

D.P.U. 93-125

Investigation by the Department of Public Utilities on its own motion as to the propriety of the rates and charges set forth in tariff schedules D.P.U. Mass. Nos. 10 and 15, filed with the Department on June 14, 1993, to become effective July 14, 1993, by New England Telephone and Telegraph Company.

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I. INTRODUCTION

A. Procedural History

On June 14, 1993, New England Telephone and Telegraph Company ("NET" or "Company") filed with the Department of Public Utilities ("Department"), revisions to the Company's tariffs D.P.U. Mass. Nos. 10 and 15 to become effective July 14, 1993. By Order dated June 25, 1993, the Department suspended the effective date of the proposed tariffs until January 14, 1994, in order to investigate the propriety of the charges sought by the Company. The matter was docketed as D.P.U. 93-125.

NET, a wholly-owned subsidiary of the NYNEX Corporation, is a local exchange carrier ("LEC") that provides telecommunications services throughout the Commonwealth. ¹ As of December 31, 1992, NET served 3,609,783 switched access lines in Massachusetts (NET Form M, 1992 Annual Report).

Pursuant to notice duly issued, four public hearings were held throughout the Commonwealth on July 21, July 22, July 26, and July 27, 1993, in Pittsfield, Worcester, Roxbury, and Plymouth, respectively, in order to afford interested persons an opportunity to comment on the proposed rates. Five days of

¹ Massachusetts is served by four other LECs: Elizabeth Islands Telephone Company serves Naushon Island; Granby Telephone Company serves the town of Granby; Richmond Telephone Company serves the town of Richmond; and Taconic Telephone Corporation, a New York-based LEC, serves part of the town of Hancock.

evidentiary hearings were held at the Department's offices, beginning on September 13, 1993 and ending on October 13, 1993.

Pursuant to G.L. c. 12, § 11E, the Attorney General of the Commonwealth ("Attorney General") filed a notice of intervention in the proceeding. In addition, the United States Department of Defense, and all other Federal Executive Agencies (collectively, "DoD"); MCI Telecommunications Corporation ("MCI"); Sprint Communications Company Limited Partnership ("Sprint"); AT&T Communications of New England, Inc. ("AT&T"); Metropolitan Fiber Systems/McCourt, Inc. ("MFS/McCourt"); the Massachusetts Payphone Association, Inc. ("MPA"); the Commonwealth's Executive Office for Administration and Finance, Office of Management Information Systems ("OMIS"); the Business Telecommunications Users Group ("BTUG");² Southwestern Bell Mobile Systems, Inc., d/b/a Cellular One ("Cellular One"); Telmarc Telecommunications, Inc. ("Telmarc"); ADT Security Systems Northeast, Inc. ("ADT"); Alltek Ltd., Inc. ("Alltek"); Representative Daniel E. Bosley; and Representative Christopher J. Hodgkins ("Representative Hodgkins") were granted intervenor status in the proceeding. The International Brotherhood of Electrical Workers, Locals 2222, 2313, 2321, 2322, 2324, and 2325; Mitchell Ziegler; George C.

² BTUG is an ad-hoc organization of substantial users of business telecommunications services provided by NET. Its members include Baybank Systems, Inc., General Electric Company, and the International Communications Association.

Jordan, III; Gerald M. Mroz; and Michael Schroeder were granted limited participant status. No other petitions for leave to intervene were filed.

AT&T, MCI, Sprint, MFS/McCourt, Cellular One, and Telmarc are all common carriers certified by the Department to provide intrastate telecommunications services. Alltek is a pay-telephone service provider that has been certified by the Department. MPA is a trade association for pay-telephone service providers in Massachusetts. DoD, ADT, and OMIS are large business customers of NET. The Attorney General represents consumers in general; however, in this proceeding, his primary advocacy is on behalf of residential customers of NET.

In support of its filing, NET sponsored the testimony of two witnesses: Paula L. Brown, assistant managing director of regulatory issues for Massachusetts, who testified in support of the Company's proposed tariffs; and Peter C. Czekanski, staff director of public affairs, who testified regarding the administration of the Company's Lifeline Telephone Assistance and Link-Up America programs. ³ DoD sponsored the testimony of Harry Gildea, a consultant with Snavelly, King & Associates. No other party to the proceeding presented a direct case.

The evidentiary record includes 339 exhibits. NET entered

³ As used herein, these programs are referred to as "Lifeline" and "Link-Up," respectively.

