

After the Commission established a revised regulatory regime for Verizon New York Inc. and Frontier Telecommunications of Rochester in our Competition III Order,[1] several independent telephone companies petitioned for similar relief. This Order changes the way the Commission sets rates for the State's 38 small, independent telephone companies and authorizes differing degrees of pricing flexibility for 33 of them.

We adopt here a regime to set rates for the independent telephone companies that considers both the level of competition in each company's territory and the earnings level of each company. For this analysis, a market is defined as competitive

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[1] Case 05-C-0616 – Proceeding on Motion of the Commission to Examine Issues Related to the Transition to Intermodal Competition in the Provision of Telecommunications Services, Statement of Policy on Further Steps Toward Competition in the Intermodal Telecommunications Market and Order Allowing Rate Filings (issued April 11, 2006).

if a company that raises its prices loses revenue on an aggregate basis. Based on a price elasticity analysis from Competition III, that situation occurs when a substantial majority of a company's customers have access to both wireless and cable alternatives to landline service. Given the data provided in this case, we can make such a finding if the estimates are that more than 69% of customers have such alternatives.

The other aspect of the analysis considers each company's earnings adjusted to reflect the amount by which the company's costs differ from expected levels (unexplained CPAL, or cost per access line.) For companies with inexplicably high costs, the adjustment will serve as a surrogate for rate case adjustments. Companies with costs below average are seen as relatively efficient and will have their adjusted returns decreased, thus supporting the reasonableness of a rate increase. The reported earnings will also be adjusted for known rate changes, changes in subsidies from the Federal Universal Service Fund (USF), extended area service (EAS) and the New York Intrastate Access Settlement Pool (Intrastate Access Pool). This approach enables these companies to address revenue deficiencies without requiring the costs and complexities of a rate case.

For companies facing competition and earning a reasonable return, non-basic rate flexibility will be granted and basic rates will be allowed to increase up to $2.00 per year for two years (relief analogous to that granted in Competition III).[2] Using 2006 data, we determined that 20 companies currently qualify for this relief. Four companies are considered competitive but are earning excessively; these companies qualify for non-basic rate flexibility only.

In an attempt to streamline regulation, companies who are not facing a significant level of competition but have inadequate returns on equity will be permitted non-basic rate flexibility and $2.00 annual basic rate increases for two years provided that

[2] Competition III capped residential basic rates at $23 statewide. Increases to residential basic rates under this framework that bring rates above this benchmark will not be allowed and increases up to the benchmark under this framework will not qualify a company to draw from the Transition Fund established in Case 02-C-0595.

the allowed return on equity is not exceeded. This framework, which is not part of Competition III, recognizes that earnings of some of the small, independent companies that do not face a significant level of competition have, nevertheless, been depressed in recent years. Using 2006 data, nine companies qualify for these increases. And finally, the remaining five companies, which are non-competitive companies earning an adequate return on equity, will only be allowed to adjust rates with corresponding revenue neutral changes or by filing a full rate case.

BACKGROUND

In April 2006, the Commission issued our Competition III Order, approving residential pricing flexibility[3] for Verizon New York Inc. (Verizon) and Frontier Telecommunications of Rochester (Frontier Rochester) based on the competitiveness of the market and associated line and revenue losses to competition. While the Competition III Order did not authorize similar residential pricing flexibility to all of New York's incumbent local exchange companies (ILECs), it noted that some ILECs were experiencing similar line and revenue losses, and that additional analysis was required, on a company-by-company basis, to determine whether we could extend residential pricing flexibility to those companies.[4] In fact, the 29 rural ILECs have reported that they have lost on average almost 7% of access lines and 15% of minutes of use in 2007 alone.

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[3] Residential pricing flexibility permits certain non-basic rates to be increased or decreased quickly to meet market conditions and retain customers with competitive options. It can increase the possibility that the incumbent telephone companies will remain one of the competitive alternatives in the future and that the competitive marketplace is sustainable.

[4] Competition III Order, <u>supra</u>, p. 36.

In September 2006, Frontier Communications petitioned the Commission for residential pricing flexibility for its six other New York affiliates.[5] Similarly, in March 2007, the six Telephone & Data Systems, Inc. (TDS) subsidiaries each filed petitions for residential pricing flexibility.[6]

To help provide consistency in our consideration of the Frontier Communications and TDS petitions, as well as future filings for residential pricing and other regulatory relief, Staff of the Department developed and proposed a framework in April 2007 entitled "Framework for Regulatory Relief" to guide our action on such requests. The framework attempted to provide a consistent method for us to act on pricing flexibility requests from the smaller ILECs. The April 2007 framework determined the status of each company with respect to four dimensions: competitive presence, financial status, network investment, and operating efficiency. Included in the four dimensions were six indicators. The first indicator, Competitive Gateway was a "threshold" indicator meaning that absent significant competition, residential pricing flexibility or other regulatory relief would not be granted. For the five other indicators -- annual growth rate of revenues, return on equity, service quality, broadband deployment and unexplained cost per access line -- the April 2007 framework recommended certain levels of performance, however, it allowed for the possibility of further consideration in conjunction with individual company compliance filings for relief. The April 2007 framework was issued for public comment on April 20, 2007.

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[5] Case 06-C-1261 – Proceeding on Motion of the Commission to Examine Issues Related to the Transition to Intermodal Competition in the Provision of Telecommunications, Petition of Frontier Communications for Pricing Flexibility (filed September 14, 2006).

[6] Cases 07-C-0274 through 07-C-0279 – Petitions of Edwards Telephone Company, Inc., Port Byron Telephone Company, Township Telephone Company, Inc., Deposit Telephone Company, Inc., Oriskany Falls Telephone Corporation and Vernon Telephone Company, Inc. for Pricing Flexibility as Authorized in Case No. 05-C-0616 (filed March 5, 2007). Collectively referred to as the TDS petitions.

PARTY COMMENTS

In June 2007, comments were received from seven parties: AT&T Communications of New York, Inc. (AT&T), Frontier Communications (Frontier), the New York Coalition of Rural Independent Telephone Companies (The Coalition), the New York State Telecommunications Association, Inc. (NYSTA), Sprint Nextel (Sprint), Verizon New York Inc. (Verizon) and Warwick Valley Telephone Company (Warwick). The comments are summarized in Appendix A. Most parties recommended rejecting the April 2007 Staff framework in its entirety, arguing that it was more onerous than the method used to measure the presence of competition in the territories of both Verizon and Frontier Rochester in the Competition III proceeding. The parties' comments addressed not only the framework in its entirety, but also each of the determinative factors. Parties urged the Commission to focus on the forward-looking contestability of the market rather than use a Competitive Gateway that relies on past competitive losses. It was suggested that access line loss, minute of use loss, and density measures be eliminated from the Competitive Gateway evaluation. Parties suggested that these measures have nothing to do with a subscriber's decision to switch due to price. Parties also recommended that the other determinative factors included in the April 2007 framework be eliminated or significantly modified. In addition, the Coalition, Frontier, NYSTA, Verizon and Warwick all commented on staff's proposal to limit the use of promotions, granted under Section 92(5)(b) of the Public Service Law. Finally, AT&T and Sprint commented that switched access rates for the small companies should not exceed those of Frontier and Verizon; Warwick opposed lowering rates until the FCC completes its inter-carrier compensation reform.

