



STATE OF CONNECTICUT

DEPARTMENT OF PUBLIC UTILITY CONTROL
TEN FRANKLIN SQUARE
NEW BRITAIN, CT 06051

DOCKET NO. 02-05-17 DPUC INVESTIGATION OF INTRASTATE CARRIER
ACCESS CHARGES

February 18, 2004

By the following Commissioners:

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DECISION

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REVISED DRAFT DECISION

I. INTRODUCTION

A. SUMMARY

The Department of Public Utility Control (Department) initiated this docket to investigate the appropriate level of access charges for all carriers in Connecticut. Specifically, the Department indicated that it would investigate: (1) the level of competition in the Connecticut access market; (2) how access should be regulated in the future; (3) the access policies that should be applied by the Department; and (4) the cost of providing access by all the carriers in Connecticut, in order to structure the future of access charges.¹ The Decision finds that intrastate switched access rates should continue to be regulated by the Department and that all carriers will not be permitted to charge no more than \$0.015/minute for access. Those carriers charging more than \$0.015/minute for access will have three years from the date of this Decision to lower their access rates to this level. Any carrier that wants to charge intrastate access rates that are more than the price cap, will be required to submit a cost of service study to the Department that demonstrates a need for the higher rates.

B. BACKGROUND

The Decision dated November 7, 2001 in Docket No. 00-11-11, Petition of AT&T Communications of New England, Inc. to Investigate The Southern New England Telephone Company's Proposed Revised Connecticut Intrastate Access Service, required all local exchange carriers (LEC) providing intrastate access services to file a long run incremental cost study for separate switched access rate elements, as well as an analysis of the Connecticut access market. On April 15, 2002, the Southern New England Telephone Company (Telco) and Verizon New York (Verizon) filed access cost of service studies and their analyses of the Connecticut access market. However, the competitive local exchange carriers (CLEC) providing access services in Connecticut did not file access studies due to the cost and time involved with development of those studies. The Department subsequently closed Docket No. 00-11-11 and opened the current docket to continue investigating the access market and rate structure for all carriers in Connecticut.

In the Scope of the Proceeding (Scope) issued on June 11, 2002, the Department directed all carriers currently charging more than the Telco for access services to file cost studies to support their rates or a detailed explanation as to why their rates are more than those charged by Telco. The Department also required all access providers to address the level of access charges and the appropriateness of utilizing incumbent local exchange carrier (ILEC) cost studies as a benchmark for setting CLEC access charges.

¹ September 30, 2002 Procedural Schedule (Procedural Schedule), p. 1.

C. CONDUCT OF THE PROCEEDING

By Notice of Hearing dated February 14, 2003, the Department announced that a public hearing in the above-cited docket would be held pursuant to the General Statutes of Connecticut §§ 16-247b(b), 16-247c(c), 16-247f(f), and 16-247g(g) on April 1, 2003, at 10:30 a.m. That hearing was cancelled. By Notice of Rescheduled Hearing dated April 23, 2003, the Department announced that a public hearing was rescheduled to June 23, 2003, at 10:00 a.m. That hearing was also cancelled and rescheduled to July 21, 2003 at 10:00 a.m. in the Department's offices, Ten Franklin Square, New Britain, Connecticut 06051. The hearing was conducted and continued to August 7, 2003. The August 7, 2003 hearing was cancelled and this docket was closed by Notice of Close of Hearing dated November 14, 2003.

The Department issued its draft Decision in this docket on December 11, 2003. All parties were offered the opportunity to file written exceptions and present oral argument concerning the draft Decision.

D. PARTIES AND INTERVENORS

A listing of the parties and intervenors to this proceeding is appended hereto as Attachment A.

II. PARTICIPANTS' POSITIONS**A. SOUTHERN NEW ENGLAND TELEPHONE COMPANY (TELCO)**

The Telco proposes that the Department abandon the mandatory reductions required of the ILECs. The Telco also proposed that CLECs with higher access rates than the Telco's be required to reduce their rates to the Telco levels or be charged by the other LECs for access at the same price they are charging. Phelan Testimony, p. 8; Telco Brief, pp. 32 and 33.

The Telco explains that in addition to providing end user service for local service a LEC also provides a gateway to and from the switched interexchange network. Historically, this gateway or access service has been used by the interexchange carrier (IXC) that receives and delivers the end user's interexchange call. Therefore, the revenue that the LECs and competitors derive from being in the local market includes both local service charges to end users and switched access charges derived from interexchange calls. Phelan Testimony, pp. 2 and 3.

The Telco suggests that access be viewed as a service that also affects local competition. The Telco believes that since some LECs, such as the Telco, are regulated, regulators should either set access prices for all LECs at the same level or allow the LECs to charge for access in the same amount that they are being charged by other access providers. In the opinion of the Telco, this approach would level the playing field among access providers. Phelan Testimony, p. 3. The Telco further discussed that it was unfair to unilaterally be required to reduce its access rates while

other access service providers are permitted to charge higher rates. Phelan Reply Testimony, p. 11.

The Telco also suggests that the Department modify its prior policy by eliminating the requirement for annual access price reductions in light of the fact that access service has a significant impact on fueling local competition. In the alternative, the Telco recommends allowing local rates to increase to replace revenues due to past and future access reductions and allow competition to regulate the price for local service. Phelan Testimony, p. 6.

The Telco does not support using long run incremental access cost studies (that the Department has required from each carrier providing access services) to set access prices. The Telco claims that total service long run Incremental costs (TSLRIC) studies have never been relied upon as the methodology to set all ILEC access prices because of the regulatory policies employed by the Federal Communications Commission (FCC) and the Department. Therefore, the Telco recommends that ILEC access cost studies and rates be used as a benchmark to compare to and set CLEC access charges. Phelan Testimony, p. 7.

In response to AT&T Communications of New England, Inc (AT&T) and MCIWorldCom, Inc (MCI) testimony, the Telco submits that its cost study was a compliance filing made in accordance with the November 7, 2001 Decision in Docket No. 00-11-11. The underlying assumptions for the cost of capital, annual charge factors and economic lives are consistent with the Department's Decisions in prior cost study rulings. Phelan Reply Testimony, p. 10. The Telco also argues that the adjustments to the Telco's switch vendor costs and utilization rate recommendations that AT&T/MCI witness, Dr. Ankum suggested are not reasonable. Barch Reply Testimony, pp. 16 and 17. The Telco further argues that Dr. Ankum's modifications to its cost study are premised on his experience in other states, which is not a credible basis for modifying its study results. Additionally, the Telco asserts that Dr. Ankum attempts to discredit the Switch Investments Identification Tool (SIIT) model (which deals with inputs) but never demonstrates how the SIIT model results are detrimental to the study results. Telco Reply Brief, pp. 16 and 17. The Telco also disputes the AT&T and MCI claim that the Telco failed to provide the information necessary for them to review the studies appropriately. The Telco maintains that it provided ample models as well as responses to over 145 interrogatories. As such, the AT&T and MCI argument relating the auditability of their cost studies has no merit. Id., p. 18.

Further, the Telco argues that AT&T and MCI have provided no credible support or factual evidence justifying the Department to modify the Telco and Verizon access rates. Telco Reply Brief, p. 1. Rather, the Telco contends that AT&T and MCI have misconstrued the purpose of this proceeding (initially to review the appropriate mode for setting intrastate access services rates and charges for all carriers in Connecticut). Id., pp. 2 and 3.

Moreover, the Telco disputes the AT&T and MCI recommendation to eliminate the Pre-subscribed Interexchange Carrier Charge (PICC). The Telco explained that contrary to the AT&T and MCI assertion that the PICC is not cost based, that charge was developed using a cost analysis that was approved in the June 24, 1998 Decision

in Docket No. 96-04-07, DPUC Investigation Into the Intrastate Rates and Charges Incurred by Long Distance Carriers to Access the Public Switched Telecommunications Network. According to the Telco, 15% of the cost of the local loop is allocated to access, and within that allocation, non-traffic sensitive costs are recovered through the PICC. Consequently, the PICC is not part of the access cost models because it recovers loop costs and not usage sensitive access costs. Id., pp. 8 and 9. Further, the Telco emphasized that the Decision in Docket No. 96-04-07 determined that cost recovery must include a portion of the local loop and the costs associated with the loop, must be recovered from all services that use the loop. The PICC is a mechanism to recover a portion of loop costs; thus, the Telco finds no reason for the PICC rate to be modified. Id., p. 10.

B. AT&T COMMUNICATIONS OF NEW ENGLAND INC. AND WORLDCOM INC.

AT&T and MCI filed joint testimony in this proceeding recommending that the Department reject the Telco cost models and requiring revisions consistent with the recommendations made by their witnesses, Dr. Ankum and Dr. Michael Pelcovits. Ankum Testimony, p. 4. AT&T and MCI also argue that access rates should be reduced to cost, and the CLECs not be permitted to increase local rates to offset the reductions in access charges. Pelcovits Rebuttal Testimony, p. 3; MCI Brief, p. 5.

AT&T and MCI further argue that there is no evidence which indicates that access rates subsidize the cost of basic local exchange service. In this regard, AT&T and MCI suggest that the Telco collects far more revenue per line from basic local rates and charges for features such as Call Waiting or Caller ID, plus the federal subscriber line charge that the Telco assesses to defray the costs of local service than it did five years ago. AT&T Brief, p. 2.

Additionally, AT&T and MCI contend that the Telco's current level of intrastate access charges exceed the costs that the Telco incurs for providing this service. Consequently, they argue that the Telco's costs have the effect of "raising the cost floor of long distance providers, and are passed on to customers in the form of higher long distance prices." Pelcovits Direct Testimony, p. 3. Additionally, Dr. Pelcovits claims that the Telco's costs provide it with an unfair advantage relative to its competitors in the long distance market. Pelcovits Direct Testimony, p. 4.

Therefore, AT&T and MCI recommend that the Department require CLECs to mirror the Telco's rates, unless a CLEC demonstrates that its access service costs exceed the rates charged by the Telco. Nevertheless, AT&T and MCI are of the opinion that CLECs should not have to provide cost studies unless they want to charge access rates that are more than the Telco's. Pelcovits Direct Testimony, p. 5; AT&T Reply Brief, p. 15; MCI Reply Brief, p. 2.

With respect to the Telco's switched access rates, AT&T and MCI contend that they are "in the range of twice to sixteen times cost, depending on the specific rate element." Pelcovits Direct Testimony, p. 5. Dr. Ankum recommends that some of the Telco's Network Usage Cost Analysis Tool (NUCAT) model inputs be replaced with the AT&T/MCI revised SIIT model inputs. Dr. Ankum specifically recommends replacing the Average Total CCS (per line); Average End Office Trunk Port Investments (per line);

and Tandem Trunk Termination per Trunk inputs. Dr. Ankum also recommends replacing the Telco's Average Yearly minutes of use MOUs (minutes of use) per DS0 (digital signal level) input value, as well as eliminating the double count of fill factors in the NUCAT model. Ankum Testimony, pp. 66 and 67.

Moreover, AT&T and MCI recommend reducing the Annual Charge Factors for the digital switch and digital circuit equipment to reflect the Telco's new switch vendor contracts. They also recommend reducing maintenance expenses relative to investments, and using a lower cost of capital (i.e., a weighted cost of capital of 8.19%). Ankum Testimony, p. 67; Pelcovits Direct Testimony, p. 60.

AT&T and MCI suggest that the Telco and Verizon intrastate switched access charges are "substantially in excess of cost" and excessive access charges distort competition between LECs and long distance providers. Pelcovits Direct Testimony, p. 60. Dr. Pelcovits recommends that the Department remedy these charges by requiring the Telco and Verizon to bring their switched access rates to forward looking costs. AT&T and MCI argue that the long distance market is highly competitive and there is a greater reason to bring access charges to cost because the benefits will be passed on to consumers. AT&T and MCI also suggest that above-cost access charges harm consumers because they raise the cost of long distance service and distort competitive market functions in the local competition industry. Pelcovits Rebuttal Testimony, pp. 5 and 6; AT&T Reply Brief, pp. 4 and 5.

Additionally, AT&T and MCI assert that a rather unique market failure exists because the long distance provider that pays the switched access rate does not have the ability to choose what local service provider will carry traffic to or from a particular customer. Thus, the LEC has the ability to set its price for switched access without regard to the cost of providing this service. Pelcovits Rebuttal Testimony, p. 20. To remedy this situation, Dr. Pelcovits suggests that intrastate switched access charges be moved to cost as soon as possible and that costs be measured using TSLRIC plus a 15% mark-up for joint and common costs. AT&T and MCI also suggest that the Department implement this cost policy change in conjunction with the input changes recommended by Dr. Ankum. Pelcovits Direct Testimony, p. 60; Pelcovits Rebuttal Testimony, p. 21; MCI Brief, pp. 7-9; AT&T Brief, p. 54; AT&T Reply Brief, p. 16.

MCI also disagrees with Cox Connecticut Telecom, LLC (Cox), and the Telco's claims that access revenues play an important role in CLEC market entry decisions. MCI claims that access revenues are a relatively small part of the total revenues which a carrier would receive if it enters the local market and that a CLEC does not make market entry decisions based on prices that are in place prior to entry. Pelcovits Rebuttal Testimony, p. 14; MCI Reply Brief, p. 14. Furthermore, MCI believes that as switched access rates have been brought closer to costs, no CLEC could realistically expect that access charges would remain above cost in the long term. Therefore, MCI maintains that a prudent firm would make market entry decisions based on cost-based access charges rather than above-cost access charges. MCI Reply Brief, p. 15.

Finally, AT&T and MCI recommend that the Department eliminate the PICC charge, or alternatively, reduce the PICC from \$1.21 to \$0.48. The elimination (or reduction) of the PICC reflects increased productivity, reductions in the cost of capital,

and the excess revenue per line over forward-looking costs. Pelcovits Direct Testimony, pp. 60 and 61. AT&T and MCI also contend that the PICC is no longer necessary and cannot be justified. Rather, the PICC represents an unjustified monopoly windfall to Telco, and it should be eliminated. AT&T Brief, pp. 5 and 54; AT&T Reply Brief, p. 16.

C. COX COMMUNICATIONS , LLC

Cox Connecticut Telecom, LLC (Cox) recommended that the Department not make any further changes to access rates. Cox argues that toll competition is flourishing in Connecticut at the current level of access rates and Cox and other CLECs rely on access revenues in order to invest in the necessary facilities to compete. Cox claims that without access revenues, it will have to implement a PICC charge or other end user charge(s) to replace the reduction in access rates. Lafferty Prefiled Testimony, pp. 24-26.

Cox explained that without the access charge revenue, network construction, service quality and choices for customers would be constrained. Because Cox and other CLECs have just recently begun developing their networks, products and customer service programs required to compete, access charges are a critical source of revenue to provide the financial resources to establish viable business. Absent the opportunity to generate revenue to finance their growth, Cox maintains that CLECs will be constrained in their ability to provide customers with choices, quality and market based prices. Lafferty Prefiled Testimony, pp. 3 and 4; Cox Brief, p. 2. Cox supports this position by explaining that the policies of market-based pricing and reduced regulation have allowed itself and other CLECs to focus their resources on building networks and serving customers, rather than complying with detailed costing and pricing rules and reporting requirements. Lafferty Prefiled Testimony, p. 6.

Cox notes that in 2001, the FCC's CLEC Access Reform Order capped what a CLEC could tariff for interstate access rates and phased these rates down over three years with the ultimate goal of parity between ILEC and CLEC rates.² Similarly, Cox argued that in many circumstances CLECs are not eligible for the same federal universal service funds (USF) as ILECs. For example, Cox claims that if a CLEC does not offer service in the entire study area where the ILEC operates it receive almost no universal service support. Further, the level of potential federal universal support that Cox could be eligible for is based on the amount currently received by the ILEC (in this case, the Telco), thus Cox is not able to benefit from universal service cost recovery. Lafferty Testimony, pp. 11 and 12.

Cox stated that historically the Department has allowed ILECs to implement a flat rate intrastate PICC charge to the presubscribed IXC to offset the elimination of the intrastate common carrier line charge. However, CLECs like Cox do not face the same regulatory environment as ILECs did when their networks were first built. Therefore, both access revenue and earlier inter-carrier settlement processes played a significant

² Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket Nos. 96-262 and 94-1, FCC 01-146, In the Matter of Access Charge Reform and In the Matter of Reform of Access Charges Imposed by Competitive Local Exchange Carriers (CLEC Access Reform Order).

role in the ILECs' abilities to finance modern telecommunications networks. Nevertheless, CLECs building networks today face many of the operational and financial challenges that the ILECs faced in the 1980s when access rates played a large role in the ability to finance network construction. Lafferty Testimony, pp. 13-17.

Cox also argues that its access rate structure is different than that of the Telco's, so making a specific rate-by-rate comparison would be somewhat complicated. Cox indicates that its intrastate access tariff includes a single per minute End Office Access Switching rate for each access minute originating from or terminating to a Cox end-user. Additionally, unlike the Telco, Cox does not charge a \$1.21/line PICC. Therefore, Cox prices access on a per minute basis rather than a combination of per minute and per line charge as does the Telco. As such, Cox believes that comparing its access prices to those charged by Telco would be difficult. Lafferty Testimony, pp. 18 and 19; Cox Brief, pp. 9 and 10.

Cox maintains that public policy benefits of competition and the necessary evolution of CLEC networks require CLEC access rates to be higher than ILEC rates because CLEC networks and customer bases are in vastly different stages of development. Cox Brief, p. 9. CLECs have significantly fewer customers from which they can recover their fixed costs. Consequently, Cox argues that given these differences, ILEC cost studies can not be used to explain CLEC costs. Cox Brief, p. 11; Cox Reply Brief, p. 8.

Similarly, Cox disputes the Telco's alternative proposal that would enable the Telco to charge a CLEC the same rate it is being charged when calls are exchanged between the two carriers without the participation of an interexchange carrier. Cox finds this alternative to be discriminatory because the Telco's rates would vary depending on the carrier involved in the exchange of traffic, even though the Telco's cost of provisioning service remains the same. Cox Reply Brief, p. 7.

Cox maintains that if it and other CLECs are to continue as viable enterprises, they must be able to price services to produce the revenue necessary to recover their total costs in the same way as ILECs did where their networks were constructed. Lafferty Prefiled Testimony, pp. 9; 21 and 22. Without adequate access revenues to contribute to their cost recovery, CLECs and possibly ILECs may be forced to increase local service rates significantly to maintain current levels of customer service. Additionally, Cox claims that CLECs may be constrained in their ability to make the network investments necessary to build the networks required to compete aggressively in the long term. Id., pp. 4, 22.

Moreover, Cox contends that lower access charges might reduce the level of local service competition in Connecticut. Competitors such as Cox, review all the revenue opportunities in a market before determining whether to enter a market. If access rates are reduced without providing CLECs an opportunity to make up those revenues, competitors might not enter a market or may be forced to exit the local telephone business all together. Lafferty Reply Testimony, p. 3. In this respect, Cox disagrees with the AT&T and MCI assertion that access charges are a subsidy for local service providers. Cox argues that access charge revenue recovers CLEC costs, thus it is not receiving any windfall. Lafferty Reply Testimony, p. 9; Cox Brief, p. 7.

Cox urges the Department to ensure that the competitive goals of the Legislature and the Telecommunications Act of 1996 are not abandoned in the name of access reform. Cox states changes to access rates at this time could jeopardize these goals by cutting off some of the funds required to invest in the necessary facilities to compete, or by forcing CLECs to increase customer rates too quickly or too much. Lafferty Testimony, p. 26.

Finally, Cox recommends that the Department not require any immediate reductions to intrastate access charges, but reduce those rates over time if necessary. Cox Reply Brief, p. 12. If reductions to access charges are deemed necessary, Cox urges the Department to gradually reduce access rates 10 percent each year for five years. Cox believes these reductions would reduce the need for Cox to implement PICCs or other end user charges to replace access rates (or minimize the amount of any new customer charges). This approach would also provide CLECs more time to mature their competitive networks and customer service infrastructures. Lafferty Testimony, pp. 24 and 25; Cox Brief, p. 8.

D. VERIZON - NEW YORK

Verizon states that its switched access cost study utilizes a forward-looking, long-run incremental cost methodology that is consistent with the November 7, 2001 Decision in Docket No. 00-11-11. Bennett Testimony, p. 2. However, Verizon does not believe that the Department should rely upon or require cost studies in regulating intrastate access charges. Verizon notes that some of the assumptions in its cost studies are extremely ambitious regarding the pace and nature of technological development. Thus, the studies are likely to understate the costs of switched access. Bennett Testimony, p. 4. Further, in order to provide a reasonable estimate of forward-looking costs, the TSLRIC costs would have to be adjusted to reflect joint and common costs. Bennett Prefiled Testimony, p. 5.

Verizon also explained that the FCC found that rather than requiring carriers to conduct cost studies and to set rates that reflect those cost studies, the market allow to establish the price for access service. Calabro Testimony, p. 2. Verizon argues that there are numerous access competitors providing alternatives for access services, and in a competitive market, carriers should not be required to disclose their costs of providing a good or service nor be compelled to price their products on the basis of cost studies. Calabro Testimony, p. 3. However, if the Department is concerned that some CLECs are charging access rates that are too high, Verizon suggests that they use the ILEC access rates as a price cap for the CLECs. Specifically, Verizon suggests that if a CLEC chooses to charge access rates that exceed those of the ILECs, that they be required to provide full and complete cost studies to support their proposed rates. Calabro Testimony, p. 3; Verizon Brief, pp. 17 and 18. Verizon also suggests that if the Department decides to continue the existing framework for Telco and Verizon, it should permit other competing carriers to set their prices based on the level of the access charges of the incumbent telephone companies without requiring the carriers to submit cost studies. Calabro Testimony, p. 5.