11 exhibits, the Attorney General entered 242 exhibits, MPA entered 22 exhibits, DoD entered one exhibit, and the Department entered 63 exhibits into the record. The record also includes the Company's responses to 125 record requests and 20 supplemental record requests.

Initial briefs were filed by NET, the Attorney General, DoD, MPA, MCI, Telmarc, OMIS, Representative Hodgkins, and Mr. Ziegler.⁴ Reply briefs were filed by NET, the Attorney General, DoD, MCI, MPA, and Mr. Ziegler.

B. Transitional Rate Restructuring Process

In 1989, the Department began the process of gradually realigning NET's rate structure to reflect cost-based rates. We determine that it is important at this time to restate the rationale and policy goals underlying the transition process that is bringing about this realignment of rates.

Traditionally, the pricing of telephone service was based on a method whereby residential monthly exchange rates were priced below cost in order to promote universal service; and long-distance, toll, and business rates were priced above cost in order to subsidize residential exchange rates. While this system

⁴ On November 12, 1993, the Attorney General filed a motion to strike an attachment to Telmarc's brief and certain portions of the brief relating to the attachment, on the ground that the materials contained statements of fact that were not part of the record. On November 19, 1993, the Hearing Officer granted the Attorney General's motion.

succeeded in serving a social purpose, it was a pricing scheme not conducive to the development of a fully-competitive market, in which the benefits associated with competition would be realized by all customers.

In response to the divestiture of the Bell Operating Companies from American Telephone and Telegraph Company in 1984, the Department opened an investigation to determine whether it should allow competition in Massachusetts. IntraLATA Competition, D.P.U. 1731 (1985). In IntraLATA Competition, the Department stated that the primary issue before it in that case was whether its policy goals for telecommunications would be best served by a monopoly provider of intraLATA service or by competition in that market. Id. at 25. The Department concluded "that there are benefits inherent in a competitive marketplace that encourage greater levels of economic efficiency and fairness than does a regulated monopoly environment," and authorized intraLATA competition starting on December 1, 1986. Id. at 26, 44.

With the endorsement of competition as the best way to achieve its policy goals of efficiency and fairness, it became necessary for the Department to confront the problems associated with the traditional policy of pricing services without direct regard to cost. The Department addressed the pricing issue in IntraLATA Competition, when it determined that "properly defined

incremental costs should be used as the primary basis for pricing all services, including local exchange service," and also found that "to the extent that current rates do not reflect an appropriate allocation of costs, the Department will, consistent with the need to avoid major discontinuities in rate levels, move toward that goal." Id. at 36-38.

Subsequently, the Department conducted a multiphase investigation of NET's rates. NET, D.P.U. 86-33 (1986). In the first phase of D.P.U. 86-33, the Department reviewed the Company's methodology for developing its cost of service study ("COSS"). NET, D.P.U. 86-33-C (1987). In the second phase of the investigation, the Department established a new revenue requirement for the Company and reviewed the Company's marginal cost study ("MCS"). NET, D.P.U. 86-33-G (1989). The Department's investigation into NET's rate structure in NET, D.P.U. 89-300 (1990) was the third phase of the investigation that resulted from the Department's general policy decisions in IntraLATA Competition.

In D.P.U. 89-300, the Department completed its investigation of NET's rate structure. The guiding principles for the rate structure approved in D.P.U. 89-300 were the Department's rate structure goals, first enunciated for telecommunications in IntraLATA Competition, supra, at 19-24. For telecommunications, the Department is guided by six goals:

economic efficiency; fairness; simplicity; earnings stability; continuity; and universal service. Id. As we stated in

D.P.U. 89-300:

- Economic efficiency means that the rate structure should reflect the cost of providing the service and therefore furnish an accurate basis for consumers' decisions about how best to fulfill their needs;
- Fairness means that the rate structure should require no class of consumers to pay more than the costs of serving that class;
- Earnings stability means that the amount a company earns from its rates should remain stable over a reasonable period of time and rate of consumption;
- Simplicity means that the rate structure should be easy to understand, so that consumers can make appropriate decisions;
- Continuity means that changes in the rate structure should occur in a predictable and gradual manner, which allows consumers reasonable time to adjust their consumption patterns in response to a change in structure; and
- Universal service means that the rate structure for telecommunications companies ensures rates that allow basic telecommunications services to be obtained by the vast majority of the state's population.

D.P.U. 89-300, at 11-12 (citations omitted).

