

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY AND COMPLIANCE DIVISION
Telecommunications Branch

RESOLUTION T-15837
February 7, 1996

R E S O L U T I O N

RESOLUTION T-15837. PACIFIC BELL. REQUEST TO ESTABLISH PROVISIONAL TARIFF FOR FLAT RATE LOCAL USAGE OVER ISDN LINES BY PUBLIC SCHOOLS, LIBRARIES, COLLEGES, UNIVERSITIES, AND PRIVATE SCHOOLS.

BY ADVICE LETTER 17248 FILED JANUARY 27, 1995.

SUMMARY

Pacific Bell (Pacific) requests authority under provisions of General Order No. 96-A (G.O. 96-A) and Decision Nos. (D.) 89-10-031 and 94-09-065 to establish a two-year provisional tariff schedule to offer a new ISDN pricing plan that would be called Knowledge Network ISDN. This pricing plan would provide educational institutions with the option of a flat monthly rate for local usage instead of the current per-minute pricing of local message charges, on ISDN lines used primarily for data and video applications. Pacific has priced this service at the monthly equivalent of the current tariff rate per minute of local measured usage for the average number of local usage minutes per month expected for customers of the service.

AT&T Communications of California, Inc. (AT&T) filed a protest to Advice Letter (AL) 17248 on February 16, 1995. In response to the protest of AT&T and meetings with Commission Advisory and Compliance Division (CACD) staff, Pacific filed supplemental AL 17248B on November 30, 1995. This Supplement satisfied CACD's concerns, and several but by no means all of the objections raised in AT&T's February 16 protest. On December 15, 1995, AT&T filed a protest of Pacific's supplemental AL 17248B requesting that the Commission reject the AL as supplemented, and order Pacific to further amend its planned Knowledge Network ISDN offering in specified ways.

This Resolution authorizes Pacific's request, as supplemented. Pacific estimates the annual revenue impact of this filing to be an increase of \$28,900,000.

BACKGROUND

By AL No. 16965, filed on April 8, 1994, Pacific sought Commission authorization to offer public schools, community colleges, and public libraries one year of free telecommunications services that would enable participants to access computerized information sources and engage in interactive distance learning via Integrated Services Digital Network (ISDN) telephone lines. Under its proposal, known as "Education First", Pacific would waive its installation charges, monthly rates, and usage charges for the following services: basic Centrex lines with ISDN, individual line Measured Rate Business service with ISDN, usage charges for local, ZUM Zones 1, 2, and 3, and IntraLATA toll calling, Inside Wire installation, maintenance, and intrabuilding network cable services, if required, and Coaxial cable installation and maintenance. After the one year of free service, Pacific proposed to charge Education First participants discounted rates, yet to be developed at the time of that proposal, for the services involved.

By Resolution T-15588 on August 3, 1994, the Commission approved Pacific's Education First proposal, subject to certain requirements and conditions. One of the conditions was that Pacific was required to notify eligible participants of the existing rates and charges for the services involved, as a worst case scenario of what their year two rates might be, before participants were enrolled in the program. Another condition ordered by the Commission was that Pacific should file by advice letter its proposed discount Education Access rate with the Commission within 180 days. The present AL satisfies this requirement.

Pacific filed AL 17021 on June 30, 1994, to extend implementation of its Education First Program to Private Schools (K-12) as defined in its tariffs. The Commission approved this filing by Resolution T-15703 dated December 21, 1994.

After filing the present AL on January 27, 1995, Pacific filed supplemental AL 17248A on February 1, 1995 to correct the estimated total study period annual revenue effect. Pacific filed its supplemental AL 17248B on November 30, 1995, to attempt to satisfy the concerns and objections described below in the "Protests" and the "Discussion" sections of this resolution. Pacific filed supplemental AL 17248C on January 30, 1996 to correct subsection headings and make other minor revisions to three of the tariff pages affected by this AL.

NOTICE

Pacific states that copies of the AL and Supplements were mailed to competing and adjacent utilities and/or other utilities, and interested parties, as requested. The AL and Supplements A, B, and C were listed in the Commission's Daily Calendars in February and December, 1995, and February of 1996, respectively.

PROTESTS

AT&T filed a protest to AL 17248 on February 16, 1995, stating that Pacific's AL would provide service below cost and, by bundling local usage (a Category I service), and intraLATA toll usage (a Category II service) at one flat monthly rate, would be inherently anticompetitive. In this protest, AT&T requested that the Commission order that Pacific redesign its plan so that it does not bundle competitive and monopoly services, so that it eliminates flat rate pricing of usage based services, and so that use of the service is limited to data and video applications. AT&T also requested that Pacific be directed to include with its redesigned proposal a cost study that clearly demonstrates that the proposed rates pass the Commission's imputation tests, and that addresses the other points raised in AT&T's protest, and to include a plan for tracking the actual costs and foregone revenues resulting from the proposed tariff.

