CSHB 111: Section-by-Section Analysis

Section 1, Findings and Purpose – The findings and purpose assert that the bill is intended to promote competition and investment, which the findings assert have been delayed by state regulation. These finding form the basis for later provisions that provide extensive deregulation of local phone companies. In fact, competition has acted as a tremendous incentive for investment. Other provisions of the bill will kill—rather than promote—competition.

The claim that competition has discouraged investment is contradicted by the facts. The total investment in Alaska telecommunications facilities by ACS, AT&T and GCI since 1997 totals $2.5 billion. In 2003 alone GCI plans to invest $100 million, ACS $60 million, and AT&T about $10 million.

Finding #2, and following findings, indicates that local phone companies in Alaska are being treated just like the Bell Operating Companies. Nothing could be further from the truth. Bell Operating Companies are not even allowed to provide long distance service until they meet a 14-point checklist that is designed to promote local competition. In Alaska, ACS entered the long distance market long ago and ACS still does not meet the checklist.

Finding #3 accurately states that a stable regulatory environment is vital, but CSHB 111 would create incredible instability. Because many of the provisions are directly contrary to and preempted by the federal Telecommunications Act, CSHB 111 will spawn costly litigation. The uncertainty that will be created by the bill, and subsequent litigation, will stifle investment and increase the cost of raising capital for all. Under the Telecom Act of 1996, state laws or regulations *can be more pro-competitive* than federal law, but *cannot be less pro-competitive* than federal law. Any provisions designed to achieve the anti-competitive purposes of the bill would be preempted under federal law. Federal law, regulations, and policies to promote competition for the benefit of consumers cannot be waived by the state, and these requirements remain necessary to protect consumers and to ensure reasonable rates.

Furthermore, **Section 8 of CSHB 111** allows ACS, unilaterally and with no regulatory oversight, to change the price at which it leases facilities to GCI pursuant to Interconnection Agreements approved by the RCA. Allowing unilateral changes in existing agreements is the polar opposite of stability. This provision would almost certainly be preempted after costly litigation.

Section 2 – This section, **adding subsection (b) to AS 42.05.145**, would exempt all local phone companies from dominant carrier regulation as soon as a competitor is even authorized to provide service. The section includes a totally meaningless limitation, specifically that it applies only to a local phone company that has less than 60 percent of statewide market share. Because there are 20 local phone companies in Alaska each serving distinct areas, no local phone company has a statewide market share of 60 percent, so the limitation it totally meaningless. By escaping dominant carrier regulation, the local phone company would be able to implement local rate increases before any competition actually exists.

The significance of "dominant carrier" regulation is limited to the ability to raise rates. The Commission already allows dominant carriers in competitive markets to lower rates, and to repackage services, with the same latitude, and on the same notice period, as non-dominant carriers. It is only for rate increases that the standard differs for dominant and non-dominant carriers. Dominant carriers are also subject to rules regarding accounting procedures, but even if these requirements were lifted on the state level the carriers would still be required by the FCC to follow the "Uniform System of Accounts."

Furthermore, while it might seem illogical that a phone company facing competition would raise rates, that is exactly what ACS did in Anchorage well after competition began—implementing a 25% retail rate increase. At the same time, ACS attempted to increase the "UNE"[1] rates that it charges GCI. ACS obtained only a small UNE increase, and GCI did not increase its retail rates. Thus, consumers had a competitive choice to ACS' rate increase. Under CSHB 111, as discussed later,

[1] Pursuant to federal law, GCI leases "Unbundled Network Elements", or "UNEs", from ACS. UNEs are portions of ACS' equipment; the most common "UNE" leased by GCI is the copper loop connecting the subscriber premises to the local switch. As discussed herein, GCI pays rates that are determined pursuant to the federal Telecommunications Act and approved by the Commission. By law, the rates include a reasonable profit.

ACS would be able to increase UNE rates as it increased retail rates, destroying the ability of competition to protect consumers against rate increases.

Section 3—In 1997, the Alaska Public Utilities Commission adopted regulations establishing a Telecommunications Modernization Plan. Among other things, the regulations required that all telephone company facilities be capable of a 28.8 kilobit per second data transmission rate by February 2003. Thus, the Commission gave the utilities 6 years to bring their existing plant up to a minimal standard. Section 3 would repeal the requirement by prohibiting any rule from requiring a telephone utility to retrofit its existing network. This section flies in the face of claims in the finding and purpose that the bill will promote improvement of existing facilities (See Section 1, Purposes, subsection 3).

Perhaps unintentionally, this section would also go much further. It prohibits every rule, regulation, and order that would require retrofit. Thus, even if the RCA found that an existing network was unsafe or that it did not meet existing standards of service, the Commission could not order the telephone utility to fix the unsafe or nonconforming situation.

Section 4 – Depreciation expense is one large component of the costs that regulated utilities are allowed to collect from ratepayers. Regulated depreciation rates are based on the actual, useful life of the equipment used to provide service. This section allows all telephone utilities to implement depreciation rates based on the service lives established by the Internal Revenue Service for income tax purposes. The IRS lives, which are only 7 years for most telephone plant, including copper lines that last up to 30 years, were never intended establish actual useful lives; instead the lives are intended to allow rapid depreciation for income tax purposes. The amendments to AS 42.05.381 in this section are intended to overturn the RCA's recent decisions, issued after a public hearing and full consideration, denying ACS increases in depreciation expense that it had requested. The Section would allow local phone companies in Alaska to raise rates by as much as $100 million per year, leading to local rate increases of up to $10 per month per customer.

Subsection (l) added to AS 42.05.381 by Section 4 establishes a cost standard for UNEs leased by ACS to GCI under federal law, allowing ACS to recover whatever costs it "expects to incur", including the higher depreciation expense based on

IRS lives. As allowed subsequently by Section 8, ACS can unilaterally implement the new rates based on its own calculation of what it “expects to incur” and the new depreciation lives. These provisions are totally contrary to the federal Telecommunications Act, both procedurally and substantively. Procedurally, the Telecommunications Act requires that rates for UNEs be established based on negotiations and arbitration, and then approval by the RCA, under specific procedures and timelines. Substantively, the Telecommunications Act and implementing FCC regulations require that the rate be based on “Total Element Long Run Incremental Cost”, or TELRIC.

Subsection (l) also requires other carriers pay for ACS’ network if they *stop* using ACS’ facilities. Under this section, every telephone utility that cancels its use of the facilities of another carrier must pay the other carrier for the full unamortized value of the facilities. As written, this requirement applies even if the facilities were not constructed for the leasing carrier. Instead, leasing facilities for even a month would cause the leasor to pay the full value of the facilities. Although ACS may have intended this section to apply only to facilities used as UNEs, as written it applies to ALL telecommunication contracts to use facilities. Such contracts abound throughout Alaska, such as contracts to lease fiber optic facilities.

Another effect of this provision is to totally protect ACS from the effects of competition. GCI leases UNEs from ACS. In the vast majority of cases, the facilities leased by GCI were installed by ACS and its predecessors long ago. Nonetheless, if GCI now cancels that lease, perhaps to place the customer on GCI’s own facilities, GCI must pay ACS for the full value of the facilities. Competition could not develop in any market if a new entrant were required to guarantee the investments of the incumbent provider.

All of the provisions of Section 4 would apply not only to rates and facilities used for local service, but also “access charges” and facilities used by long distance carriers to originate and terminate calls to local subscribers. Access charges would skyrocket, probably increasing long distance rates.

The combined effect of the provisions in Section 4 and Section 8 would (if not preempted by Federal law) be to allow ACS to unilaterally raise the rates it charges to GCI for lease of UNE loops and then charge GCI for the full remaining value of those loops if GCI decided to discontinue use because the new rate was too high. This is like having your rent raised in the middle of your lease, and when you cant afford the higher rent the landlord gets to rent the house to someone else and send you a bill for the cost of the house.

Section 5– **Subsection (g) added to AS 42.05.433** defines the entire state of Alaska as a "competitive service area" for long distance service and thereby provides near total deregulation of long distance carriers, even in 150 villages where AT&T Alascom retains a facilities monopoly. **Subsection (d)** then completely eliminates the authority of the Commission to require just and reasonable rates (AS 42.05.381), to prohibit discrimination in rates and services (AS 42.05.301 and. 391), and to protect consumers from unsafe facilities (AS 42.05.291). Because of these provisions, the Commission would be unable to require "geographic rate averaging", which keeps down long distance rates in rural Alaska. AT&T would be able to raise Bush long distance rates to an amount it chose and the RCA would not be able to do anything about it. This is NOT the relief AT&T asked for in its proposals, but it is what happens when AT&T's request for "non-dominance" is combined with ACS' request for total deregulation.

This section makes no distinction between "wholesale" and "retail" rates. Thus, the wholesale rates charged by AT&T to other carriers would be completely deregulated, even for wholesale service that other carriers must use to complete calls to the 150 bush locations where by FCC rule AT&T still retains a complete monopoly on facilities.