Except for the addition of the goal of universal service, these goals are the same as the public policy goals that the Department consistently has followed in the gas and electric industries. Cambridge Electric Light Company, D.P.U. 92-250 (1993); Berkshire Gas Company, D.P.U. 92-210 (1993).

The Department's decisions in D.P.U. 89-300, and the subsequent transitional rate restructure proceedings, NET, D.P.U. 91-30 (1991) and NET, D.P.U. 92-100 (1992), reflected the need to balance the goals of economic efficiency, fairness, and simplicity with the goals of rate continuity, earnings stability, and universal service. D.P.U. 89-300, at 22. Thus, the Department found that while rates resulting in equalized rates of return among the residence, business, coin, and carrier access customer classes represented a desirable objective, the implementation of equalized rates of return in a single filing would have required such a large increase in residential rates that it would have violated the principle of rate continuity and adversely affected universal service. Id. at 15-16.

In order to achieve its ultimate objective of equalized rates of return among the different classes, the Department found the Company's "illustrative tariffs" to be useful. Id. at 22-23. The illustrative tariffs are based on strict application of the revenue requirement, COSS, and MCS, that would equalize rates of return for all classes of service and set rates at full marginal cost for the traffic-sensitive portions of rates. Id. at 17; D.P.U. 86-33-G at 477. Using illustrative tariff rates as a tool, for certain services the Department set target rates that were based on, but not identical to, illustrative rates. D.P.U. 89-300, at 22-23. The current target rates are used as a

framework by which to guide the transition to a realigned rate structure.

In D.P.U. 89-300, the Department directed NET to make a series of revenue-neutral transitional filings, and the Department prescribed the desired supporting documentation for purposes of evaluating the effects of the rate restructuring during the transition. Id. at 433-440. In D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100, the Department approved specific rate changes that represented the first, second, and third steps, respectively, in the direction of target rates and a target rate structure. For some services the target rates and rate structure have been achieved, while other services continue to move toward the target rates and structure. The filing under investigation in this proceeding is referred to as the third transitional filing. In fact, it represents the Company's fourth set of changes that move in the direction of achieving the Department's objective of equalized rates of return among customer classes.

C. D.P.U. 93-125

The Company filed the tariffs under review in this proceeding in compliance with the Department's directives in D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100. In accordance with the process established by the Department, the Company's proposal by design does not produce a general revenue increase, but rather contains revenue-neutral structural rate changes that

result in increases in the rates for some services and decreases in the rates for other services (Exh. NET-1, at 2-4).

For the transitional rate changes reviewed in this proceeding, we must determine whether the proposed tariffs move in the direction of target rate levels, and whether the magnitude of the proposed changes reflects an appropriate balancing of the Department's six rate structure goals. See D.P.U. 92-100, at 11. For the structural changes to the Company's tariff, the Department must ensure that the Company's proposal is consistent with the overall structure approved in D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100, and determine whether the proposed changes comply with the Department's directives in those Orders. Id.

The Department remains fully committed to achieving a rate structure for NET that will enable greater competition in the telecommunications industry in Massachusetts so that the benefits of competition may accrue to the customers of NET. Further, the Department reaffirms the goals and cost methodologies that formed the basis of the Department's decisions in D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100. The record in this case indicates that the transition to cost-based rates is being accomplished while achieving or maintaining all of the Department's rate structure goals. For example, the transition has required substantial increases in the basic exchange rates

for residential customers, yet the data show no statistically significant change in penetration rates for residence telephone service (see Section IV.A.1 for a more complete discussion of universal service). ⁵ Also, the reduction in usage rates that has occurred in each transitional filing has increased the value of connection to the telephone network and has enhanced the ability of all customers to make greater use of NET's network. ⁶

As discussed in more detail in the next section, we accept most of the transitional rate changes proposed by the Company in this filing. The rate changes proposed in this filing are reasonable, in light of the Department's directive in D.P.U. 92-100, to complete the remaining transitional rate changes in no more than three additional filings.

The Attorney General has used the Department's directive for NET to achieve the target rates in three filings as a foundation for proposing on brief a "one third" formula for achieving target rates. In other words, the Attorney General argues that the Department should not approve any rate change

⁵ The overall penetration rate for telephone service in Massachusetts was 97.1 percent in 1989, 96.6 percent in 1990, 96.4 percent in 1991, and 96.8 percent in 1992 (Exh. NET-5, Tracking Reports at 26).