After an initial meeting with CACD staff, Pacific responded to some of CACD's and some of AT&T's concerns by agreeing to unbundle toll usage from local usage by proposing separate flat monthly rates for each, and to provide an analysis of Knowledge Network ISDN based on observed usage patterns of the institutions currently participating in the Education First Program. Such data are more recent and more numerous than those provided previously by Pacific to CACD, and the analysis based on more recent data was felt to be more relevant and convincing than that submitted by Pacific with its original Knowledge Network ISDN proposal. Pacific submitted this analysis to CACD on September 13, 1995. After reviewing these more recent data and analysis, CACD staff met again with Pacific in October and early November, and requested that Pacific supplement its AL to change the pricing of intraLATA toll calling from a flat monthly rate to a usage-sensitive pricing plan. Pacific responded on November 30, 1995 with supplemental AL 17248B, which removed toll calling entirely from the Knowledge Network offering, and made other minor changes.

DISCUSSION

In its supplement B to AL 17248, Pacific proposes to offer unlimited local calling on ISDN lines to educational institutions, as defined, for a flat monthly rate of \$40.00 per line. Pacific proposes this offering as a two-year provisional tariff, limited to five lines per location, and for primarily data and video applications. In addition to the \$40.00 per line per month for unlimited local calling, customers of this service will also pay the existing tariff rates of \$10.32 per line per month for measured rate business access lines, \$11.00 per month for ISDN service on each such line, and the current monthly End-User Common Line (EUCL) charge per line. Centrex customers will pay as line charges instead the tariff rates of \$8.35 per month for each Centrex access line, \$2.69 per line for Centrex basic features, the current EUCL charge, and \$16.00 per month for the Centrex ISDN feature package on each Centrex line.

In AT&T's final protest, received December 15, of Pacific's supplemented AL 17248B, AT&T stated "Pacific's supplement of November 30 provides for substantive changes to its original advice letter offering. ... By removing IntraLATA toll usage from its proposed flat rate structure, Pacific has satisfied AT&T's first objection with respect to binding Category I and II services within a single rate. Pacific's proposed modification to limit flat rate treatment to only five lines per location marginally addresses AT&T's concern regarding the limitation of potential losses ... and ... does nothing to alleviate the remaining AT&T objections..." AT&T objects, in particular, that "Pacific's proposed offering, as amended, continues to fly in the face of established Commission policy that prices should reflect the underlying costs of usage-based services. It also does not limit the discount to only data and video applications nor does it provide any reasonable assurance that Pacific's rate proposal covers its cost."

AT&T goes on to suggest that "In order to alleviate the potential for below cost rates, ... the Commission [should] consider a hybrid two part rate structure that simultaneously stimulates initial usage while ensuring that the service revenues recover service costs. AT&T suggests that Pacific's basic monthly charge of \$40.00 per line be designated for usage up to the average monthly usage for all customers of the service. Knowledge Network ISDN customers who abuse the flat rate aspect of the service and/or maintain an unnecessary around-the-clock connection to the network and thus utilize more than the average minutes-of-use per month would pay an additional charge per hour of usage with the incremental hourly rate set high enough to recover the cost of each incremental hour."

Pacific's Knowledge Network ISDN offering, as originally proposed, would indeed have violated portions of D.94-09-065 designed to prevent the stifling of competition by use of monopoly power possessed by local exchange companies (LECs) by virtue of their control of certain network bottlenecks. In D.94-09-065, at page 228, the Commission expressly reaffirmed its prohibition against the inclusion of Category I local usage and ZUM in contracts with Category II services. This prohibition applies to tariffed services as well as to services offered under contracts with individual customers of LECs operating under the New Regulatory Framework (NRF). Pacific's original proposal to bundle local and ZUM usage with intraLATA toll calling at one flat monthly rate would have made it difficult if not impossible for other providers of intraLATA toll service besides Pacific to compete for this portion of the intraLATA toll business of educational institutions.

Additionally, as originally proposed, Pacific's offering would have certainly provided intraLATA toll calling to some individual educational institutions with high levels of toll usage at a monthly rate well below the price floor for intraLATA toll calling when stated in the form of its monthly equivalent, contrary to the pricing rules established by the Commission in D.89-10-031, and confirmed and refined in D.94-09-065. In fact it is entirely possible that even the average amount of intraLATA

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toll calling by educational institutions subscribing to Pacific's originally proposed flat monthly rate for toll calling would be high enough to cause the monthly equivalent price floor, or even possibly the incremental cost by itself of providing toll calling, to be higher than the flat monthly rate proposed for the service. The tendency of usage-insensitive pricing to stimulate usage well above original projections would almost certainly have operated in this market as it does in most markets. The significant likelihood of this occurring if a flat rate for toll calling were approved for Pacific's Knowledge Network ISDN proposal convinced CACD to urge Pacific to modify its filing to eliminate the flat rate option for intraLATA toll calling.

