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MAIL DATE
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Decision 98-12-028 December 3, 1998

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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| Rulemaking on the Commission's Own Motion to Govern Open Access to Bottleneck Services and Establish A Framework for Network Architecture Development of Dominant Carrier Networks. | R.93-04-003 (Filed April 7, 1993) |
| Investigation of the Commission's Own Motion into Open Access and Network Architecture Development of Dominant Carrier Networks. | I.93-04-002 (Filed April 7, 1993) |

# ORDER DENYING REHEARING OF DECISION 98-02-106

This order denies the Joint Application for Rehearing of Decision (D.) 98-02-106 by AT&T Communications of California. Inc. (AT&T), and MCI Telecommunications Corp. (MCI).

## I. INTRODUCTION

In D.98-02-106 we adopted the Total Element Long Run Incremental Cost (TELRIC) methodology set forth in the August 8, 1996 First Report and Order of the Federal Communications Commission (FCC.) We concluded that the TELRIC methodology is very similar to the Total Service Long Run Incremental Cost (TSLRIC) Methodology we adopted in D.95-12-016 and applied in D.96-08-021. We rejected Version 2.2.2 of the Hatfield Model jointly sponsored by AT&T and MCI because it has

too many structural infirmities to allow it and the hypothetical costs for the local exchange network it models, to be used in place of Pacific Bell's (Pacific) TELRIC study. We concluded after approximately $677 million in dollar adjustments, that Pacific's study was a suitable basis for setting prices for unbundled network elements (UNEs). Finally, and most significantly, we decided it would not be appropriate at this time to institute geographically deaveraged prices for UNEs.

The procedural background of D.98-02-106 is set forth in some detail at pages 3-12 of the decision. Following our adoption of TSLRIC in D.96-08-021, the FCC issued its First Report and Order in the Implementation of the Local Competition Provisions of the Telecommunications Act of 1996 (Telecom Act), CC Docket No. 96-98 (FCC 96-325). Hereinafter this document is referred to as the First Report and Order. On October 15, 1996 the United States Court of Appeals for the Eighth Circuit issued a stay order of the FCC First Report and Order in Iowa Utilities Board v. FCC, 109 F. 3rd 418 (8th Cir. 1996). The stay order did not disturb the list of UNEs prescribed by the FCC, but did stay those portions that directed the states to use the TELRIC methodology.

On December 18, 1996, the assigned ALJ issued a ruling concluding that in view of the October 15, 1996 stay order the Commission is free to set UNE prices based on TSLRIC, as adopted in D.96-08-021. It became clear that costs for additional network elements had to be established and that there was a possibility that in its decision on the merits the Eighth Circuit might uphold the FCC authority to prescribe a costing methodology utilizing TELRIC. Therefore, the ALJ ruling directed Pacific to submit TELRIC refinements to the existing TSLRIC cost studies by mid-January 1997. Other parties to the proceeding were invited to file opening and reply comments on the new cost studies, which would be followed by a proposed decision on the consistency of the new studies with TELRIC principles. The ruling also designated the Hatfield Model sponsored by AT&T and MCI, along with the costing results based thereon, for review in the forthcoming proceeding. The ruling also opened for consideration whether costs should be reported on a geographically deaveraged basis as required by the FCC in its

August 8, 1996 First Report and Order. Pacific and GTEC were given their choice as to the form of the geographic deaveraging they would present. After Pacific submitted its TELRIC cost studies on January 13, 1997, the ALJ granted a series of extensions of time for parties to submit opening comments. Comments were submitted in March 1997 and reply comments submitted on April 15, 1997.

On July 18, 1997, the Eighth Circuit issued its decision on the merits concerning the challenges to the FCC's First Report and Order. Iowa Utilities Board v. FCC, 120 F3d 753 (8th Cir. 1997). The decision upheld the stay order designating the boundaries between state and federal jurisdiction and rejected most of the other challenges that the Regional Bell Operating Companies (RBOCs) and GTE had raised to the First Report and Order. The decision emphatically rejected FCC authority to require the use of TELRIC studies, or pricing for intrastate services, including geographic deaveraging, by the states. On January 26, 1998 the United States Supreme Court granted petitions for a Writ of Certiorari. Oral argument was held before the Supreme Court in mid-October, 1998.

On March 25, 1998, AT&T and MCI (Joint Applicants) jointly filed an application for rehearing. The application challenged the Commission's decision not to permit geographic deaveraging of loop costs in this phase of the ongoing proceeding. The application alleged that the decision not to recognize geographic deaveraging violated the cost-based and competitive standards of the Telecom Act and sections 709 and 709.2 of the California Public Utilities (PU) Code. It further alleged that the Commission committed error by not taking notice of new facts submitted by the Joint Applicants and that the decision violated FCC regulations concerning the costs associated with the switching of UNEs. Furthermore, the Joint Applicants complained that D.98-02-106 misapplies facts in the record, fails to reflect facts in the record, and is internally inconsistent in its use of facts. The Joint Applicants concluded by requesting oral argument before the Commission to address the arguments raised in their application for rehearing.