⁶ We also note that all customers have benefited from the reductions in switched access rates to the extent that the interexchange carriers ("IXCs") have lowered intrastate toll rates in response to their lower intrastate access costs.

proposed by the Company in this filing that is not equal to one third of the difference between current rates and target rates.

The Department's directive to complete the transition in three filings was not a directive to increase or decrease every rate element by one third in each filing. Application of such a formula is not possible in a revenue-neutral filing because a one-third change in some rates would result in more than a one-third change in other rates. For example, if the Department adopted the Attorney General's suggested one-third rate changes in this filing, the residence dial-tone line increase would have to be reduced from the Company's proposed \$2.49. This formula would require larger than one-third increases in the residence dial-tone line rate in the two subsequent transitional filings in order to achieve the target rate of \$15.00. Moreover, the Department explicitly noted in D.P.U. 89-300 that the "movement toward target levels may vary for different rates, as we attempt to balance all rate structure goals." D.P.U. 89-300, at 435 n.200.

D. Cost Studies

Throughout this proceeding, the Attorney General raised issues regarding the sufficiency of NET's marginal cost study, MCS VI. Besides addressing these issues in the context of the Company's transitional rate changes in the next section, we consider it important to review in this introductory section the

role of the Company's cost studies in the transitional filings.

In D.P.U. 89-300, the Department required that each transitional filing shall be accompanied by supporting documentation, including, inter alia, a COSS and a MCS.⁷ Id. at 436. The Department further directed that the Company use the COSS and MCS methodologies that the Department approved in D.P.U. 86-33-C, D.P.U. 86-33-G, D.P.U. 86-33-L, and D.P.U. 86-33-N. Id.

The Department also required NET to file illustrative tariffs in which all traffic-sensitive rates are set at marginal cost. Id. at 22. The Department had found that the illustrative tariffs were instructive, but did not represent either desirable or plausible rate structures for the near future. Id. The Department stated that the illustrative tariffs were useful in meeting three objectives: (1) to assist in determining the direction in which NET's rates must move in order to meet the rate structure goals; (2) to serve as a benchmark to evaluate the proposed tariff; and (3) to gauge the need, schedule, and parameters for future transitional filings. Id. at 23-24.

The Department required that NET file a COSS and MCS as part of the supporting documentation for each transitional filing

⁷ NET had argued in D.P.U. 89-300, that the COSS would not need to be repeated for each transitional filing and that repetition of the MCS would be an unnecessary expenditure of resources. Id. at 433-434.

for the same reason that it requires illustrative tariffs. In

D.P.U. 92-100, the Department stated:

The Department's investigations into NET's annual transitional filings are investigations into the Company's rates and rate structure, and not investigations into general rate filings by the Company. An investigation by the Department in a general rate filing may encompass an examination into virtually all aspects of a company's operations as part of a determination of an appropriate revenue requirement to support just and reasonable rates. Transitional rate proceedings are narrow in scope in order to focus on the objective of achieving the target rates and rate structure outlined in D.P.U. 89-300 and the subsequent transitional rate Orders. The importance of reiterating here the narrow scope of these transitional filings becomes even more evident in light of our ... three-year schedule for completion of the transitional process.

Id. at 76 (citations omitted).

In describing the scope of review in a transitional filing, the Department has directly contrasted the transitional filings with D.P.U. 89-300, "which occurred after a multi-year investigation of NET's cost of service and revenue requirement." D.P.U. 91-30, at 7.

The Attorney General has chosen to attempt a lengthy review of NET's MCS in this case (see e.g., Attorney General Brief at 20-35).⁸ However, the Attorney General does not contend that NET's marginal cost study is not in compliance with the MCS

⁸ During the initial hearing on the Company's direct case, the Department expressed its concern about the relevancy of the Attorney General's examination, and the Attorney General indicated that the examination would lead to relevant issues (Tr. 1, at 58).

methods that the Department approved in D.P.U. 86-33. See D.P.U. 86-33-G, at 382-468. In his brief, the Attorney General never mentions the Department's approved MCS methodology.

In D.P.U. 91-30, when the Attorney General similarly attempted to argue that the Company's cost study methodology was inappropriate, the Department stated:

We do not find it appropriate in this proceeding to revisit fundamental decisions concerning the cost allocation methodology, as has been urged by the Attorney General. These matters were fully litigated and determined in D.P.U. 86-33, when the Department committed to equalized rates of return for rate classes and approved the methods for NET's cost of service and marginal cost studies. These cost allocation methods were adopted as part of the foundation for the rate structure approved in D.P.U. 89-300.