Local phone companies would receive the same exemptions as soon as another carrier is able to offer service to 50 percent of the subscribers, but even before development of actual competition. Given the structure of existing local service areas, if GCI was able to offer service to the Kenai Peninsula, ACS would gain unfettered discretion to raise rates in Kodiak and Sitka, which are in the same service area. The local phone company itself is authorized to make the determination that its service area is competitive. (Subsection (a)) The full list of exemptions in subsection (d) includes the statutes that prohibit discrimination in service (AS 42.05.301); that authorize "Lifeline" rates (AS 42.05.306); that require just and reasonable rates and tariffs (AS 42.05.361-381); that prohibit discrimination in rates and unreasonable preferences among customers); and, indeed, the entire power of the RCA to review and set rates (AS 42.05.411, .421, .431, .451, .471). Thus, as soon as a competitor is authorized and has the theoretical ability to serve 50 percent of the subscribers in an area, the incumbent local phone company would be able to set rates however it wished, discriminating among customers, and with no Commission review.

Deregulation would be available for a dominant carrier even though it controls the facilities necessary for competitors to provide service. Dominant carriers will be able to use deregulation to stamp out competition. The RCA is currently engaged in a proceeding to look at the rules for deregulation where carriers no longer have a substantial market share, and the RCA should be allowed to continue its work in the public interest.

The bill does not have any provision whatsoever to bring utilities back under regulation if competition ends—the deregulation is a one-way door. Once a local phone company is deregulated, the RCA would be powerless to regulate them even if, as a result of the other anti-competitive provisions of the bill, competition were eliminated.

Another portion of **Section 5, the amendments to AS 42.05.435**, provides that rates for UNEs should be set "as closely as possible to market prices" and should guarantee full compensation of all capital expenditures. Again, UNEs are the portions of ACS' system that GCI leases, particularly copper loops. These provisions violate the federal UNE pricing methodology. Pursuant to the Telecom Act of 1996, the FCC has established mandatory regulations for the arbitration and pricing of UNEs. These regulations are very specific and have now been upheld by the U.S. Supreme Court as a fair and reasonable pricing method. No state prohibition can disturb or modify that standard and would be preempted by federal law. However, this provision will create prolonged litigation that will tie up RCA resources and threaten competition.

Section 6 – This section provides AT&T with immediate exemption from dominant carrier regulation in the intrastate long distance market. Under the standard set forth in this section, AT&T Alascom would be escape dominant carrier regulation, even though it maintains a facilities monopoly in some 150 locations across the state, because it serves less than 60 percent of the statewide retail customers. As discussed previously, the section makes no distinction between "retail" and "wholesale" service. As a result, AT&T Alascom would be free to raise rates to its carrier customers, harming competition and the ability of other carriers to serve customers.

Section 5 and 6 illustrate one of the recurring problems with CSHB 111: it is incredibly poorly written and redundant. Thus, for example, the relief granted to AT&T under Section 6 is entirely redundant to the relief granted by Section 5. Similarly, the deregulation granted to local exchange carriers by Section 5 is generally redundant of deregulation granted by Section 2.

Section 7 – This section extends the RCA through June 30, 2007, and is the only section that is needed so the RCA can continue its independent regulatory oversight for the protection of consumers in the public interest.

Section 8 – This provision allows incumbent carriers to unilaterally impose higher rates for interconnection agreements to the detriment of competition and consumers. As previously discussed, this section violates the bilateral negotiation and arbitration procedures for setting the rates, terms, and conditions between incumbent carriers and competitive carriers established by the Telecom Act of 1996 and would be subject to preemption.

There is no doubt that ACS would raise UNE rates to at least the unreasonable levels that they have proposed to, and that have been rejected by, the RCA. The rates that would be established by ACS would, if not preempted, preclude local exchange competition. After eliminating local competition, the other provision of the bill would still allow ACS to raise local rates at will and the RCA would have no power to stop it.

Section 9 – This provision requires the RCA to "adjust and allocate the financial obligation" of being a carrier of last resort in a so-called "competitive service area," proportionate to each carrier's share in the particular market. While carrier of last report obligations should be shared under certain conditions, the method and extent of sharing must be designed to meet the particular service and technological needs of the market on a case-by-case basis. This very matter is now under consideration by the RCA and the RCA should be allowed to complete its investigation of this issue.

Section 10 – This section makes the bill immediately effective. Thus, the bill would enable ACS to escape the effect of decisions by the RCA regarding its depreciation rates and its overall rate level, including rates in rural, noncompetitive areas. Although those decisions have been made, they have not been fully implemented, and Section 10 combined with Section 5 would enable ACS to completely reverse the effects of the Commission's decisions.