Pacific responded to the joint application for rehearing by opposing the arguments raised by AT&T and MCI. Pacific alleged that no new arguments are presented, the Commission has considered the arguments raised by the applicants for rehearing and rejected such arguments, and that consumption of the Commission's time and resources in hearing oral argument is not justified. GTEC also responded to the joint application for rehearing limiting its response to the issue of geographic deaveraging. GTEC supported the Commission's decision to maintain statewide average loop prices and argued that such decision did not violate PU Code sections 709 and 709.2.

We have carefully considered the arguments raised by the Joint Applicants and conclude that D.98-02-106 does not contain errors of law or fact.

## II. DISCUSSION

### A. Geographic Deaveraging

The Joint Applicants allege that D.98-02-106 violates the pro competitive requirements of the Telecom Act and PU Code sections 709 and 709.2. They claim that violations arise because the decision denies parties the right to propose cost-based prices for the loop unbundled network elements that reflect the significant difference in loop cost by geographic region. They further claim that the decision also violates the requirements of the FCC's rules defining the minimum set of unbundled network elements an incumbent must provide, specifically that the switching unbundled network element must provide all the features in functionality of the switch. The Joint Applicants state that by not allowing geographic deaveraging, the Commission has prejudged the pricing phase of this ongoing proceeding and has established an unfair and discriminatory treatment of loop unbundled network elements that is a bar to the development of competition for residential and single line business customers. The Joint Applicants complain that the Commission is inconsistent in its decision and ignores evidence on the record by calling for evidence on the subject of deaveraging and then not authorizing

deaveraging. The Joint Applicants rely upon a declaration attached to their application for rehearing which they assert explains why the Commission should grant deaveraging.

We do not agree. The question of deaveraging is extremely complex. The FCC's geographic deaveraging requirement was, like TELRIC, stayed by the Eighth Circuit. Accordingly, we were not required to adopt deaveraging in this round of the ongoing proceeding. We concluded that the underlying principle of the unbundling provisions in the Telecom Act, and the theoretical justification for geographic deaveraging, is that prices for UNEs should be based on an Incumbent Local Exchange Carriers (ILEC's) costs. Accordingly, we did not adopt Pacific's revenue zone proposal because it did not satisfy this test. We further determined that the averaging proposal presented by AT&T and MCI which relies on the Hatfield Model also was not persuasive. We concluded that the Hatfield Model contains elements that will only tend to aggravate problems caused by the model's internal assumptions about rural areas. Accordingly, we decided to establish only statewide average prices for Pacific's UNEs in the upcoming supplementary pricing hearings. In their January, 1998 comments to the draft decision herein, AT&T and MCI challenged our decision, asserting that not to establish geographically deaveraged loop costs would be legal error because we would be prejudging issues that we set aside for the pricing phase of this proceeding. We rejected that argument in D.98-02-106. We concluded therein that the record was not adequate for rendering a decision on this important issue. As noted above, geographic deaveraging is complex and can lead to unacceptable market distortions unless it is undertaken based upon an adequate record.

### B. D.98-02-106 Properly Relies Upon The Underlying Record In This Proceeding

The Joint Applicants complain that the Commission is arbitrary in its treatment of the underlying record and inconsistent in its handling of the data contained in the record.

When conflicting evidence is presented from which conflicting inferences can be drawn, our findings are final. Camp Meeker Water System, Inc. v. Public Utilities Commission (1990) 51 Cal.3d 845, 865; City of Los Angeles v. Public Utilities Commission, 7 Cal.3d 331, 351 (1972). Much of what the Joint Applicants complained about was resolved in D.96-08-021, in which we adopted the TSLRIC Methodology based upon the consensus costing principles developed and approved in D.95-12-016. The common costs adopted in D.96-08-021 are identical to the common costs presented in Pacific's TELRIC cost study. The Commission had already determined that there are no retail related costs in this common cost category. Our adoption of TELRIC methodology in D.98-02-106 does not alter the adoption of the TSLRIC Costs adopted in D.96-08-021. We have long recognized that the costs challenged by AT&T and MCI are common costs.

It must be emphasized that the Local Exchange Carriers (LECs) and requesting carriers may negotiate with each other for services utilizing the adopted costing methodology in D.98-06-102. Should this prove to be unsuccessful, they may submit to arbitration, the result of which is subject to approval by the Commission and may be reviewed in federal court. (Iowa Utilities Board, 120 F. 3rd at 818.)

## III. CONCLUSION

We conclude that all the arguments presented by the Joint Applicants have been considered, adjudicated and rejected. AT&T and MCI have not offered any evidence demonstrating errors of fact or law in D.98-02-106. Consequently, we see no value in granting the request for oral argument in this phase of the proceeding. It is foreseeable that the decision by the Supreme Court on review of Iowa Utilities Board v. FCC will provide further guidance in these matters. The resources of all parties would be better utilized in resolving issues that may be indicated in that forthcoming decision.

**IT IS ORDERED** that the Joint Application for Rehearing of D.98-02-106 filed by AT&T and MCI is denied.

This order is effective today.

Dated December 3, 1998, at San Francisco, California.

GREGORY CONLON
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners