STATE OF NEW HAMPSHIRE
SUPREME COURT

DOCKET NO. 2009-0168 (Consolidated)

Appeal of
Union Telephone Company d/b/a Union Communications

APPENDIX TO SUPPLEMENTAL MEMORANDUM OF PETITIONER-APPELLANT

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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

[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

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[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, supra, 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

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[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.

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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]

[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. **Inadequate competitive presence and a sub par adjusted intrastate ROE.**[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. **Inadequate competitive presence and adjusted intrastate ROE greater than allowed.**

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.

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.

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[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).

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

Appendix A

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.

Appendix B

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

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[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%

Framework for Regulatory Relief - Case 07-C-0349

Appendix D

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**

STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

DT 08-013

COMCAST PHONE OF NEW HAMPSHIRE

Application for Authority to Serve Customers

in the TDS Service Territories

Order Granting Authority

O R D E R N O. 24,938

February 6, 2009

APPEARANCES: Mintz Levin by Cameron F. Kerry, Esq. for Comcast Phone of New Hampshire, LLC; Devine Millimet & Branch by Frederick J. Coolbroth, Esq. and Patrick C. McHugh, Esq. for New Hampshire Telephone Association and the TDS Companies; Rothfelder Stern, LLC by Martin C. Rothfelder, Esq. for Union Telephone Company d/b/a Union Communications; Office of the Consumer Advocate by Meredith A. Hatfield, Esq. on behalf of residential ratepayers; and F. Anne Ross, Esq. of the Staff of the Public Utilities Commission.

I. PROCEDURAL HISTORY

On December 12, 2007, Comcast Phone of New Hampshire ("Comcast") filed an application for authority to provide local exchange telecommunications services pursuant to RSA 374:22 and to do business as a competitive local exchange carrier ("CLEC") in the service territories of three affiliated incumbent local exchange carriers (ILECs) – Kearsarge Telephone Company (KTC), Merrimack County Telephone Company (MCT) and Wilton Telephone Company (WTC) – all subsidiaries of TDS Telecom (collectively, the TDS Companies or TDS). Comcast completed the required attachments to its CLEC application on January 22, 2008. Comcast is a CLEC currently authorized to provide intrastate telecommunications services in the New Hampshire exchanges formerly served by Verizon and now served by Northern New England Telephone Operations, LLC d/b/a FairPoint Communications-NNE (FairPoint).

On April 4, 2008, the Commission issued Order No. 24,843 on a *nisi* basis, granting Comcast's application for authority effective May 5, 2008, unless any interested party filed comments or requested a hearing. On April 16, 2008, the TDS Companies filed a motion to suspend Order No. 24,843 pending resolution of Docket No. DT 07-027,[1] or alternatively for a hearing. On April 21, 2008, the New Hampshire Telephone Association (NHTA) filed an objection to Order No. 24,843 and requested a hearing. Comcast filed an objection to the TDS motion and a response to the NHTA objection on April 30 and May 2, 2008, respectively.

On May 2, 2008, the Commission issued Order No. 24,854 suspending the order *nisi* and scheduling a prehearing conference. Following that order, the TDS Companies, NHTA and Union Telephone Company filed petitions to intervene. On May 20, 2008, the Office of Consumer Advocate entered an appearance on behalf of residential ratepayers pursuant to RSA 363:28. On May 21, 2008, the prehearing conference was held as noticed and the Commission granted all petitions to intervene. Following the prehearing conference, the parties and Staff met in a technical session and agreed to a procedural schedule including discovery, an additional technical session to develop stipulated facts, and written briefs. The Commission approved the proposed schedule on June 11, 2008.

On June 18, 2008, Staff filed a letter attaching stipulated facts, which the parties agreed would provide a basis for briefs. On June 26, 2008, NHTA, MCT and KTC, (Joint ILECs) filed a joint brief; Union also filed a brief. Comcast filed its brief on June 27, 2008. On July 14, 2008, the Joint ILECs filed a reply letter and the OCA filed a response to the Joint ILEC brief. Comcast filed a reply brief on July 15, 2008.

SegTEL, Inc. filed a motion to intervene on July 22, 2008, and stated that it would accept the process where it was and would not delay the proceedings. On August 18, 2008, the

[1] Docket DT 07-027 involved the TDS Companies' petition for alternative regulation pursuant to RSA 374:3-b.