DISCUSSION

The Commission concurs with the parties' concerns regarding the administrative complexity of the methodology used in the April 2007 framework and adopts a new methodology below. This methodology simplifies the April 2007 framework and focuses on two factors: 1) competitive presence as measured by the percent of cable and wireless alternatives available, and 2) an adjusted return on equity. These two factors will be used to determine each company's rate relief and pricing flexibility going forward. Our significant departure from the April 2007 staff framework obviates the need to address many of the parties' comments. As a result only those comments pertinent to the framework we are adopting will be discussed.

Competitive Presence

The revised framework measures competitive presence by the percent of cable and wireless competitive alternatives to landline service available to customers in each ILEC's service territory. It has been argued that competition, as determined using a forward-looking, dynamic framework based on contestable markets theory, is sufficient to assess the appropriateness of rates. Pricing flexibility for retail residential services is consistent with Commission precedent in the Competition III Order and is warranted by the competitive environment in this state. Simply put, if there is significant competition in an ILEC's service territory, that company should be granted pricing freedom. Thus, in order to grant an ILEC pricing flexibility, we must find that the ILEC is competitively constrained. The Competition III Order found Verizon and Frontier Rochester to be reasonably constrained, as the availability of competitive alternatives was such that those companies could not raise prices in order to generate extra revenues. A range of likely price elastic effects was analyzed in coming to this conclusion.

Our new methodology does not rely upon the arguably-complex Competitive Gateway and its six factor elasticity calculation contained in the April framework to evaluate the likely price elastic response of customers facing a price increase. Instead, it utilizes the elasticities[7] previously discussed in the April 2006 Competition III Order and requires that each ILEC have a significant percentage of customers with both cable phone and wireless alternatives available to them in order to be

7 Elasticity is the relationship between price and quantity sold. The theory is that the lower the price, the more you will sell.

deemed competitively constrained. The question that must be addressed is at what level that threshold should be set.

At the time of the Competition III Order, the percentages of Verizon and Frontier of Rochester customers with at least two competitive alternatives were 93% and 87% respectively. However, our Competition III Order indicated that these percentages were more than reasonable to constrain prices and thus a threshold percentage set somewhere in the range of these two percentages would be too high. In its September 2005 Competition III White Paper, Staff performed a revenue impact sensitivity analysis to illustrate the effectiveness of the uniformity rule. The revenue impact analysis indicated that a proportion of customers in an ILEC's service territory with both wireless and cable telephone options could be as low as 51% yet still reflect a situation where the uniformity rule would constrain the incumbent ILEC. At levels of 51% or greater, the analysis indicated that the ILEC would lose money to competitors if it attempted to raise prices. If the percentage was below 51%, the ILEC would have market power since it would generate more revenues from the customers that it keeps than it would lose from the customers who switched to alternative providers.[8] In its comments in this case, Frontier put forth a threshold availability of 80%, but did not provide a methodology to support this percentage.

Staff asked each of the companies to provide a more robust estimate of the availability of both platforms in their respective services territories and received responses in December 2007. However, since each company is providing an estimated percentage (i.e., none of the companies examined each and every customer location in the presence of two competitive alternatives), the reported percentages should be viewed within confidence bands.

[8] The 51% figure was determined via a revenue impact scenario that utilized price elasticities of -1.5 for customers with two alternative platform options and a -0.5 for customers without two competitive options. See page 24 of the April 11, 2006 Competition III Order and page 33 and Appendix E of the September 21, 2005 Staff White Paper for more details.

Staff obtained from each ILEC a comprehensive explanation, including appropriate supporting documents and work papers of the process and calculation used by each company to provide its estimates of the percentage of customers who have competitively provisioned cable and wireless available. Each submission included the name of the company expert who conducted the analysis and was attested to by an officer of the company.

The cable availability submissions were generally based upon the companies' knowledge of where cable facilities coexist on the same outside plant used to provide telephone services. The companies submitted telephone engineering maps and plant records upon which they indicated where cable plant coexisted. The companies used these maps and records to determine the percentage of customer locations which have both phone and cable service. We have reviewed these submissions and view this methodology as being reasonably accurate.

We do not have the same degree of comfort with the wireless availability submissions provided by the companies. In many cases, ILECs overlayed coverage maps obtained from wireless provider marketing web sites upon their own outside plant engineering maps. These wireless provider maps may not indicate the location of all "dead zones" or other quality problems which would limit cellular from being a substitutable service for traditional landline telephone service at each residential location. In other cases, the ILECs estimated cellular availability based upon the experience of company personnel in using cellular phones while in the field.

In order to verify the companies' wireless availability estimates, the Department purchased wireless coverage maps from American Roamer Inc. (www.americanroamer.com). The American Roamer maps rely upon generally accepted methodologies to identify where coverage "holes" exist in service areas. The Department of Public Service's Geographic Information Service (GIS) unit overlaid GIS versions of the American Roamer maps with maps in the GIS system which show ILEC service territory boundaries and residential household locations. The GIS unit then counted the number of households in each ILEC service territory which are also contained within areas which the American Roamer maps indicate have reasonable cellular coverage.

We think the software is a reasonable check on the submissions of the companies and we will rely on it as support. Accordingly, we conclude that wireless penetration at a threshold level, together with cable service, provides effective competition.[9] That level of competitive presence can be determined using a statistical methodology to set the threshold level at which we are reasonably confident that the reported threshold could not be lower than 51%. In other words, if the availability percentage reported by the company is high enough above 51%, we can be confident that the company does not have market power. The calculations result in a threshold of 69.3% based upon a 99% confidence level for each modality (i.e., cable and wireless).[10]

Adjusted Return on Equity

Although a telephone company may demonstrate a definitive competitive presence based on our model, its return on equity (ROE) must be examined given the Commission's continuing statutory obligation to ensure just and reasonable rates. Some parties commented that using the ROE subject to separations[11] potentially exceeds the Commission's jurisdiction. To avoid this concern, the companies' most recently reported 2006 intrastate ROEs will be used as a starting point.[12]

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[9] Based on confidential, company-reported data, most companies are constrained by the percentage of cable available.

[10] Given the 40 estimates for competitive availability, the binomial model is used to determine at what threshold percentage we would be 99% confident that the underlying level of competitive availability is not less than 51%.

[11] ROE subject to separations includes intrastate and interstate revenues and costs.

[12] ROE subject to separation will still have to be used for four companies that did not separate their revenues and costs in 2006. These ROEs will be compared to an appropriate, jurisdictionally-weighted allowed return. The companies are: Cassadaga Telephone Corporation, Delhi Telephone Company, Ontario Telephone Company, Inc. and State Telephone Company.

Because companies will not be subjected to a full rate case review of their books, the reported intrastate ROE will be adjusted to reflect the portion of intrastate unexplained cost levels, both high and low. Adjustments for costs that exceed the expected level will serve as a surrogate for potential rate case adjustments, and will increase the reported ROE. Adjustments for costs that are less than expected recognize companies that have found efficiencies and will reduce the reported ROE.

As part of its April 2007 framework, staff estimated a cost model for purposes of evaluating the relative cost efficiencies of the 40 incumbent local exchange telephone companies in New York State. The costs predicted by the staff regression model were stated on a cost per access line basis (CPAL)[13] and compared to actual costs levels. Companies with large amounts of costs over and above those predicted by the regression model were deemed to be relatively cost inefficient. Staff recognized that further refinement of its April cost modeling effort might be appropriate and, thus, invited parties "to propose analyses that better determine both the predicted CPAL and the causes of unexplained costs."[14] A number of useful criticisms and suggestions provided by the parties were reflected in our updates to the cost model.

The updated cost model differs from the April model in two major respects. First, the new model is more robust as it is estimated on data spanning the three year period from 2004 through 2006, whereas the April model was estimated using only 2005 data. Second, the updated model is more theoretically correct because it is based on the

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[13] The Cost per Access Line tool has been used to make financial adjustments in several other cases including: Case 02-C-0595, - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of the New York State Access Settlement Pool, Inc. for Traffic Sensitive and Non-Traffic Sensitive Access Rates; Case 04-C-1002, Crown Point Telephone Corporation's Multi-Year Rate Plan; Case 02-C-1294 - Minor Rate Filing of Chazy & Westport Telephone Corporation; Case 06-C-1257 – Newport Telephone Company's Multi-Year Rate Plan, and Case 92-C-0665, Investigation Performance-Based Incentive Regulatory Plans for New York Telephone Company – Track 2.

[14] April 2007 Framework, p. 29.

economic concept that costs are a function of both the outputs produced, and the prices of inputs purchased. The April model specified costs as solely a function of three outputs. In contrast, the revised model specifies costs as a function of three outputs and three input prices. The input prices used in the revised model reflect each company's relative economic cost of capital deployment, labor rates and costs of materials and services. The outputs are the same as those in the April model. Companies' costs should vary with the number of residence access lines served, the number of business access lines served, and the size of the service territory area over which each company's residence and business customers are located.

Our updated model reasonably addresses the parties' concerns by relying upon a more theoretically correct cost specification, and by increasing the data used to estimate the model from one year to three years. Unlike the April model, the updated model is not susceptible to change if either the five largest or five smallest companies are dropped from the analysis. In contrast with the April model, the revised model includes all possible interactions of the output variables and, therefore, does not raise questions over why certain interactions of the output variables were included and why others were excluded. The new model reflects the scaling of costs associated with smaller companies, costs associated with varying technology mixtures and the costs associated with the obligation to serve entire service territories. The revised methodology does not systematically underestimate predicted CPAL as did the April method. Appendix B contains a more detailed description of the updated CPAL method, as well as company specific CPAL results from the application of the methodology.

In addition to adjustments for unexplained costs, the reported intrastate ROE will be adjusted for known rate changes and expected changes in Federal Universal Service Fund, Extended Area Service and Access Pool subsidies and then compared to a table of allowed ROEs, as shown in Appendix C.

Relief to Be Granted

Based on the revised analysis, a company's level of competitive presence and adjusted ROE is used to determine the extent of regulatory relief that will be granted under the following four scenarios:

1. **Definitive competitive presence and a reasonable adjusted intrastate ROE.**[15]

In order to be included in Scenario 1, a company must demonstrate that more than 69% of its customers have two competitive options, and have an adjusted intrastate ROE less than the allowed ROE plus 500 basis points. Companies included in this category are either already losing revenues to competitors or are in imminent danger of doing so. Under Scenario 1, pricing flexibility will be granted at a level to match that granted to Frontier Rochester in Competition III (basic rates will be allowed to increase up to $2 per year for two years; unlimited non-basic rate flexibility). Basic rate increases will be limited such that the forecasted adjusted ROE after increases does not exceed the allowed ROE plus 500 basis points. The companies' rate levels and customer impacts will be revisited in two years. ROE levels will be checked again at that time.

2. **Definitive competitive presence and an excessive adjusted intrastate ROE.**

In order to be included in Scenario 2, a company must demonstrate that more than 69% of its customers have two competitive options, but have an adjusted ROE that exceeds the allowed ROE plus 500 basis points. Companies in this category are in danger of losing revenues but have financial results suggesting that no change in basic rates is necessary. Under Scenario 2, no increase will be allowed to basic rates without an offsetting reduction in access charges (as required under Competition III).[16]

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[15] A reasonable ROE for a company in a competitive environment will be considered as the allowed ROE level plus 500 basis points. This is consistent with our past treatment of excess earnings for the small ILECs. It also recognizes that these competitive companies face additional risks which, due to their small size and limited ability to quickly respond and adjust business and cost structures, could see some earnings erosion in the near term as they try to meet competition.

[16] Basic rates can be decreased as long as they are decreased uniformly across the service territory and there is not evidence of predatory pricing.

Unlimited flexibility will be allowed on non-basic rates. This acknowledges that competition is present in a company's territory by allowing more freedom to package services. The companies' rate levels will be revisited in two years and ROE levels will be checked again at that time.

3. **<u>Inadequate competitive presence and a sub par adjusted intrastate ROE.</u>**[17]

Companies that fall in Scenario 3 are not able to demonstrate that more than 69% of their customers have two competitive options, but their adjusted ROE is below the allowed level. Recognizing that company earnings have been significantly depressed due to some access line loss, reduction in minutes of use, and the reduction in subsidies from the Federal USF, the Intrastate Access Pool and EAS, expedited rate relief will be granted in the form of non-basic rate changes and up to $2 annual increases in basic rates for two years. Increases will be limited such that the forecasted adjusted ROE after increases does not exceed the allowed ROE level. Companies may file for additional consideration after the two year period.

4. **<u>Inadequate competitive presence and adjusted intrastate ROE greater than allowed.</u>**

Companies that fall into Scenario 4 cannot demonstrate that more than 69% of their customers have competitive options and their adjusted ROE is greater than the allowed level. No rate adjustments, other than revenue neutral changes as contemplated in the Competition III Order, will be permitted. Companies may file a petition with additional information to demonstrate their competitive and financial circumstances at any time.

Appendix D shows the results of the new model. Based on the companies' updated responses as to competitive presence and 2006 adjusted earnings, below is a summary of the number of companies that qualify under each of the above scenarios.

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[17] For companies in a monopoly environment, ROEs will be compared to the allowed ROE. No competitive increment will be allowed.