D.P.U. 91-30, at 15.

The Department has stated consistently that it will not undertake a review of the Company's cost studies in the transitional rate restructuring process. D.P.U. 92-100, at 11; D.P.U. 91-30, at 14-15. A review of NET's costs is undertaken only in the context of a full rate case. The transitional rate restructuring process is a review of rates, not costs, using cost information as an important, but not the only, factor in determining just and reasonable rates. In the transitional filings, the Department does not approve the cost studies. Furthermore, even if a review of the Company's cost studies was within the scope of the transitional rate proceedings, there is an insufficient record in the instant proceeding for any

substantive findings regarding the cost studies. No cost witness appeared on behalf of the Company, and the Attorney General chose not to sponsor a witness on this issue.

II. TRANSITIONAL RATE CHANGES

A. Introduction

As noted, most of NET's proposed changes represent transitional movement toward target rates adopted in D.P.U. 89-300. In addition, based on new data, the Company has proposed to revise target rates for certain of its premium service options using the methodology adopted in D.P.U. 89-300 (see Section II.B.1.b, infra, for discussion). Further, in compliance with the Department's directive in D.P.U. 92-100, the Company has proposed to introduce a new premium service option in the Western LATA (see Section IV.B, infra, for discussion). Id. at 20-21. The proposed rate changes for the Company's services are discussed in this Order by customer class.

B. Residence Class

1. Residence Exchange Service, Message Telecommunications Service, and Operator Service

a. Introduction

Residence exchange services include measured service, local unlimited service, and "premium" services. ⁹ In D.P.U. 91-30, the

⁹ Premium services include, but are not limited to, Metropolitan service, Circle Calling service, Suburban service, and Baystate East (metropolitan and
(continued...)

Department adopted a target rate structure for residence exchange services that includes two components: dial-tone and usage. Id. at 61-62. The Department found that by disaggregating exchange service components, the proper pricing signals would be sent to consumers. Id. NET customers are informed semiannually, through the use of bill inserts, of the rates associated with the dial-tone component and the usage component of their rates. In D.P.U. 89-300, the Department approved the Company's proposal to move over time toward a dial-tone line target rate of \$15.00 per month for all residence exchange services. Id. at 82.

The residence exchange service rate structure in place before D.P.U. 89-300 consisted of 22 different rates for local unlimited service, accounting for variables such as the number of residence access lines that were within an end user's primary calling area ("PCA").¹⁰ In D.P.U. 89-300, the Department found that the number of main exchange lines that can be reached should not be a determinant in the pricing of exchange services. Id. at 129. Therefore, the Department approved a target rate structure for all residence exchange services that includes the achievement of a single rate for each exchange service. Id.

⁹(...continued)

nonmetropolitan) services (Exh. NET-1, at 43).

¹⁰ In D.P.U. 89-300, the Department adopted a uniform definition for a toll-free, local calling area, or PCA, consisting of home and contiguous exchanges. Id. at 65-66.

at 128.

In D.P.U. 89-300, the Department accepted NET's method for deriving target rates for the usage component of local unlimited and premium residence exchange services based on average usage of all subscribers. Id. at 101. The target usage component for local unlimited service includes \$6.94 worth of local usage, assuming 111 calls per month priced at the applicable usage rates. Id. at 79. The target usage component for premium services is calculated by adding \$6.94 (the target usage component for local unlimited service) to the average toll usage of subscribers to the premium service, priced at the target toll rates. Id. at 125.

Residence message telecommunications service ("MTS"), or toll service, and operator service (for business, residence, and coin) are currently charged under NET's MTS Schedule II (Exh. NET-1, Att. A at 4).

b. Company Proposal

The current residence dial-tone line rate is \$7.42. In this filing, the Company proposed to increase the dial-tone line rate to \$9.91, an increase of \$2.49, in order to move closer to the target dial-tone line rate of \$15.00 (Exh. NET-1, at 44).