In response to AT&T and MCI, Verizon urges the Department not to ignore the fact that access rates have been set to recover costs of other services, and reducing those rates would significantly impact the overall health of Verizon and the Telco. Verizon Brief, p. 5. Verizon also argues that the AT&T and MCI attempt to set prices equal to the costs of the service is an artifact of traditional rate of return regulation and that businesses in competitive industries do not undertake these types of exercises. Verizon Brief, pp. 7 and 8. Additionally, Verizon argues that AT&T and MCI are not required to demonstrate to their competitors that their rates cover no more than their respective costs. Id., p. 8.

Verizon further suggested that although the current framework for reducing access charges has worked well, the incumbent telephone companies should also be allowed to recover the effects of the annual reduction in access charges that will result from the continuance of the existing access charge regime. For example, Verizon's alternative regulation plan (Plan) permits it to reflect these reductions and other exogenous cost changes in rates during the term of the Plan. Calabro Testimony, p. 6.

Finally, Verizon notes that the Department's existing policy, combined with technological advancements, has allowed competition to grow in Connecticut. Requiring the Telco and Verizon to massively cut access charge rates and eliminate the PICC (as recommended by AT&T and MCI) would tilt the competitive balance against Verizon and the Telco. Verizon Brief, p. 15. Verizon argues that AT&T and MCI have failed to provide a factual basis for the Department to approve their proposed access rate reductions. Consequently, Verizon recommends that the Department maintain the existing regulatory policy regarding access rates in Connecticut. Id., p. 18.

III. DEPARTMENT ANALYSIS

The purpose of this proceeding was to structure the future of access charges for all carriers providing access in the state. Specifically, this proceeding was opened to review the current intrastate access services rates and charges for all carriers. In this respect, the Department asked the telecommunications industry in Connecticut to provide data and comments on: (1) the level of competition in the Connecticut access market; (2) how access should be regulated in the future; (3) the access policies that should be applied by the Department; and (4) the cost of providing access by each of the carriers in Connecticut.³

The purpose of this proceeding was not to relitigate the access charges or costs of Telco or Verizon since the Department has already examined these issues in prior dockets. The Department has investigated the access charges of the Telco and Verizon (collectively, the Telephone Companies) in Docket Nos. 96-04-07 and 00-11-11. The investigation of this docket addresses all access providers and not just the Telephone Companies. In addition, prior to this docket, in the June 24, 1998 Decision the Docket No. 00-11-11, the Department removed the requirement that intrastate traffic-sensitive access rates must remain in parity with interstate traffic-sensitive access rates. That Decision also required the Telephone Companies to continue lowering access charges pursuant to the framework adopted by the FCC in the FCC Access

³ Procedural Schedule, p. 1.

Charge Order⁴ as if the Coalition for Affordable Local and Long Distance Service (CALLS)⁵ had not been implemented. Over the years the Telephone Companies have made significant reductions to access charges. Meanwhile, CLEC access charges have not been investigated. Therefore, the Department opened the instant docket to investigate the access charges for all carriers in Connecticut and determine the appropriate rates and policies for the Telephone Companies and CLECs' switched access rates in the market going forward.

A. THE COST OF ACCESS

The Department opened this proceeding in order to continue investigating the access market and rate structure for all carriers in Connecticut. The only carriers filing cost studies were Verizon and the Telco. None of the other carriers provided a cost study for the access charges that they impose. However, their rates are generally equal to, or more than, the Telco's rates. The focus of MCI and AT&T in this proceeding was to analyze the cost study submitted by the Telco. AT&T and MCI provided a critique and recommendations for changing Telco's intrastate access cost studies. In their critique, AT&T and MCI challenged many of the inputs in the Telco's access cost study, such as the fill factors and cost of capital. Ankum Testimony, pp. 8 and 60; Pelcovits Direct Testimony, p. 52. Ultimately, AT&T and MCI recommend that the Telco's cost models be rejected and changed using the many inputs that they recommended. *Id.*, pp. 2-4. Although the Department did not preclude parties from their own analysis of either the Telco's or Verizon's costs, the Department finds nothing in the parties' presentations that demonstrates that the Telco or Verizon access costs need to be reexamined.

The Department has reviewed the recommendations made by AT&T and MCI and finds no basis for ordering the Telco to change its access charges. The Telco's access cost studies were previously analyzed by the Department and found to be appropriate for establishing a target price floor. Response to OCC-1. Although the MCI and AT&T recommendations may be useful in another context, they are not sufficient to order changes to the Telco and Verizon costs that were approved prior to this proceeding. The Department understands that depending on the cost assumptions used in a cost study, the results will change. For example, AT&T and MCI recommend changes to fill factors and the cost of capital. The Department has reviewed the fill factors used by the Telco and has found them to be reasonable, especially since they are based on the Telco's actual use of its facilities. The usage of Telco facilities has been stable since the Department first analyzed its costs. However, the Department has always permitted all parties, as it has in this case, to demonstrate cost changes.

⁴ First Report and Order in CC Docket Nos. 96-262, 94-1, 91-213, 95-72, In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing and End User Common Line Charges, (FCC Access Charge Order), dated May 7, 1997.

⁵ On May 31, 2000, the Federal Communications Commission adopted and released a decision In the Matter of Access Reform in CC Docket Nos. 96-262 et al. (96-262), Sixth Report and Order, approving the CALLS proposal to integrate access reform and universal service. CALLS members consisted of AT&T Corp, Bell Atlantic Corp., GTE Telecommunications Services, Inc., SBC Communications, Inc., and Sprint Communications Company, Inc. As part of this plan, the subscriber line charge assessed on residential and single line business end users increased, while the single line PICC rates would be eventually eliminated. Connecticut intrastate access charges are currently not subject to CALLS.

The MCI and AT&T recommendation to use a 95% fill factor across the board has not been supported with any actual usage data. In addition, the MCI and AT&T recommendation to change other inputs used in the cost study will not be adopted. The Telco and Verizon direct costs have been analyzed and the rates were targeted to include recovery for not only the direct costs, but also the costs of providing the loop in addition to the direct and common costs of providing access. Access without the use of the loop facilities provided by the Telco and Verizon is impossible and can not be ignored. As discussed below, the Department finds that setting a cap on access rates is a reasonable approach to regulatory access charges. The Department is moving toward a market based approach to access rather than costs.

The Department will be reexamining the UNE rates in the future and the parties will have the opportunity to present their analysis of the Telco and Verizon UNE costs in that investigation with factual support for their recommendations. Additionally, the FCC has recently released a Notice of Proposed Rulemaking to review and reconsider the methods used to determine UNE costs.⁶ For example, the FCC has recently ordered changes in how UNE cost studies should assign the cost of capital and depreciation.⁷ Due to these recent FCC actions, the Department will be required to review ILEC UNE rates in the near future, and therefore, will not do so at this time. Accordingly, the Department will not adjust the Telco's access or UNE costs based on the AT&T and MCI recommendations in this proceeding. Indeed, based on the Department's established method of regulating access charges, the Department finds no need to adjust or change the Telco and Verizon access service cost studies.

B. ACCESS TODAY

The Telephone Companies' access rates have significantly declined over the past six years and the current framework for reducing access has been successful. Consequently, the Telco and Verizon submit that the Department should not rely on cost studies in regulating intrastate access charges. The Telco explained that TSLRIC studies have not been used in the past to set ILEC access rates and charges; rather, regulatory policies employed by the FCC and the Department have dictated the pricing of access services in Connecticut. Phelan Testimony, p. 7. The Department never ordered or expected access charges to be equal to direct costs (TSLRIC). Access charges have always recovered the direct costs, common costs and loop costs. Verizon submits that the FCC found that the market should establish the price for access services. Calabro Testimony, p. 2. Market based rates would make sense if and when the market for access is competitive. The Department finds, however, that there is no record basis for determining that access is competitive at this time. Nevertheless, lacking a competitive access market does not mean that there is not some pricing flexibility that can be afforded to access providers now.

⁶ See WC Docket No. 03-173, Review of the Commission's Rules Regarding the Pricing of Unbundling Network Elements and the Resale of Service by Incumbent Local Exchange Carriers, dated September 15, 2003.

⁷ Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, CC Docket No. 01-338; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-98; and Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket No. 98-147, FCC 03-36, Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, released August 21, 2003.

The Telco and Verizon recommend that access rates remain at their current levels in order to enhance local competition. Phelan Reply Testimony pp. 7 and 11; Bennett Testimony, pp. 5 and 6. Cox submits that access charges provide a critical source of revenue for competition in the local exchange market. Specifically, Cox claims that without revenues from access charges, network construction and facilities-based competition would be constrained because such revenues finance investments. Lafferty Testimony, pp. 2-4; Lafferty Reply Testimony pp. 3-5. Further, Cox disagrees with the AT&T and MCI suggestion that access rates are providing guaranteed profit levels and a subsidy to local exchange carriers. According to Cox, access revenues are part of its overall cost recovery for entering and operating in the market, as opposed to a subsidy to the company. Therefore, any reductions in access must be made up through increased prices for other services. Lafferty Reply Testimony, p. 9.

AT&T and MCI submit that now that the long distance market is "highly competitive," there is an even greater incentive to bring access rates to direct costs and that the benefits will be passed on to consumers. AT&T and MCI claim that as access charges have declined, long distance prices have fallen and consumers have increased their use of long distance services. Pelcovits Direct Testimony, p. 5; Pelcovits Rebuttal Testimony, p. 4. The Department finds that moving access rates to recover only direct costs is not appropriate. AT&T and MCI also suggest that lower intrastate switched access rates would eliminate the discrimination in prices paid by wireline and wireless carriers, since wireless carriers pay the reciprocal compensation rate for calls that terminate within their local calling areas, rather than switched access charges. Pelcovits Rebuttal Testimony, pp. 9 and 10. The Department agrees that long distance service competition has increased in Connecticut. However, the fact is that the wireless local calling areas are greater than the wireline local areas and that these wireless carriers must be treated as local exchange companies using reciprocal compensation is not germane to the access charge issue before the Department.

Additionally, AT&T and MCI urge the Department to lower access rates without increasing local service rates. However, they did not provide an analysis of the Telco and Verizon current local exchange costs to justify this approach. Nor was such an approach noticed in the scope of this proceeding. This investigation had nothing to do with establishing different rates or costs for local exchange service offered by the Telco and Verizon. AT&T and MCI also argue that the Telco has not reduced its PICC rate since it was adopted in 1998, while productivity improvements over the past five years have far outpaced inflation. Pelcovits Rebuttal Testimony, pp. 18 and 19. The PICC charge was established to recover a minimum amount of loop costs (15%) when it was initially introduced. Productivity improvements may or may not have impacted the cost of the loop. The Department has not been presented with evidence that the actual cost of providing loops has changed since the PICC charge was introduced. The loop is used by long distance service providers to complete toll calls and was designed for toll uses in addition to other services. Therefore, the Department has required recovery of the cost of the loop from all services that use the loop. Ultimately, AT&T and MCI recommend that intrastate access charges be brought to only direct costs as soon as possible by requiring the Telco and Verizon to set prices based on forward-looking economic costs and by eliminating the PICC. Pelcovits Rebuttal Testimony, p. 21; AT&T Reply Brief, p. 16. However, the Department has repeatedly disagreed with their

claim that long distance service providers have no cost responsibility for using the local network. The costs for the local network that are included in the PICC are appropriate. Ignoring the fact that a long distance call uses the loop to complete the call is to ignore the cost of the facilities used in making the call and past Department Decisions. Both recognize that local exchange carriers derive revenue from monthly local service charges and from switched access charges to provide for the direct cost of access service and the common costs of using the local loop.