Scenario	Number of Companies	Rate Treatment
1 – Competitive Presence ROE less than allowed plus 5%	20	Non-Basic Rate Flexibility $2 Basic Rate Increase for 2 Yrs (limited to allowed ROE plus 5%)
2 – Competitive Presence ROE greater than allowed plus 5%	4	Non-Basic Rate Flexibility No Increase to Basic Rates
3 – Inadequate Competitive Presence ROE less than allowed ROE	9	Non-Basic Rate Increase allowed $2 Basic Rate Increase for 2 Yrs (limited to allowed ROE)
4 – Inadequate Competitive Presence ROE greater than allowed ROE	5	No increases allowed

This new approach responds to a number of the commenters' concerns that the original framework proposed in April was too cumbersome, too complicated and not forward looking enough. It relies on just two criteria, competitive presence and adjusted ROE, and the ROE analysis has been modified to address commenters' jurisdictional concerns and concerns about the original CPAL model. Ultimately, the updated approach grants some level of rate relief, based on a competitive showing, to 33 of the 38 companies[18] as compared to the original Framework which would have granted only 5 companies relief.

Accordingly, we find that companies meeting the competition standard (i.e., that at least 69% of its customers have two alternatives to wireline service) should receive the appropriate relief, depending on their adjusted returns, as described above. Those companies can file tariff leaves, effective on thirty days notice, to obtain appropriate relief. We will also follow the same process in subsequent years: We will verify company-reported data (based on Annual Reports and cable and wireless coverage

[18] As previously discussed, Verizon and Frontier of Rochester already have been granted rate flexibility under the Competition III Order.

submitted by March 31) to determine if additional companies satisfy the above criteria. Those companies that do will be notified and allowed to submit revised tariff leaves.

OTHER ISSUES RAISED BY PARTIES

Access Rates

AT&T and Sprint commented that any rate relief granted to small companies be tied to lowering of their switched access rates, which AT&T and Sprint deem high. Conversely, Warwick opposes any change until the FCC deals with intercarrier compensation reform.[19] We do not find that the flexibility to be granted needs to be linked with a reduction in access rates. Any review of the state's access charge structure would best be done in a comprehensive manner. However, we do not see a need to start a generic proceeding on access rates at this time.

Application of PSL 92(5) (b)

Section 92(5)(b) of the Public Service Law states that companies are allowed to offer free or reduced non-basic service (i.e., promotions) for a length of time determined by the company. This legislation was passed after the Commission granted non-basic rate flexibility to Verizon and Frontier of Rochester in Competition III. Subsequently, Verizon proposed a promotion – Save Bundle. The Commission was concerned that lengthy promotions would defeat the intention of the uniformity rule i.e., that customers in both competitive and non-competitive areas pay the same rate. In December 2006, the Commission issued the Save Bundle Order[20] which limited the duration for Save Bundle. We find that a similar limitation must be in place for the small companies.[21]

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[19] FCC CC Docket No. 01-92.

[20] Case 06-C-0954, Introduction of Verizon Save Bundle, Order Approving Tariff Filing (issued December 4, 2006).

[21] Companies wishing to use lengthy promotions could forego unlimited pricing flexibility, an option that was given to Verizon in the Save Bundle Order.

The "START" Plan

On November 7, 2007, the New York Coalition of Rural Independent Companies filed additional comments in this proceeding proposing its "Small Telco Regulatory Transition Plan" ("START" plan) to deal with the issues faced by its members. Procedurally, these additional comments were filed substantially past the deadline noticed for comments on the April 20, 2007 Framework.[22] Nevertheless, we will briefly address the issues raised.

The START plan consists of two phases. Phase I would establish policies to provide any Carrier of Last Resort ("COLR")[23] pricing flexibility similar to that granted to Verizon and Frontier Rochester in Competition III and reduce the regulatory burdens on such carriers. Phase II would begin a process to develop a State Universal Service policy and the establishment of a State Universal Service Fund.

Although not couched in terms of COLR, the new framework we are adopting addresses the issue of pricing flexibility based on individual service territory

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[22] This deadline was originally established as May 9, 2007 but later extended until June 23, 2007 to allow the parties additional time to comment on the issues and compile the requested data. In addition, Verizon filed comments on November 28, 2007 in response to the November 7, 2007 Coalition submission stating that prior to instituting any new proceeding to consider the aspects of the START Plan, the Commission should set a schedule for comments addressing the threshold issue of whether such proceedings would be appropriate in view of the history and current status of Cases 07-C-0349 and 02-C-0595.

[23] The Coalition defines a COLR as "an entity that, within its Commission-certificated service area, provides facilities-based local exchange service upon reasonable request to any individual or entity physically located within that certificated area." To date, the Commission has not seen a need to establish a COLR for telecommunications carriers and has instead relied on migration rules for exiting carriers.

2. The independent telephone companies in New York are authorized to file tariff leaves, effective on 30-days notice, consistent with this Order and the determinations contained in Appendix D to this Order.

3. This proceeding is closed.

By the Commission,

(SIGNED) JACLYN A. BRILLING
Secretary

differences. Further, in Case 02-C-0595, among other things, a timeframe was established for examining a State Universal Service Fund.[24] There, the parties agreed, and we concurred, that the discussion of a more permanent State Universal Fund should wait until the Transition Fund, which was established as a temporary funding mechanism, was forecasted to be exhausted. That now appears to be by mid-2010 (approximately 27 months) if existing rate cases grant companies' full requests. Accordingly, we will seek input on and address these issues and the START Plan in a separate proceeding in the near future.

CONCLUSION

We find that the revised framework addresses parties' comments that the former proposal was too cumbersome and more rigorous than that used in Competition III. The relief we are granting for companies facing competition is consistent with what the Commission granted Frontier Telephone of Rochester i.e., two dollar increases for two years and unlimited non-basic pricing flexibility. Companies not yet facing competition but struggling financially will receive some relief. We expect that the flexibility and rate relief granted will encourage these companies to continue investment in a modern infrastructure necessary to compete for customers.

The Commission orders:

1. The framework described in this Order is adopted as the regime to set rates for the independent telephone companies in New York.

[24] Case 02-C-0595 – Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of the New York Intrastate Access Settlement Pool, Inc. for Traffic Sensitive Access Rates, Order Adopting Comprehensive Plan (issued December 23, 2003).

COMMENTS

Access Service

AT&T and Sprint believe that high switched access rates should be lowered and not exceed those of Verizon and Frontier. Warwick opposes any lowering of access rates and states that any change to the rates should not be done until after the FCC completes it inter-carrier compensation reform.

Backsliding

Frontier states that no additional provisions are needed to prevent backsliding on service quality or other indicators. PSC Section 97(2) provides sufficient authority to the Commission to deal with backsliding. The Coalition believes that backsliding can be addressed through the monitoring of consumer complaints.

Competitive Gateway

Frontier states the Commission should not include broadband service commitments as a gateway for regulatory relief but rather specific broadband investment may be relevant to the disposition of Rural Telephone Bank (RTB) proceeds. The gateway as proposed contains a number of highly arbitrary elements: three of the six elements used to determine the elasticity factor have nothing to do with a subscriber's decision to switch carriers due to price. Growth rate of access lines and minutes of use (MOU) have little to do with a subscriber's behavior, customers care about alternatives and what they cost. Frontier competes with cable, CLECs, VOIP and wireless. Frontier believes that competition in 80% of a ILECs exchanges is sufficient to measure pricing flexibility. Frontier suggests that a competitive gateway is appropriate such as the presence of at least two switched based competitors offering residential service, wireline or wireless in a company's territory. By definition, if there are three viable switched based competitors providing residential services that are sustainable for each other, competition is occurring.