Commission issued Order No. 24,887 granting segTEL's petition to intervene and scheduling a hearing for September 22, 2008. The Commission also directed the parties to file testimony and briefs regarding the remaining unresolved issue to be decided in this docket: whether granting Comcast Phone's CLEC application is consistent with the public good pursuant to RSA 374:22, RSA 374:22-g and RSA 374:26. The Joint ILECs filed written testimony on September 9, 2008 and Comcast filed testimony on September 10, 2008. By Secretarial Letter dated September 22, 2008, the Commission accepted the parties' recommendation to resolve the matter by briefs, entered the prefiled testimony into the record, and canceled the hearing. NHTA, Union and Comcast filed initial briefs. The Joint ILECs filed a joint reply brief on October 10, 2008, and Union and Comcast filed reply briefs on October 14, 2008.

On January 22, 2009, the NHTA, MCT and KTC filed a joint motion to supplement the record, seeking to introduce a letter from the General Counsel of the Wireline Competition Bureau of the Federal Communications Commission (FCC) to Comcast asking Comcast to explain why its VoIP (Voice over Internet Protocol) offering should not be treated as a telecommunications service. Comcast responded on January 26, 2009 that it does not oppose the motion so long as its answer to the FCC is included in the record as well. On February 4, 2009, Comcast filed its answer to the FCC.

II. POSITIONS OF THE PARTIES

1. Comcast Phone

A. Testimony

Comcast provided testimony by David Kowolenko, Vice President of Voice Services, and Michael D. Pelcovits, Ph.D., an independent consultant. Mr. Kowolenko testified as to Comcast's managerial, financial and technical ability to provide competitive local exchange services in the TDS Companies' service territories. Mr. Kowolenko stated that Comcast has operated as a CLEC since 1998 in the FairPoint (formerly Verizon) service territory in New Hampshire. Mr. Kowolenko pointed out that Comcast offers the same business, and schools and libraries network services described in its CLEC application in the FairPoint service territory. Mr. Kowolenko also described the local interconnection service provided by Comcast to an affiliate, Comcast IP Phone II, LLC (Comcast IP), in the FairPoint service territory; a service which will also be offered in the TDS service territories.

According to Mr. Kowolenko, Comcast currently serves as a CLEC in Maine, Vermont, Massachusetts, New York and more than thirty other states and offers services similar to those described in its CLEC application, and already offered in the FairPoint service territory. Comcast will utilize the same experienced management and technical staff to conduct its business in the TDS service territories as it currently uses in the FairPoint service territory.

Mr. Kowolenko referenced the annual report for 2007 for the Comcast parent company, Comcast Corporation, and stated that Comcast Corporation is a publicly held company with $30 billion in annual revenues and $2.5 billion in annual net income. In addition, Mr. Kowolenko stated that Comcast has invested $110 million to upgrade and expand its fiber network in New Hampshire.

Regarding the TDS Companies' ability to recover expenses they incur as a result of Comcast's entry into their service territories, Mr. Kowolenko explained that Comcast does not require the use of TDS's unbundled network elements to provide services. As a result, Comcast needs an interconnection agreement to provide for the mutual exchange of traffic. According to Mr. Kowolenko, the parties are in the process of negotiating an interconnection agreement for New Hampshire. Mr. Kowolenko stated that the New Hampshire interconnection agreement will be modeled after the one reached between TDS and Comcast in Vermont in 2008 and noted that Comcast is also in the process of negotiating interconnection agreements with TDS in Georgia, Michigan and Washington.

Mr. Kowolenko indicated that Comcast has long offered video services and broadband internet services to customers in the TDS service territory. Mr. Kowolenko stated that TDS already offers video service through Dish Network Satellite TV and broadband access to its customers in competition with Comcast's video and broadband offerings.

Dr. Pelcovits began by observing that New Hampshire explicitly recognizes the benefits of competition, "[c]ompetitive markets generally encourage greater efficiency, lower prices, and more consumer choice. It is the policy of the state of New Hampshire to encourage competition for all telecommunications services, including local exchange services, which will promote lower prices, better service, and broader consumer choice for the residents of New Hampshire." 1995 N.H. Laws 147:1. According to Dr. Pelcovits, competition compels firms to produce goods as efficiently as possible and encourages innovation, new services and new technologies.

Dr. Pelcovits observed that for a number of years following the 1996 Telecom Act[2] unbundled network elements (UNEs) formed the basis of most competitive services, but more recently cable providers have taken the leading competitive role. According to Dr. Pelcovits, over the past ten years cable companies have invested over $100 billion in infrastructure and are now capable of providing broadband, and in most cases IP-voice service, to over 117.7 million homes in the United States.

Dr. Pelcovitz observed that competition has been slow to develop in the TDS territories because of regulatory and other barriers to entry. With the passage of SB 386 in July, 2008, the legislature removed the barrier posed by RSA 374:22-f and stated a clear preference for

[2] 47 U.S.C. § 251 et seq.

competition in the small ILEC service territories in New Hampshire. He claimed that granting Comcast's CLEC application will not only extend competition for businesses, schools and libraries, but will also extend competition to additional markets since Comcast would be free to introduce other forms of local exchange service, exchange access and interexchange services. Finally, Dr. Pelcovitz pointed out that granting Comcast's CLEC application reduces barriers to Comcast IP's participation in the TDS territories and therefore contributes to the public good.

Dr. Pelcovitz claimed, based on a 2007 nationwide study he conducted, in which he attempted to quantify the customer savings, that cable voice competition brings consumer benefits of $100 billion over a five year period. He explained that approval of Comcast's application would eventually enable Comcast to offer triple play, video, data and phone service as a bundled offering, to compete with the triple play product currently offered by TDS.

As to the effect of competition on TDS, Dr. Pelcovitz explained that competition will force inefficient ILECs to reduce price levels to economic costs and will prevent the recovery of excessive costs. On the other hand, competitors will not price below their own long-run costs and therefore will not drive prices below those of an equally or more efficient ILEC. Thus, to the extent that TDS is currently recovering costs in excess of economic costs, competition could over time reduce TDS's cost recovery to economic costs.

Dr. Pelcovitz claimed that there is no reason to think that TDS's ability to offer universal service or serve as carrier of last resort will be harmed by Comcast's entry into the market. He pointed to TDS's testimony in a recent docket in which the TDS witness, Michael Reed, stated that TDS could continue to serve as carrier of last resort despite significant existing and increasing competition in its service territories.[3] In addition, Dr. Pelcovitz referred to the TDS Companies receipt of $2.4 million in Federal high cost support in 2007 and pointed out that such funds are designed to assist the TDS companies in providing universal service by offsetting the embedded cost of local switching and common line plant.

Dr. Pelcovitz stated the costs that the TDS Companies will incur to serve Comcast are limited to interconnection costs. Interconnection costs are the costs of the physical exchange of traffic from one carrier to another. The 1996 Telecom Act requires ILECs to terminate calls to their own customers originating on a competitor's network. According to Dr. Pelcovitz, the cost of terminating traffic consists of the incremental cost of interoffice transport and local switch terminating usage. Under the 1996 Telecom Act, the TDS Companies are entitled to recover the forward looking economic costs of transport and termination provided to interconnecting CLECs.[4] Likewise the CLEC is entitled to recover its own costs of terminating traffic originating on the TDS Companies' network. The interconnection agreement between Comcast and the TDS Companies should include negotiated cost-based interconnection fees.

B. Brief

Comcast asserts that it is beyond dispute under New Hampshire public policy, as well as basic economic principles, that competition in local telecommunications is for the public good. Comcast claims that its application advances the state policy encouraging competition and meets statutory and regulatory standards. Comcast alleges that the Commission's own rules "provide an appropriate balance between the interests of incumbent telecommunications providers and those of competitive entrants." *See,* N.H. Code of Admin. Rules Puc 431.01 and 431.02.

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[3] Kearsarge Telephone Company, Wilton Telephone Company, Inc., Hollis Telephone Company, Inc., and Merrimack Telephone Company Petition for an Alternative Form of Regulation, DT 07-027, Direct Testimony of Michael C. Reed, at 10 (filed March 1, 2007).

[4] 47 CCR § 51.505

Comcast suggests that Commission rules require that the Commission "shall" issue a CLEC authorization unless the applicant is denied based upon one of the acts or omissions enumerated in Puc 431.02. Comcast argues that the burden is on the ILEC to show evidence why its application should not be granted, and that in this case no such evidence was established.

In addition, Comcast indicates that its entry into the TDS Companies' territories will benefit New Hampshire consumers by bringing competition to the telecommunications services it proposes to offer, including services to small businesses and schools and libraries. In addition, the wholesale communications services provided by Comcast would enable Comcast IP to serve New Hampshire residential customers with VoIP service, offering consumers another alternative in residential voice communications. Comcast states that approval of its application would promote lower prices, better service and broader consumer choice within the TDS Companies' service territories.

Finally, Comcast emphasizes that to place conditions on its CLEC application regarding the services it could offer, as the TDS Companies suggest, would be inconsistent with state and federal law and policy, by requiring Comcast to seek further Commission approval in order to offer other competitive services. Moreover, Comcast states, under Puc 431.06 CLECs are free to introduce additional services as the market demands, without prior notice to, or review by, the Commission. Comcast contends that any such conditions would create a troubling precedent and delay or upset the well-established streamlined CLEC entry process contained in Puc 431.01 and 431.02.

Comcast argues that there is no basis in New Hampshire law to treat Comcast differently from any other CLEC and that the Commission has not previously inquired into the business plan of a CLEC applicant beyond the information required on the application. As a matter of fact, this unprecedented proceeding is the first time on record that the Commission has allowed incumbent carriers to prompt a hearing on entry of a CLEC.

C. Reply Brief

In its reply brief, Comcast reiterates that granting its CLEC application is for the public good. Comcast alleges that it has submitted far more information and evidence to support its application than has ever been required of any other CLEC applicant in New Hampshire, and that such evidence meets its burden of proof. Comcast also reiterates its claim that the burden is on incumbent carriers to present evidence to show why the application should not be approved. Comcast claims that to hold it to a different, higher standard, impose unprecedented conditions, or undertake additional proceedings would further delay competitive entry, to the sole benefit of the incumbent.

Additionally, Comcast argues that questions regarding appropriate regulatory treatment of VoIP services or new rules for "fair and equitable competition" are outside the scope of this proceeding. Comcast maintains that the ILECs are free at any time to petition the appropriate authority to address such issues without holding Comcast's CLEC application hostage. According to Comcast, there are no bases in statutes or regulations for the Commission to impose conditions and limitations on the services Comcast is allowed to offer. Comcast urged the Commission to find that approval of Comcast's CLEC-10 petition is for the public good.

2. NHTA, MCT and KTC

A. Testimony

The Joint ILECs submitted the testimony of Ms. Valerie Wimer, an independent consultant on telecommunications issues. Ms. Wimer testified that, absent Commission action to address the regulatory treatment of Comcast's VoIP service, competition from such VoIP services would be skewed heavily in Comcast's favor and would not be fair competition. Ms. Wimer also stated that the Commission should not allow Comcast to operate in the TDS service territories without first determining the appropriate regulatory treatment of the Comcast VoIP service. Ms. Wimer took the position that the Commission must determine whether both the retail and the wholesale services to be provided for Comcast VoIP, are in the public good. Further, Ms. Wimer pointed out that pricing rules, reporting rules and consumer protection rules all favor Comcast over the TDS Companies. Although Ms. Wimer acknowledged that alternative regulation provides some improvement over rate of return regulation for the TDS Companies, she asserted that alternative regulation does not match the regulatory freedom provided to Comcast. Ms. Wimer stated that Comcast is not required to offer equal access to all inter-exchange carriers, nor to offer lifeline and link-up services, all of which are required of the TDS Companies.

Ms. Wimer claimed that whenever the TDS Companies lose customers there will be a negative economic impact. Further Ms. Wimer stated that whenever business customers leave a rural telephone carrier's efficiency decreases and the cost per customer increases. Ms. Wimer acknowledged that some costs are saved when a customer leaves a rural ILEC, but she noted that carrier of last resort obligations require carriers to remain available to serve all customers in the franchise area.

According to Ms. Wimer, the VoIP service to be offered by the Comcast affiliate is in regulatory limbo due to the FCC's failure to classify VoIP service as either a telecommunications or an information service. Further, Ms. Wimer claimed that the wholesale interconnection service Comcast proposes to offer to its VoIP affiliate is not classified as either telecommunications or information services.

Ms. Wimer asserted that the Commission is not preempted by federal statute or the FCC from determining whether intralata services, both retail and wholesale, are telecommunications services. Ms. Wimer claimed that both Missouri and Vermont have undertaken an examination of VoIP services. Ms. Wimer urged the Commission to open a docket to determine whether Comcast's VoIP services are telecommunications or information services.

Ms. Wimer pointed out that only revenue from Comcast's retail service and its wholesale service would be reported and subject to utility assessment, while the revenue from Comcast's VoIP service would escape both regulation and assessment.

Ms. Wimer recommended that the Commission limit its approval of Comcast's CLEC application to those retail services specifically listed, i.e. business local service and schools and libraries exchange service. Ms. Wimer further suggested that the Commission not require the TDS Companies to provide any porting or interconnection services until Comcast wins a schools and libraries customer.