The Department also recognizes that as access charges have declined, many new long distance competitors have entered the market. Likewise, CLECs that have entered the Connecticut local exchange market base their decisions on access charges contributing to their overall earned revenue. Further, as Cox explained in its testimony, many CLECs rely upon access charges in order to fund the development of network facilities. Access charges are an essential component of operating revenue for ILECs and CLECs, and they are a factor in the development of competition in Connecticut. The Department has placed significant emphasis on the development of competition in the local telecommunications market and does not want to jeopardize the success in achieving what competition exists today. In fact, what the Department establishes today gives carriers the freedom to price access services under a price cap that is based on the cost of providing access.

Moreover, the Telco and Verizon have significantly reduced access charges annually since 1998, and the decline in those charges has not been offset by increased PICC or end-user charges. The Department continues to see merit in requiring all carriers that use the loop network to contribute to the costs of the network they use. The PICC was developed to recover a portion of non-traffic sensitive loop costs. Accordingly, the Department is not persuaded by AT&T and MCI that the PICC should be eliminated.

The current mechanism that gradually reduced access rates has been successful without placing a financial burden on Connecticut consumers. The Department intends to continue regulating access charges in a manner that does not harm consumers, yet allows carriers to have some flexibility to lower access rates. It is for these reasons, combined with the significant reductions in access rates that have already taken place in Connecticut, that the Department will, as discussed below, establish a new access charge structure that will be applied to all carriers providing access service in Connecticut.

C. ACCESS POLICY GOING FORWARD

The Telephone Companies, AT&T and MCI recommend that access charges for all carriers (including CLECs) be set at the same level. AT&T Reply Brief, p. 15; MCI Reply Brief, p. 2; Telco Reply Brief, pp. 25 and 26. The Telco suggests that access significantly affects local competition; thus it encourages the Department to require CLECs to charge the same access rates (or less) than it and Verizon are allowed to charge in Connecticut. In the alternative, the Telco recommends allowing itself and the other carriers in the market to charge the same amount for access that they are being charged by other access providers. Phelan Testimony, pp. 2 and 3; Brief, pp. 32 and 33. The Department does not have sufficient basis to adopt this alternative approach,

but may investigate it further in future proceedings. Similarly, Verizon proposes that ILEC access rates be used as a price cap for CLECs. Under this policy, if a CLEC seeks to charge access rates that exceed those of the ILECs, the CLEC would be required to provide full and complete cost studies to support the higher rates being proposed. Verizon Testimony, p. 3; Calabro Brief, pp. 18 and 19.

In this regard, Cox explains that its access rate structure is different than the Telco's, thereby making a comparison of rates difficult. Cox explained that it does not charge a per line PICC charge to offset some of the revenue lost as intrastate access charges decrease. Rather, it prices access on a per minute basis, while the Telco uses a combination of per minute and per line charge. Lafferty Testimony, pp. 18 and 19; Cox Reply Brief, p. 3. Cox also explained that its customer base is smaller than the Telco's, thereby making its access cost per minute higher than the Telco's cost. Cox Brief, p. 3. Consequently, Cox urges the Department to allow it and other CLECs to be able to price services to produce the necessary revenue to recover their total costs and not to arbitrarily set them equal to the Telco's rates. Lafferty Testimony, pp. 21 and 22; Lafferty Reply Testimony, p. 2.

The Department agrees that carriers need flexibility in establishing access charges. Based on the data supplied by the parties, it is obvious that some carriers find merit in a per-minute charge while others use a combination of per-minute and per-line. For example, AT&T estimated that it paid between \$0.015 to \$0.022 per minute to the Telco and Verizon⁸ when the per line charges are spread across minutes of use. Meanwhile, Cox's access charges, which are on a per minute basis, are approximately \$0.026.⁹ Although setting all access charges equal to the Telco's would simplify the process, it does not lend itself to a long-term solution. The Department is cognizant of the fact that some access providers prefer to charge a minutes-of-use rate, rather than a combination of minutes-of-use and a flat fee (i.e., PICC). The Department finds that establishing a price cap on access rates would protect long distance carriers from unreasonable access rates and afford local switch providers sufficient flexibility in how they charge for access.

The Department recognizes that CLECs face an upward battle competing with the established ILECs and with generating a sufficient level of revenue to invest in network facilities. Likewise, the Department recognizes that developing cost models and participating in litigation can be quite costly. It is not the Department's intention to use resources that CLECs would otherwise use in the development of their businesses. It is for this reason that the Department relaxed its requirement for Connecticut CLECs to submit access cost studies ordered in the Decision in Docket No. 00-11-11. However, without submitting cost studies to the Department that provide evidence that CLECs' costs are more than the Telco's, the Department will not permit CLECs to charge higher access charges than those imposed by the Telephone Companies.

⁸ See Responses to AT&T Communications of New England, Inc. to the Department's Questions issued in its June 21, 2002 Scope of Proceeding, p. 4.

⁹ Cox Connecticut Telecom D.P.U.C. Tariff No. 2, Section 3.

¹⁰ Telco Response to Interrogatory WCOM/ATT-49. See also Telco Total Switched Lines and Switched Access MOUs from Switched Access Cost Study (January 2003), Tab 7.4

¹¹ Cox Connecticut Telecom D.P.U.C. Tariff No. 2, Section 3.

Consequently, the Department will require the CLECs to use Telco's intrastate access rates on a per minute basis as a benchmark. AT&T estimates that based on its calculation, it paid Telco \$0.015499 per minute. The Department finds that \$0.015 per minute is a reasonable cap for access rates in Connecticut that recognizes the direct cost of access, common costs and a reasonable contribution to loop costs. CLECs may choose to charge any rates for intrastate switched access as long as their rates do not exceed the cap. Therefore, the Department will establish a cap on access of \$0.015 per minute, which is an average of Telco's per-minute costs and flat rates, for an average switched access rate. The Department also finds that there is merit to a gradual shift to this new price cap. Consequently, those carriers with access rates exceeding the price cap will have three years to lower their rates in their respective service territories.

Accordingly, any carrier currently charging more than \$0.015 per minute on average will take the difference between its current rate and \$0.015 and reduce its rate by one-third the difference by the end of one year after the issue date of this Decision, two-thirds the difference by the end of year two, and charge a cap rate by the end of the third year. The Telco's cap will be equal to their access charges at the rates that have been filed with the Department on the date of this Decision. Verizon will continue to phase down its rates until it can demonstrate that its access charges are under the cap. Any carrier wishing to charge a higher rate than that prescribed above will have 60 days to justify its rate with a cost study.

All carriers will be free to charge a rate equal to or less than the cap. Alternatively, if a carrier is not willing to lower its rates because its costs are higher than those under the price cap, then it must submit a cost of service study to the Department that justifies charging rates higher than the prescribed cap within 60 days of the issue of this Order. Upon review of those cost studies, the Department will make a determination concerning the appropriate access rates for that CLEC.

The Department will continue to monitor the access market and require each carrier to file its charges every year. As such, all carriers will be required to file its actual access rates and its access rates charged on an equivalent per minute basis.

IV. FINDING OF FACT

1. Access charges have declined over the past six years and competitors have entered the market during that time.
2. CLECs that have entered the local exchange market with the knowledge that access charges contributed to their overall earned revenue.
3. Intrastate switched access rates will continue to be regulated by the Department.
4. A per minute rate cap of \$0.015 per minute is reasonable.
5. Access rates higher than the cap must be justified with a cost study.

V. CONCLUSION AND ORDER

A. CONCLUSION

The Department must strike a balance between the access and toll markets, and therefore, has established an access service price cap. As such, the intrastate access tariffs being charged by Telco (including the PICC charge) are reasonable and will serve as the rate cap for all carriers providing intrastate switched access in Connecticut and the Telco's costs (resulting from its cost studies including common costs and a share of loop costs) will be the floor. Therefore, intrastate switched access rates will be capped at \$0.015/minute and carriers charging higher rates that are more than this cap, will have three years to reduce their access rates to that level. Any carrier that intends to charge more for access than that permitted under the price cap, must file cost studies with the Department which demonstrate that its access rates should exceed that cap. Only a cost study that justifies a rate higher than the cap will be considered by the Department. The \$0.015/minute rate will remain in effect for three years, at which point no carrier in Connecticut may charge intrastate switched access rates that exceed the price cap unless it has submitted cost justification to the Department and received approval from the Department to do so. In addition, over this three-year period, the Department will monitor the access charges of all carriers to determine whether the flexibility given to carriers today should continue.

B. ORDER

For the following Order, please submit an original and 3 copies of the requested material, identified by Docket Number, Title and Order Number to the Executive Secretary.

1. All LECs (including CLECs) currently charging more than the price cap level of \$0.015/minute for access services in Connecticut must lower their tariffs so that they are equal to or less than the price cap within three years of the effective date of this decision. Any carrier that intends to charge higher intrastate access rates than those provided under the price cap must submit cost of service studies to the Department which demonstrate the need for the higher access rates within 60 days of the effective date of this Decision.
2. No later than March 12, 2004, each carrier providing access in Connecticut shall file with the Department its access charges as of the date of this Decision on a per minute basis. Carriers shall also provide in that filing, the per minute detail necessary to replicate the per minute revenue including how flat charges were distributed on a per minute basis. Each carrier must file with the Department their access charges and data described above by January 31st of each year.
3. No later than March 12, 2004, carriers with rates that are more than \$0.015 per minute shall provide the Department a tariff or pricing schedule detailing the anticipated price changes and expedited dates of the change which indicate compliance with Section III, C. above.

4. Reductions to access charges below the cap can be made on 21 days advanced notice.

**DOCKET NO. 02-05-17 DPUC INVESTIGATION OF INTRASTATE CARRIER
ACCESS CHARGES**

This Decision is adopted by the following Commissioners:

John W. Betkoski, III

Donald W. Downes

Jack R. Goldberg

CERTIFICATE OF SERVICE

The foregoing is a true and correct copy of the Decision issued by the Department of Public Utility Control, State of Connecticut, and was forwarded by Certified Mail to all parties of record in this proceeding on the date indicated.

Louise E. Rickard
Acting Executive Secretary
Department of Public Utility Control

February 19, 2004
Date

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