Verizon believes that the Commission should take the attributes of each particular alternative service into account for the relative price portion of the Competitive Gateway.

Carrier of Last Resort

The Coalition believes the Commission needs to recognize the Carrier of Last Resort responsibilities and obligations of each coalition member including the need to respond to competition. There should be an assurance of recovery mechanisms for the infrastructure that the members provide. This should be done through rate design and a State Universal Service Fund.

Cost per Access Line (CPAL)

The Coalition and NYSTA both reject Staff's reliance on CPAL as it is without basis and it is inevitable that CPAL will increase with competition and the model can not incorporate all potential cost differences between companies nor take into account economies of scale and density. Frontier believes that the CPAL gateway should be eliminated at this time but re-established with more robust data. Verizon argued that variation in company sizes makes meaningful cost predictions unlikely. They also remarked that the cost regression breaks down if repeated without the five largest companies and that the April 2007 model predicts negatives economies of scope in the joint provision of residence and business lines. Finally, Verizon states that the April staff methodology systematically underestimates predicted CPAL by a factor of 1.046. Warwick wants to have company specific costs and circumstances to be investigated to determine if a company is operating efficiently, not just use the unexplained CPAL model currently used.

Density Calculation

Verizon believes that the density calculation has to be modified to reflect total number of lines or line-equivalents "in-play" which would include the incumbent's access lines as well as resold lines, UNE loops, lines provided by cable companies and wireless connections. The attributes of alternative services as wireless have to be included as it provides mobility that traditional service does not – a price for value issue.

Elasticity

The Coalition states that the Commission should modify the weighting of the six elasticity factors to increase the weighting of access line growth and minutes of use growth relative to elasticity. The Commission should also consider expanding the elasticity factors. Frontier believes that three of the six elements used to determine the elasticity factor have nothing to do with a subscriber's decision to switch carriers due to price. Also, growth rates of access lines and minutes of use have little to do with a subscriber's behavior. The main thing customers care about is alternatives and price. Frontier and Verizon both believe that there is a need to change the 2.5% threshold percentage revenue loss used since it appears to be results oriented --if used, it should be for any loss of revenues.

Infrastructure

The Coalition states that infrastructure development should be encouraged as good competition can exist only if there is a good underlying backbone infrastructure. The Commission needs to look at what already exists and what is likely to exist -- competition is here. Wireless carriers report coverage in excess of 75%, VOIP already exists. Coalition members have already lost access lines and revenue from intrastate access minutes.

Measuring Competition

The Coalition states that there is no industry definition for broadband other than that provided by the FCC. The market for the provision of high speed access is competitive and either the market or the FCC will define broadband requirements. Frontier believes that if there is competition in 80% of an ILECs exchanges that is sufficient to grant pricing flexibility. In addition, modify the 90% penetration requirement as there is no empirical evidence that it is the right number. NYSTA wants the DSL capability requirement eliminated as it is beyond Commission jurisdiction and goes beyond the Competition III requirements applied to VZ and Frontier. VZ states that when the Commission is measuring competition all potential competitive modes should be measured for example, non-cable VOIP, fixed and mobile wireless and fiber based technologies. DSL should not be given preference as a broadband option. Warwick states that the Commission should only evaluate competition as the basis for relaxing or terminating rate regulation.

One Way Ratchet

Verizon states that opening markets to competition is a one way ratchet and lifting and then imposing regulatory restrictions on companies will disrupt markets and thus impair rather than promote competition.

Price Flexibility

The Coalition states that rate increases are not necessarily synonymous with pricing flexibility in a competitive market as pricing flexibility allows for both increases and decreases to prices so companies can respond to competitive pressures. NYSTA states that the Commission, in its Competition III Order, granted pricing flexibility to VZ and Frontier based on 92% for VZ and 87% for Frontier of customers were served from wire centers that had competition in two other platforms. The ILECs reach 66% coverage and have 16 metrics to meet. Warwick believes there should be no limitations on rate increases. Rate increases should be based solely upon competition -- other facts such as efficiency, service complaints, investment in the network or offering broadband services should not be a part of considering eligibility for regulatory flexibility.

Reduce Regulatory Burden

Frontier states the Commission needs to take steps to reduce the regulatory burdens so that ILECs that qualify for pricing flexibility be regulated like CLECs. Such steps should include: streamlining or eliminating the capital program filing; complete the process to modernize and streamline service quality and consumer protection guidelines and eliminate part payment bucket allocations, eliminate regulations on late payment charges and interest on overpayments; streamline the annual report; harmonize the state and federal Uniform System of Accounts; eliminate the regulatory reserves as part of pricing flexibility; eliminate the filing of procurement practices; and, eliminate EAS expansion and balloting requirements.

Reject Staff Framework

The Coalition states the Commission should reject the White Paper in its entirety as it is based on false premises and methodologies. It is not aware that density is equally as important as the growth rate of access lines and MOU. The elasticity score options are too narrow and do not adequately address companies facing the extreme impacts of competition. Frontier states the Framework allows general flexibility to only one carrier, strictly limits flexibility to six other companies and grants no pricing flexibility to 33 other carriers. Frontier agrees that maintenance of adequate service quality is an appropriate gateway as is the Customer Trouble Report Rate but the Commission should not target a 90% target for entities with a CTRR of 3.34 or less if the company is achieving the 85% target.

Return on Equity

Frontier wants the Commission to eliminate the Return on Equity (ROE) gateway because it will throw out operational efficiency to achieve the "required" ROE. The Commission should not penalize Frontier for its efficiency and ability to maintain its revenues in the face of competition. These thresholds undo everything considered in Competition I, II and III and bring us back to rate of return regulation. Verizon wants to have the ROE and Revenue Gateways to reflect only intrastate results since Subject to Separations focus goes beyond the Commission's jurisdiction. (The Competition III Order specifically states that the Commission declined to "rely on non-jurisdictional earnings to offset jurisdictional losses.)

Wait and See

NYSTA wants the Commission to stop taking a "wait and see" approach and to act in a more timely fashion in the fast-changing marketplace.

Description of Updated Cost Model[1]

Summary

As part of its April 18, 2007 "Framework for Regulatory Relief", NYSDPS Staff estimated a cost model for purposes of evaluating the relative cost efficiency of the 40 incumbent local exchange telephone companies in New York State. The costs predicted by the staff regression model were stated on a cost per access line basis (CPAL) and compared to actual costs levels. Companies which had large amounts of costs over and above those predicted by the regression model were deemed to be relatively cost inefficient. Staff recognized that further refinement of its April cost modeling effort might be appropriate and, thus, invited parties "to propose analyses that better determine both the predicted CPAL and the causes of unexplained costs". A number of useful criticisms and suggestions were provided by the parties. As will be described below, the updated cost model addresses each of the concerns raised in the parties' comments.

The updated cost model differs from the April cost model in two major respects. First, the updated model is more robust since it is estimated on data spanning the three year period from 2004 through 2006. The April model was estimated using only more limited data for 2005. Second, the updated cost model is more theoretically correct. According to economic theory, costs are a function of both the outputs produced, and the prices of inputs purchased. The April model specified costs to be solely a function of three outputs. By including no input prices, the April model restrictively assumed that the input costs faced by the 40 incumbent telephone companies are similar. In contrast, the updated model specifies costs to be a function of three outputs and three input prices. The input prices used in the updated model reflect each company's relative economic cost of capital deployment, labor rates and costs purchasing materials & services. Clearly these input prices vary across New York State. The outputs are the same as in the April model. Companies costs should vary with the number of residence access lines served, the number of business access lines served, and the size of the service territory area over which each company's residence and business customers are located. According to a major econometrics text, the updated model's "translog" specification has remained the most popular of several alternative methodologies.[2]

The updated cost model reasonably addresses the parties' concerns by relying upon a more theoretically correct cost specification, and by increasing the data used to estimate the model from one year to three years. Unlike the April model, the robust updated model is not unreasonably susceptible to change if either the five largest or five smallest companies are dropped from the analysis. In contrast with the April model, the updated model does not raise questions over why certain interactions of the output variables were included and why others were excluded (all possible interactions of the output variables were included). The updated model reflects the scaling of costs associated with smaller companies, costs associated with varying technology mixtures and the costs associated with the obligation to serve entire service

[1] A more detailed explanation and additional results are available upon request.

[2] See "Econometric Analysis, 4th Edition", by William H. Greene, 2000, Prentice-Hall, Inc., page 641.

territories. The updated cost methodology does not systematically underestimate predicted CPAL as did the April method.

Responses to Parties Comments on the April Model

As a general matter, CPAL should not be eliminated as suggested by some parties since CPAL is a necessary check on ROE figures. The updated cost model reflects the parties' suggestion that, if to be utilized, the CPAL model must be significantly modified.

The parties indicated that the cost methodology should be modified to reflect carrier of last resort (COLR) obligations. Since an explanatory variable reflecting the square mileage of each company's service territory was included in both the April, and updated cost models, both methodologies are reflective of the costs of the obligation of ILECs to serve their entire service territory.

Similarly, NYSTA suggested that modifications should be made to reflect buried vs. aerial plant, fiber vs. copper, broadband deployment and network diversity. However, the companies' actions re buried vs. aerial, fiber vs. copper, broadband deployment and network diversity are reflected in companies' cost levels. The cost function regression method helps identify inefficient technology mixtures.

The translog model addresses Frontier's criticism that "it is puzzling [at least to Frontier] why the residential and business access lines are not differentiated"[3]. The original April model did not have residence lines and business lines as separate variables. The updated translog cost model includes residence and business lines separately as well as including a variable for the product of these two output measures (i.e., residential lines multiplied by business lines). Verizon argued that the April model predicts negative economies of scope in the joint provision of residence and business lines. The updated translog model coefficient for the joint residence lines/business lines coefficient is statistically significant and indicates positive economies of scope.

NYSTA commented that CPAL is discriminatory to smaller companies, and will increase as a result of competition. As shown below, the returns to scale estimates from the updated model indicate that the CPAL method is not insensitive to small companies. The updated model estimates reflect economies of scale and density. Moreover, the updated cost model indicates that their smaller scale prevents smaller companies from shedding costs as contemporaneously with competitive losses as can larger companies.

Another major criticism of the April model was its lack of robustness. The updated cost model addresses parties' lack of robustness arguments since it is estimated on three years of data, as opposed to a single year's data. Thus, the updated cost regression is estimated on 120 data points for 2004-2006 time period. With extra 80 observations, regression is more robust. The updated cost model is also more theoretically robust since it includes both input prices and outputs and better comports with economic theory. The more robust updated cost model has

[3] See Frontier's June 25, 2007 comments in Case 07-C-0349, page 12.

explanatory variable coefficient estimates which are, in general, more statistically significant than the explanatory variables in the April regression.

It was also argued that the variation in company sizes (e.g., Verizon with 8.54 million lines vs. Oriskany with 663 lines) makes meaningful cost predictions unlikely. Verizon indicated that the April cost regression breaks down if repeated without the five largest companies. However, such size differences have not been obstacles to other cost modeling efforts. A widely recognized study[4] relies on data with similar size variations (17.01 million lines down to 8,500 lines). The updated model is fairly insensitive to dropping either the five largest or five smallest companies.

Finally, the updated model addressed Verizon's criticism that the April regression systematically underestimates predicted CPAL by factor of 1.046. In particular, Verizon notes "that u = E[y] = E[ln(x)] is not necessarily equal to ln(E[x]), and that we, therefore, cannot simply apply the antilog function to u," [5]. Verizon's concern regarding systematic underestimation appears to be valid. However, instead using the 1.0468 adjustment factor Verizon proposed based upon the April model (0.970 R-squared statistic, 0.30233 standard error of the regression), the appropriate adjustment factor changes to 1.012 based upon the variance associated with the very good fitting translog equation (0.993 R-squared statistic, 0.15557 standard error of the regression). To illustrate this impact, if based upon the standard error of the less robust April regression model, a $20 unexplained CPAL without Verizon's underestimation correction for a company with actual CPAL of $83.56 would be the same as a $17.03 with Verizon's proposed correction. However, based upon the much smaller standard error of the more robust updated translog model, and its associated new adjustment factor of 1.012, a $20 unexplained CPAL without Verizon's underestimation correction for a company with the same actual CPAL of $83.56 would be the same as a $19.24 with the proposed correction.

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4 See " UnNatural Monopolies in Local Telephone", by Richard T. Shin; John S. Ying; The RAND Journal of Economics, Vol. 23, No. 2. (Summer, 1992), pp. 171-183.

5 See Verizon's June 25, 2007 comments in Case 07-C-0349, Attachment A.

Below are the predicted, average annual actual and unexplained results for the 2004 to 2006 period upon which the model was estimated.

Company	avg 2004-2006 economic CPAL	avg 2004-2006 predicted CPAL	avg 2004-2006 unexplained CPAL translog model	avg 2004-2006 adjusted predicted CPAL (1.012 factor)	avg 2004-2006 adjusted unexplained CPAL
Windstream (ALLTEL)	52.76	61.76	-9.01	62.51	-9.75
Armstrong	118.41	106.68	11.73	107.96	10.45
Frontier of Ausable Valley	71.40	93.48	-22.08	94.60	-23.20
FRP - Berkshire	65.93	62.15	3.78	62.89	3.04
Lynch - Cassadaga	68.37	69.26	-0.89	70.09	-1.73
FRP - C&E	75.88	71.81	4.07	72.67	3.21
Citizens (Hammond)	148.18	110.26	37.92	111.59	36.59
Champlain	85.29	70.17	15.12	71.01	14.28
Crown Point	187.11	144.94	42.17	146.68	40.43
Chazy & Westport	91.02	83.78	7.24	84.79	6.23
Delhi	74.82	67.61	7.20	68.42	6.39
TDS - Deposit	64.29	69.73	-5.44	70.57	-6.28
Lynch - D&F	76.01	63.36	12.65	64.12	11.89
TDS - Edwards	85.04	98.29	-13.25	99.47	-14.43
Empire	83.77	73.81	9.95	74.70	9.07
Fishers Island	81.05	71.52	9.53	72.38	8.67
Germantown	118.80	97.31	21.49	98.48	20.32
Frontier - Citizens NY	63.56	72.06	-8.50	72.92	-9.36
Hancock	109.22	94.00	15.22	95.13	14.09
Frontier of New York	55.24	61.89	-6.65	62.63	-7.40
Margaretville	66.25	62.05	4.20	62.79	3.46
Middleburgh	70.94	62.91	8.03	63.67	7.28
Newport	87.14	74.51	12.64	75.40	11.74
Nicholville	136.58	120.77	15.81	122.21	14.36
Verizon NY	93.49	74.20	19.29	75.09	18.40
Frontier - Ogden	44.79	52.06	-7.26	52.68	-7.89
Oneida County Rural	99.16	87.57	11.59	88.62	10.54
Ontario - Ontario	79.36	74.24	5.11	75.13	4.22
TDS - Oriskany Falls	61.10	78.37	-17.28	79.31	-18.22
Pattersonville	127.00	91.67	35.33	92.77	34.23
TDS - Port Byron	76.86	87.62	-10.76	88.68	-11.81
Frontier of Rochester	70.79	67.60	3.18	68.42	2.37
Frontier of Seneca Gorham	54.39	64.92	-10.53	65.70	-11.31
State	53.82	51.55	2.27	52.17	1.66
Frontier of Sylvan Lake	61.46	69.37	-7.91	70.20	-8.74
FRP - Taconic	68.78	68.47	0.31	69.29	-0.52
TDS - Township	74.61	81.62	-7.00	82.60	-7.98
Ontario - Trumansburg	87.10	90.53	-3.43	91.61	-4.51
TDS - Vernon	78.02	82.74	-4.72	83.73	-5.71
Warwick	74.74	63.14	11.60	63.90	10.84

Data Used in Updated Cost Model

The updated cost model was estimated using output and input price data for each of the 40 NYS incumbent local exchange carriers. The data covered the three-year period from 2004 through 2006.

Outputs: The residential lines output variable was taken directly from the access line schedule in the companies' NYPSC Annual Reports. The business access line output measure is the total access line figure from the annual reports less the residential access line figure. The service territory area output variable is measured in square miles and was obtained from the NYDPS GIS section[6]. Total cost for each company is defined as capital expenditures plus total non capital related operating expenses.

Costs: Total company operating expenses were measured by Total Operating Expenses Subject to Separations (including depreciation) from Schedule 9, Column E, Line 18 of the PSC annual reports. An economic measure of the cost of capital was substituted for the depreciation and amortization expenditures reported annually to the PSC on Schedule 9, Column E, Line 17.

Input Prices: An annual economic cost of capital variable was created using the Telephone Plant in Service - Subject to Separations figures from the NYPSC- Annual Reports Schedule 9. In order to determine a real measure of capital stock, the TPIS amounts were deflated by the Bureau of Economic Analysis' communications equipment price index. This real measure of capital stock was multiplied by a factor of 0.0625 in order to calculate the annual economic cost of depreciation (using the annuity form of depreciation and assuming constant productivity of each asset over its useful life). A property tax rate of 1% was also applied to this measure of capital stock. Finally, the real capital stock was multiplied by a factor of 0.0974 in order to estimate the return on investment. The annual economic capital cost for each company reflects the sum of these three items.[7] The price of the labor input was determined by dividing the wages and benefits figures reported on the PSC 5 Year Books, Table F, Line 80 by the number of company employees reported on the PSC annual reports, schedule 65a.[8] The catch-all materials price

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[6] The area of Warwick Valley Telephone was doubled in order to reflect that approximately half of its service territory stretches into New Jersey.

[7] The real capital stock measure relies upon the communications equipment price index reported for 2004, 2005 and 2006 on line 7 of the National Income and Product Accounts Table 5.5.4. (http://www.bea.gov/national/nipaweb) The FCC relied upon a 16.17 year overall average economic life for the TELRIC costing model it uses for high cost funding purposes. (see especially "TELRIC Pricing with Vintage Capital" by David Mandy, in the November 2002, Volume 22 of the Journal of Regulatory Economics") Table 3.17 in Dale Jorgenson & Kun-Young Yun's 1991 book on "Tax Reform and the Cost of Capital" indicates that the property tax rate should be about 1% annually. The return on investment figure of 0.0974 was obtained from the NYDPS Office of AF&E.

[8] Zero values for the number of employees and wage expenses were changed to 0.00001. A labor price of $50,000 was used for Oriskany Telephone.

calculation begins with what remains in the NYPSC annual report's Total Operating Expenses Subject to Separations figure after depreciation and wages & benefits expenses are subtracted out. These remaining "material" expenses are divided by the total access lines for each company in order to create a materials input price.

Allowed Return on Equity

Updated December 2007

Equity Ratio	Hypo. Rating	Pre-Tax ROR	Cost of Debt	Cost of Equity
100%	AA	10.04%	5.72%	6.43%
99%	AA	10.04%	5.72%	6.45%
98%	AA	10.04%	5.72%	6.48%
97%	AA	10.04%	5.72%	6.51%
96%	AA	10.04%	5.72%	6.54%
95%	AA	10.04%	5.72%	6.57%
94%	AA	10.04%	5.72%	6.60%
93%	AA	10.04%	5.72%	6.63%
92%	AA	10.04%	5.72%	6.67%
91%	AA	10.04%	5.72%	6.70%
90%	AA	10.04%	5.72%	6.73%
89%	AA	10.04%	5.72%	6.77%
88%	AA	10.04%	5.72%	6.80%
87%	AA	10.04%	5.72%	6.84%
86%	AA	10.04%	5.72%	6.88%
85%	AA	10.04%	5.72%	6.91%
84%	AA	10.04%	5.72%	6.95%
83%	AA	10.04%	5.72%	6.99%
82%	AA	10.04%	5.72%	7.03%
81%	AA	10.04%	5.72%	7.07%
80%	AA	10.04%	5.72%	7.12%
79%	AA	10.04%	5.72%	7.16%
78%	AA	10.04%	5.72%	7.21%
77%	AA	10.04%	5.72%	7.25%
76%	AA	10.04%	5.72%	7.30%
75%	AA	10.04%	5.72%	7.35%
74%	AA	10.04%	5.72%	7.40%
73%	AA	10.04%	5.72%	7.45%
72%	AA	10.04%	5.72%	7.50%
71%	AA	10.04%	5.72%	7.55%
70%	AA	10.04%	5.72%	7.61%
69%	AA	10.04%	5.72%	7.67%
68%	AA	10.04%	5.72%	7.73%
67%	AA	10.04%	5.72%	7.79%
66%	AA	10.04%	5.72%	7.85%
65%	AA	10.04%	5.72%	7.91%
64%	AA	10.04%	5.72%	7.98%
63%	AA	10.04%	5.72%	8.05%
62%	AA	10.04%	5.72%	8.12%
61%	AA/A	10.04%	5.74%	8.19%
60%	AA/A	10.04%	5.75%	8.25%
59%	AA/A	10.04%	5.77%	8.32%
58%	AA/A	10.04%	5.79%	8.40%
57%	AA/A	10.04%	5.81%	8.47%
56%	AA/A	10.04%	5.82%	8.55%
55%	A	10.04%	5.84%	8.62%
54%	A/BBB	10.04%	5.87%	8.70%
53%	A/BBB	10.04%	5.91%	8.77%
52%	A/BBB	10.04%	5.94%	8.85%
51%	A/BBB	10.04%	5.98%	8.92%
50%	A/BBB	10.04%	6.01%	9.00%
49%	A/BBB	10.04%	6.05%	9.09%
48%	A/BBB	10.04%	6.08%	9.17%
47%	A/BBB	10.04%	6.12%	9.26%
46%	BBB	10.04%	6.15%	9.35%
45%	BBB/BB	10.04%	6.18%	9.44%
44%	BBB/BB	10.04%	6.22%	9.54%
43%	BBB/BB	10.04%	6.25%	9.64%
42%	BBB/BB	10.04%	6.29%	9.74%
41%	BBB/BB	10.04%	6.32%	9.85%
40%	BBB/BB	10.04%	6.36%	9.96%