B. Brief

The Joint ILECs argued that Comcast's CLEC-10 application fails to disclose the actual services it will provide and does not define the terms "access" "exchange access" and "interexchange service." The Joint ILECs contended that Comcast plans to offer "Business Local Service" at a rate of $66.25 per month per access line, a rate well above rates charged by ILECs operating in New Hampshire. The Joint ILECs stated that Comcast plans to provide resold business local service and schools and libraries network service and that Comcast also intends to provide its digital voice product through Comcast IP Phone II, LLC. The Joint ILECs alleged that testimony shows that Comcast phone provides Comcast IP local interconnection service.

The Joint ILECs asserted that Comcast's request does not meet fairness criteria because the regulatory burden on the TDS Companies does not permit them to compete fairly with an unregulated Comcast. The Joint ILECs claimed that Comcast's CLEC application is intended to facilitate the provisioning of the VoIP products to residential customers who live within the TDS Companies' service territories. The Joint ILECs contended that the Comcast petition is not for the public good. The Joint ILECs suggested that if the Commission grants Comcast's CLEC application it should limit approval to business local service and schools and libraries exchange service.

The Joint ILECs argued that Comcast bears the burden of proving that its application is complete and that the requested relief is for the public good. The Joint ILECs maintained that, in determining the public good, the Commission must consider all of the factors set out in RSA 374:22-g. According to the Joint ILECs, Comcast cannot prove that its entry into the TDS service territory would promote free and fair competition considering each of these conditions. The Joint ILECs contended that Comcast's testimony regarding facts and circumstances in Vermont has no relevance to this proceeding.

The Joint ILECs further asserted that pricing rules, reporting rules and other regulatory requirements disadvantage KTC and MCT when trying to compete with a completely unregulated entity. The Joint ILECs claimed that the regulatory playing field would be skewed under Comcast Phone's plan to provide its VoIP product, while requiring KTC and MCT, but not Comcast Phone, to adhere to all of the regulations which benefit consumers. Meanwhile, universal service and carrier of last resort obligations require that KTC and MCT must continue to provide service to all customer locations. According to the Joint ILECs, Comcast is not required to offer equal access to all inter-exchange carriers (IXCs) for toll service which, even under alternative regulation, MCT and KTC are required to provide. Also, MCT and KTC are required to provide Lifeline and Link-up services. The Joint ILECs concluded that granting Comcast Phone's CLEC application is not in the public good. The Joint ILECs claimed that absent the Commission providing a level regulatory playing field and allowing fair competition, the Comcast proposal will not be fair, promote efficiency, promote universal service, nor allow the ILEC to obtain a reasonable rate of return.

C. Reply Brief

The Joint ILECs addressed two questions: (1) do the Commission's rules for submission of a CLEC-10 Application lessen Comcast Phone's burden of establishing that its services serve the public good; and (2) is the evidence proffered by Comcast Phone sufficient to meet its burden of proving that approval of its CLEC-10 application is in the public good?

The Joint ILECs contended that Comcast's narrow interpretation of Commission rules that entry of a CLEC into the territory of an incumbent carrier serves the public good, and that the simple registration process adopted by the rules forestalls further adjudicative hearings, would reduce the Commission's broad statutory power to regulate telephone services to merely a rubber-stamping procedure and would undermine the governing statutes. The Joint ILECs argued that the plain language of RSA 374:26 and 374:22-g mandating the fostering of free and fair competition cannot simply be relegated to a rubber-stamping process. Comcast must be held to its burden of establishing that its services are for the public good.

The Joint ILECs also allege that the evidence proffered by Comcast is not sufficient to establish that approval of its application is in the public good. The Joint ILECs maintain that Comcast has not satisfied the six factors identified in RSA 374:22-g. The Joint ILECs argue that RSA 374:26 authorizes the Commission to grant a CLEC-10 application only if it is for the public good, "and not otherwise" and that the Commission may prescribe such terms and conditions for the exercise of the privilege granted as it deems for the public interest. The Joint ILECs maintained that they proffered reasonable and appropriate conditions for the granting of Comcast's CLEC-10 application; however, the Joint ILECs held that Comcast has failed to meet its burden of proving that expansion into the TDS Companies service territories is for the public good.

3. Union Telephone

A. Brief

Union contended that Comcast did not provide sufficient evidence regarding the incumbent utilities' opportunity to realize a reasonable return on its investment, carrier of last resort obligations, and universal service. Therefore, Union argues that Comcast's application does not comply with RSA 374:22-g and, as a matter of law, the Commission cannot find such authorization to be in the public good. Union suggests that Comcast failed to provide any facts or evidence specific to the TDS Companies' ability to earn a reasonable return. Union also contends that Comcast's application failed to address statutory requirements showing how universal service and carrier of last resort obligations will be impacted in the TDS Companies' territories. Union concludes that, due to the lack of credible evidence, the Commission must deny Comcast's petition.

B. Reply Brief

In its reply brief, Union reiterated that the evidence offered by Comcast in its CLEC-10 application is insufficient for the Commission to grant its application inasmuch as New Hampshire law requires the Commission to make findings on whether granting the requested authority is in the public good based on evidence on competition and six additional factors.

Union asserted that Comcast mischaracterized aspects of this case, asked the Commission to grant authority without meeting the basic requirements of the law, and misstated the burden of proof. Although Comcast made statements in its brief regarding the TDS Companies' opportunity to realize a reasonable return on their investment, Union contended that Comcast simply provided no evidence to support such statements. Union asserted that Comcast cannot simply assume facts, and the Commission must reject Comcast's attempt to make an argument regarding the TDS Companies' opportunity to earn. Likewise, according to Union, Comcast's claim that universal service support is "ample" is not supported by evidence or explanation as to how granting the requested authority would actually impact universal service or carrier of last resort obligations.

Union also argued that the requirement of fairness is not supported by the evidence in this case. Both constitutional and statutory requirements regarding competition explicitly require fairness. Comcast is an unregulated utility petitioning the Commission to provide regulated services. The highly disparate regulatory treatment between incumbent utilities and Comcast disadvantages the incumbents when trying to compete. Union alleged that Comcast presented no evidence and made no reasonable argument that this disparate regulatory treatment is fair, but instead claimed it is irrelevant. Union concluded that the Commission must deny Comcast's requested authority.

III. COMMISSION ANALYSIS

A. Statutory Standards for Granting Comcast Authority to Operate

When Comcast filed its application for authority to operate as a CLEC in the TDS Companies' service territories the legislature had not yet amended RSA 374:22-f and 374:22-g to make clear that telephone franchises are not exclusive in New Hampshire and to bring the New

Hampshire statutes in line with the federal regime. *See*, 47 U.S.C. §§ 251 et seq. (1996 Telecom Act).

The 1996 Telecom Act established a framework of rights and obligations for telecommunications carriers in order to promote competition for local exchange service. Under the 1996 Telecom Act, telecommunications carriers, including both ILECs (TDS Companies) and CLECs (Comcast) have the obligation to interconnect either directly or indirectly with the facilities and equipment of all other carriers. *See*, 47 U.S.C. § 251 (a). Local exchange carriers, including ILECs (TDS Companies) and CLECs (Comcast), also have duties to allow resale of services, to port telephone numbers to other carriers, to provide dialing parity, to afford access to rights of ways and to establish reciprocal compensation arrangements for the transport and termination of telecommunications. *See*, 47 U.S.C. § 251 (b). Finally, ILECs have additional duties, including among others, providing competitors with access to certain unbundled network elements (UNEs) and allowing competitors to collocate within ILEC facilities for the purpose of interconnection. *See*, 47 U.S.C. § 251 (c). Certain rural ILECs, like the TDS Companies, are exempt from 251 (c) obligations, including UNEs and collocation, until their exemption from these requirements is terminated as a result of a bona fide request from a carrier. *See*, 47 U.S.C. § 251 (f).

In addition to allowing the development of competition for local exchange services the 1996 Telecom Act prohibits states from taking any actions which create barriers to competitive entry into the telecommunications markets.

> "No State or local statute or regulation, or other state or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service." 47 U.S.C. § 253 (a)

By repealing RSA 374:22-f, which prohibited telephone utilities from competing in territories with fewer than 25,000 access lines, the New Hampshire Legislature removed a barrier to entry into those service territories. Further, by amending RSA 374:22-g so that it applies to all telephone service territories, regardless of size, the Legislature made clear that the Commission must consider the same factors whenever additional carriers wish to enter a service territory. RSA 374:22-g begins with the words, "[t]o the extent consistent with federal laws and notwithstanding any other provision of law to the contrary..." Clearly, the Legislature intends that the Commission's application of RSA 374:22-g be guided by the federal laws and override any conflicting state laws.

Without the statutory amendments of RSA 374:22-f and RSA 374:22-g, which did not exist when Comcast first filed its CLEC application, the Commission considered Comcast's CLEC application under the more general franchise statutes, RSA 374:22 and RSA 374:26. RSA 374:26 provides for a hearing in cases where any party opposes the franchise application. As a result, requests for a hearing in this case were granted. Given the recent amendments to RSA 374:22-f and 374:22-g, however, our decision in this case will be guided by the standard set out in RSA 374:22-g.

Pursuant to RSA 374:22-g, we must determine whether granting Comcast's application fulfills the interests of competition together with: (1) fairness; (2) economic efficiency; (3) universal service; (4) carrier of last resort obligations; (5) the incumbent utility's opportunity to realize a reasonable return on its investment; and (6) the recovery from competitive providers of expenses incurred by the incumbent utility to benefit competitive providers, taking into account the proportionate benefit or savings, if any, derived by the incumbent as a result of incurring such expenses.

B. Burden of Proof

Before beginning our analysis of Comcast's CLEC application, we address arguments concerning the burden of proof. Our rules require the moving party, in this case Comcast, to "bear the burden of proving the truth of any factual proposition by a preponderance of the evidence." N.H. Code of Admin. Rules Puc 203.25. As fact finder, the Commission must weigh the evidence in the record before it to determine whether factual propositions have been proved. In this case, the factors identified in RSA 374:22-g involve the development of a competitive telecommunications market. We note that certain company specific information concerning the potential impact of a competitive market on ILECs is known only by the ILECs. Comcast bears the burden of producing evidence reasonably available to it and the TDS Companies bear the burden of producing evidence which is in their exclusive control. We will weigh the testimony and briefs submitted by all parties to determine whether the factors outlined in RSA 374:22-g have been satisfied by a preponderance of the evidence, recognizing that the parties agreed to forego a hearing in this matter.

C. Competition and Fairness

Comcast requests permission to offer telephone and other services in competition with the TDS Companies in their service territories. Comcast, through its expert witness, presented evidence of the benefits of competition to consumers. We agree that competitive markets, which are favored by both federal and state statutes, generally encourage greater efficiency, lower prices and more consumer choice.

Although they acknowledge that Comcast will introduce competition, the ILECs argue that Comcast's offering of a VoIP service through an affiliate company is not fair because such a service will compete with local phone service, but will not be regulated. The regulatory treatment of VoIP service has not been determined and, as we have stated previously, is beyond the scope of this proceeding. Currently, other competitive providers, including a TDS affiliate, offer unregulated cellular telephone services that compete with local exchange service in the TDS service territory. Such cellular telephone service is not subject to regulation or any of the consumer protections provided by our rules. The TDS Companies also currently offer bundled triple play services which combine unregulated video and high speed data services with telephone service. We do not find TDS offerings of bundled regulated and unregulated services unfair. Nor do we find Comcast's proposal to offer both regulated and unregulated services in the TDS service territories unfair. In making this finding, we do not assume that the Comcast VoIP service is either regulated or unregulated. We have authorized CLECs to operate throughout the FairPoint service territory in New Hampshire. Many of those CLECs, either directly or through affiliates, offer a variety of services with varying degrees of regulation, including cellular phone service, intralata and interlata toll service, video service, high speed data service and VoIP services. These competitive offerings are consistent with the state and federal policies we are bound to promote and are not unfair to the ILECs.

In this case, the TDS companies maintain that Comcast's VoIP services should be regulated and we have already found that question to be beyond the scope of the Comcast CLEC application. Whether or not those VoIP services are regulated does not impact the fairness of Comcast's entry into the TDS Companies' territories, because we have found that both regulated and unregulated services already contribute to the competitive market in the TDS Companies' service territories. We further note that neither the inquiry from the FCC's Wireline Competition Bureau, nor Comcast's answer, provide a basis for concluding otherwise. We find the competition proposed by Comcast to be fair and the ILECs have not presented sufficient evidence to rebut that finding.

D. Competition and Economic Efficiency

As a state and national policy competition in telecommunications services is encouraged. Policy makers have chosen that policy because they believe it leads to economic efficiency. Comcast's expert witness presented evidence, on a national level, of the savings created by competition in telecommunications services. Such customer savings support the conclusion that services are being provided at lower costs and thus more efficiently.

In testimony, the ILECs claimed that if business customers left the TDS Companies there would be a negative economic impact and the carrier's efficiency would be reduced. On the other hand, Comcast's testimony indicated that competition fosters economic efficiency and prevents carriers from charging prices in excess of economic costs. The only thing which distinguishes this CLEC application from the numerous others we have approved is that in this case the ILEC whose service territory is being entered is subject to the rural exemption under the federal statute. *See*, 47 U.S.C. § 251 (f). We find no indication in the 1996 Telecom Act that ILECs subject to the rural exemption are protected from competitive entry. In fact, 47 U.S.C. § 251 (b) makes clear that all LECs must interconnect with other carriers operating in their service territory. The recent amendments to RSA 374:22-f and RSA 374:22-g make New Hampshire law consistent with federal law on this point. As a result, small ILECs in New Hampshire must not erect barriers to competitive entry and the CLEC approval process should not become a barrier to competitive entry.

One of the ways to achieve economic efficiency is by eliminating barriers to entry. In fact, the 1996 Telecom Act specifically prohibits states from creating barriers to the entry of competition.[5] In an effort to support this important policy goal and to comply with federal statutes, the Commission's rules provide for a streamlined and efficient process for competitors to enter the local telecommunications market. See, N.H. Code of Admin. Rules Puc 431.01.

E. Competition, Universal Service and Carrier of Last Resort Obligations

CLECs in New Hampshire are not required to serve all customers in the service territories in which they operate. ILECs, on the other hand, are required to be the carrier of last resort and to provide service to all customers in their service territories. Under the current federal statutory scheme, ILECs are compensated for this service obligation through the universal service fund (USF). *See,* 47 U.S.C. § 254. Comcast points out in its testimony that the TDS Companies received a total of $2.5 Million in federal high cost USF support in 2007 and that this support is designed to support TDS's universal service obligations. Although Union argued that Comcast has not presented evidence supporting the TDS Companies' ability to meet universal service obligations, Comcast has produced evidence of the federal universal service fund support of those obligations. The TDS Companies have not presented evidence demonstrating that competition will prevent them from meeting those obligations. Based on the record before us, we find that Comcast's entry into the TDS Companies service territories will not prevent them from meeting universal service and carrier of last resort obligations.

F. Competition and the ILEC's Opportunity to Realize a Reasonable Return on its Investment

Whether or not competition from Comcast would adversely impact the TDS Companies' ability to earn a reasonable return can be judged only by monitoring the TDS Companies' performance after Comcast actually begins operating in their territories. At this point, the analysis is, at best, speculative. The TDS Companies have not argued that their return on

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[5] 47 U.S.C. § 253.

investment will be unreasonable as a result of competition. Instead, TDS witness Wimer testified that if business customers leave a small ILEC, the carrier's efficiency is reduced and its cost per customer increases. While acknowledging that loss of a customer saves some costs, Ms. Wimer testified that carrier of last resort obligations require ILECs to remain ready to serve those lost customers. Ms. Wimer's testimony falls short of indicating any impact on TDS Companies' return on investment and such information is in the exclusive control of the TDS Companies. Further, as noted above, federal USF support is designed to support such obligations and should increase investment return. USF support to the ILEC continues even in a competitive market and provides protection against reduced return on investment.

Based on the record before us, we do not find that competition from Comcast will adversely impact the TDS Companies' opportunity to realize a reasonable return on its investment. Accordingly, we find that the interests of competition are not outweighed by the risk that the TDS Companies may not maintain their opportunity to earn a reasonable return on investment.

G. Competition and the Recovery from Competitive Providers of Expenses Incurred by the Incumbent Utility to Benefit CLECs

The TDS Companies are currently subject to the rural exemption and are therefore not required to unbundle network elements to competitors. The TDS Companies are, however, required to provide interconnection to Comcast. Interconnection consists of the physical exchange of traffic between carriers. TDS will incur the cost of terminating traffic from its customers to Comcast customers and will be reimbursed for terminating calls from Comcast customers to TDS customers. These costs will be negotiated between Comcast and the TDS Companies and included in an interconnection agreement.

re in the process of negotiating an interconnection
to Comcast, are negotiating similar agreements in
hat the TDS Companies will set the terms of
ent any carrier requests that the rural exemption
o consider the cost and feasibility of
eir networks to other carriers. That case is
that the TDS Companies will recover any costs incurred in
Comcast through fees implemented in a negotiated agreement. The TDS
ompanies have not provided any evidence to the contrary in this proceeding.

H. Conclusion

Having considered all of the factors contained in RSA 374:22-g, we find that granting Comcast authorization to operate in the TDS Companies service territories is for the public good.

Based upon the foregoing, it is hereby

ORDERED, the application to operate as a competitive local exchange carrier by Comcast Phone of New Hampshire in the TDS Companies' franchise area is granted.

By order of the Public Utilities Commission of New Hampshire this sixth day of February, 2009.

Thomas B. Getz Chairman	Graham J. Morrison Commissioner	Clifton C. Below Commissioner

Attested by:

Debra A. Howland
Executive Director & Secretary