These same arguments, of course, can be leveled against the flat rate pricing of any service for which the costs of provision vary positively and significantly with the level of output, and for which the cost of the measuring itself of usage is not unduly high. In other words, these arguments could be appropriately leveled at the provision of almost all goods and services, including local calling, at flat rates. Local calling differs, however, in one very important respect from intraLATA toll calling. Local calling is a service for which the dominant LEC still retains substantial monopoly power, and which we therefore regulate under Category I rules that are stricter than the rules that apply to Category II services such as intraLATA toll calling. Specifically and most importantly, we do not yet allow LECs to flexibly price Category I services, and we retain the authority to set prices for Category I services at rates that may not fully cover their incremental costs, if competing societal goals convince us to do so. Secondly, we do not expect local calling levels of customers subscribing to Knowledge Network ISDN to be so high as to exceed, on average, the level of usage at which the monthly flat rate for local calling will cover its costs. The higher number of hours of local usage assumed by Pacific and priced into its proposed flat rate for local usage, compared to the number of hours of intraLATA toll usage it was assuming previously, limits the extent to which yet higher local usage could drive the cost of providing it above the proposed flat rate. The lower elasticity of demand for local calling vs. intraLATA toll calling previously found by this Commission in D.94-09-065 also lessens the likelihood that flat rate pricing of local calling will stimulate its usage far above the levels projected in Pacific's cost studies underlying this proposal. Furthermore, the fact that we are authorizing flat rate local calling for these customers as a two-year provisional offering will give us the opportunity to review flat rate pricing of local usage after more substantial usage data from paying customers of the service are available. It is for these reasons, then, that we approve Pacific's Knowledge Network ISDN proposal.

In reviewing the AL and Supplements, we also note the following:

- a. The AL as supplemented meets the requirements set forth in Commission Orders and G.O. 96-A, and should be approved.

- b. Pacific requests that the workpapers and supporting cost documentation associated with the AL and supplements be treated as confidential.
- c. Pacific has agreed to CACD's requirement that the usage, costs, and revenues associated with this service be tracked and reported to CACD semiannually.

FINDINGS

1. Pacific filed AL No. 17248 and Supplements requesting Commission authorization to establish a two-year provisional tariff schedule to offer a new local usage pricing plan for educational institutions, as defined, called Knowledge Network ISDN.
2. Pacific's pricing plan, as supplemented, provides educational institutions with the option of a flat monthly rate for unlimited local usage instead of the current per-minute pricing of local message charges, on ISDN lines used primarily for data and video applications.
3. Pacific's Knowledge Network ISDN offering is limited to a maximum of five lines per customer location.
4. Pacific has priced this service at the monthly equivalent of the current tariff rate per minute of local measured usage for the average number of local usage minutes per month expected for customers of the service.
5. AT&T filed a protest to AL 17248 on various grounds.
6. Some of AT&T's objections to this AL were satisfied by the changes Pacific made to the offering in its supplemental AL 17248B.
7. Pacific has agreed, in discussions with CACD, to provide semiannual reports tracking the local usage actually incurred by customers of Knowledge Network ISDN, and the costs and revenues caused by the provision of this service.
8. The AL as supplemented conforms to the requirements of D.94-09-065, and G.O. 96-A.
9. Pacific states that authorization of this provisional tariff will result in \$28,900,000 of estimated annual revenue.
10. Commission authorization of this AL as supplemented does not establish a precedent for the contents of future filings or for Commission approval of similar requests. Commission approval is based on the specifics of this service, as demonstrated by the observed usage data and analysis submitted by Pacific to CACD.
11. The rates, charges, terms and conditions of the provisional tariff schedules approved in this Resolution are just and reasonable.

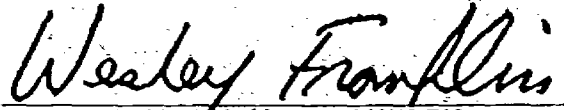
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THEREFORE, IT IS ORDERED that:

1. Pacific Bell (Pacific) is hereby granted provisional authority for two years from the effective date of this resolution for its Knowledge Network ISDN tariff under the conditions specified in Resolution T-15837.
2. The Advice Letter as supplemented shall be marked to show that it was authorized by Resolution T-15837.
3. Pacific shall provide to the Commission Advisory and Compliance Division semiannual reports tracking the local usage actually incurred by customers of Knowledge Network ISDN, and Pacific's costs and revenues caused by the provision of this service.
4. The portions of the protest of AT&T Communications of California, Inc. that have not been satisfied by Pacific's supplemental Advice Letter 17248B are denied.

The effective date of this Resolution is today.

I certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on February 7, 1996. The following Commissioners approved it:


WESLEY M. FRANKLIN
Executive Director

DANIEL Wm. FESSLER
President
P. GREGORY CONLON
JESSIE J. KNIGHT, Jr.
HENRY M. DUQUE
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Commissioners