TDS 0221

Company	Competitive? If Cable/Wireless Greater Than 69.3%	2006 Intrastate Adjusted ROE	2007 Intrastate Allowed ROE	Flexibility Treatment
Armstrong	Not Competitive	5.72%	9.35%	Group 3
Champlain	Not Competitive	43.44%	7.79%	Group 4
Chazy and Westport	Competitive	12.88%	7.03%	Group 2
Citizens (Hammond)	Not Competitive	5.21%	7.91%	Group 3
Crown Point	Not Competitive	10.57%	9.96%	Group 4
Delhi	Not Competitive	14.65%	8.14%	Group 4
Empire	Not Competitive	4.16%	6.51%	Group 3
Fishers Island	Not Competitive	4.13%	6.54%	Group 3
Frontier - Citizens NY	Competitive	17.99%	7.79%	Group 2
Frontier - Ogden	Competitive	5.26%	7.79%	Group 1
Frontier of AuSable Valley	Competitive	-11.37%	6.43%	Group 1
Frontier of New York	Competitive	15.25%	6.43%	Group 2
Frontier of Rochester	Competitive	10.99%	8.25%	Group 1
Frontier of Seneca Gorham	Competitive	2.68%	6.43%	Group 1
Frontier of Sylvan Lake	Competitive	-5.81%	6.43%	Group 1
FRP - Berkshire	Competitive	13.88%	7.16%	Group 2
FRP - C&E	Competitive	-4.13%	6.48%	Group 1
FRP - Taconic	Competitive	4.99%	6.43%	Group 1
Germantown	Not Competitive	-14.12%	6.60%	Group 3
Hancock	Not Competitive	11.56%	6.99%	Group 4
Lynch - Cassadaga	Competitive	-1.53%	7.88%	Group 1
Lynch - D&F	Competitive	-2.50%	8.25%	Group 1
Margaretville	Not Competitive	0.46%	6.60%	Group 3
Middleburg	Not Competitive	15.71%	7.07%	Group 4
Newport	Not Competitive	5.40%	6.99%	Group 3
Nicholville	Not Competitive	-20.34%	9.35%	Group 3
Oneida County Rural	Competitive	-14.33%	7.50%	Group 1
Ontario - Ontario	Competitive	5.34%	8.30%	Group 1
Ontario - Trumansburg	Not Competitive	-3.51%	7.16%	Group 3
Pattersonville	Competitive	3.45%	6.48%	Group 1
State	Competitive	8.89%	7.88%	Group 1
TDS - Deposit	Competitive	-7.82%	6.43%	Group 1
TDS - Edwards	Competitive	-5.66%	6.45%	Group 1
TDS - Oriskany Falls	Competitive	-5.36%	6.43%	Group 1
TDS - Port Byron	Competitive	-10.70%	6.45%	Group 1
TDS - Township	Competitive	-5.43%	6.43%	Group 1
TDS - Vernon	Competitive	-9.14%	6.43%	Group 1
Verizon	Competitive	-0.24%	9.96%	Group 1
Warwick	Competitive	-15.97%	7.07%	Group 1
Windstream (ALLTEL)	Competitive	-3.37%	6.67%	Group 1

Totals (including VZ and FTR)	Competitive	26	Group 1	22
			Group 2	4
	Non-Competitive	14	Group 3	9
			Group 4	5

TDS 0222

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TITLE XXXIV PUBLIC UTILITIES

CHAPTER 374 GENERAL REGULATIONS

Supervisory Power of Department of Transportation

Section 374:3-b

374:3-b Alternative Regulation of Small Incumbent Local Exchange Carriers. –

I. In this section, ""small incumbent local exchange carrier" means an incumbent local exchange carrier serving fewer than 25,000 access lines.

II. A small incumbent local exchange carrier subject to rate of return regulation may petition the public utilities commission for approval of an alternative form of regulation providing for regulation of such carrier's retail operations comparable to the regulation applied to competitive local exchange carriers, subject to paragraph III, due to its status as carrier of last resort.

III. The commission shall approve the alternative regulation plan if it finds that:

(a) Competitive wireline, wireless, or broadband service is available to a majority of the retail customers in each of the exchanges served by such small incumbent local exchange carrier;

(b) The plan provides for maximum basic local service rates at levels that do not exceed the comparable rates charged by the largest incumbent local exchange carrier operating in the state and that do not increase by more than 10 percent in each of the 4 years after a plan is approved with the exception that the plan may provide for additional rate adjustments, with public utilities commission review and approval, to reflect changes in federal, state, or local government taxes, mandates, rules, regulations, or statutes;

(c) The plan promotes the offering of innovative telecommunications services in the state;

(d) The plan meets intercarrier service obligations under other applicable laws;

(e) The plan preserves universal access to affordable basic telephone service; and

(f) The plan provides that, if the small incumbent local exchange carrier operating under the plan fails to meet any of the conditions set out in this section, the public utilities commission may require the small incumbent local exchange carrier to propose modifications to the alternative regulation plan or return to rate of return regulation.

IV. The alternative regulation plan may allow the small incumbent local exchange carrier to offer bundled services that include combinations of telecommunications, data, video, and other services.

V. Following approval of the alternative regulation plan, the small incumbent local exchange carrier shall no longer be subject to rate of return regulation or be required to file affiliate contracts or seek prior commission approval of financings or corporate organizational changes, including, without limitation, mergers, acquisitions, corporate restructurings, issuance or transfer of securities, or the sale, lease, or other transfer of assets or control.

Source. 2005, 263:7, eff. July 22, 2005. 2006, 154:1, eff. July 21, 2006.