¹¹

¹¹ At present, there is a charge for temporary suspension of residential service. That charge is equal to the residential dial-tone line rate. In order to maintain parity with the dial-tone rate, the Company proposed to increase the charge for residence temporary suspension of

The Company also proposed to consolidate rates for the usage component of residence exchange service toward target levels, which would result in increases for some customers and decreases for other customers (id. at 43). Thus, the Company would reduce the number of rates for residence unlimited service from five to one, ¹² for Metropolitan service from six to one, and for Circle Calling service from four to one (id., Att. C at 8-9). The consolidation would result in an average increase of \$1.96 for local unlimited service customers and an average increase of \$3.37 for residence premium exchange services customers (id., Att. A at 1). Increases in usage rates for residence premium exchange services reflect the results of the Company's June, 1992 calling data (id., Att. C at 10-15). In order to determine the usage component rate for each of the residence premium exchange services, the increase in average toll use was priced at target toll rates (id.).

As noted above, the Company also proposed changes to the usage component target rates for residence premium exchange service. In D.P.U. 89-300, the Department accepted the Company's method for deriving target rates for the usage component of these

service to \$9.91 (Exh. NET-1, Att. C at 9).

¹² NET proposed similar consolidations for two-party service, in order to maintain the existing rate relationship with one-party service (Exh. NET-1, Att. C at 8). On June 6, 1993, NET eliminated four-party service and transferred existing customers to two-party service (id.).

services and instructed the Company to revise the targets as appropriate. Id. at 128.

The Company's target rate revisions for residence premium services are consistent with previous Department directives, using the methodology developed in D.P.U. 89-300. The Company indicated that June, 1992 calling characteristics data reflected changes in usage, which necessitated increases in the target usage components for these services (Exh. NET-1, Att. C at 23-28). The data show an increase in the average number of calls made by subscribers of each of these services and a slight shift in the time of day that calls are placed, i.e., peak usage increased and off-peak usage decreased by a corresponding amount (id.). Based on this data, the Company proposed to revise the target usage component rates for premium services (id. at 22).¹³ The increases in the revised target rates range from zero to \$1.90 per month (id. at 23).¹⁴

NET proposed in this filing to reduce the residence MTS and operator service rates (id., at 4-5). Specifically, the Company proposes a \$0.02 per minute reduction in the initial period

¹³ In order to derive a new target usage component for these services, the new average number of toll calls is priced at the applicable peak and off-peak target rates (Exh. NET-1, Att. C at 23-27).

¹⁴ The Company's proposed target rate for Baystate Non-Metropolitan service decreased by \$5.45 (Exh. NET-1, Att. C at 23).

charge and a reduction of up to \$0.01 per minute for the overtime period (id. at 5).

c. Positions of the Parties

i. The Company

The Company maintains that residence exchange services, MTS, and operator service rates are revised in accordance with the Department's directives to move rates toward target rate levels (Company Brief at 19-20, 34). The Company argues also that no party opposed the proposed changes, and, therefore, the Department should approve the changes as filed (id.).

ii. The Attorney General

The Attorney General contends that the Company's proposed residence dial-tone rate increase is "excessive" and should be rejected (Attorney General Brief at 4). The Attorney General argues that while the Department is charged with protecting monopoly ratepayers, it has allowed NET to "shift a large proportion of its costs onto those captive monopoly ratepayers whom the Department should protect" (id.).

d. Analysis and Findings

Based on the record in this case, we approve as filed NET's proposals for residence exchange services.

The current residence dial-tone line rate is \$7.42. In D.P.U. 89-300, the Department found that \$15.00 was a reasonable target rate for the residence dial-tone line. Id. at 82. In

D.P.U. 92-100, the Department directed the Company to achieve the target rate in three filings, including the instant case. Id. at 69. The current residence dial-tone line rate is still approximately only half of the target rate. In light of the increasingly competitive markets in which the Company operates, and the imminence of competition at the local exchange level (see Exh. DoD-1), it is more important than ever that steady progress toward cost-based rates be maintained. Therefore, the proposed increase of \$2.49 in the rate for the residence dial-tone line represents a reasonable step toward the target rate and is consistent with our directives in D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100.

The Company's proposed consolidation of exchange rate groups into a single rate for the usage components of local unlimited service and premium services also continues the gradual movement of rates toward their intended target levels. We find that these changes are consistent with the Department's rate structure goals, and we approve the changes as filed. The Department also finds that the revised target rates for premium services are in compliance with the Department's directives in D.P.U. 89-300. In order to ensure that the target rates for residence exchange services reflect the cost of providing these services, we direct the Company to continue to propose revised target rates for residence exchange services as changes in usage

patterns occur.

The Department also finds that the Company's proposed changes to its MTS Schedule II (residence toll and all operator services) represent reasonable movement toward target rates and are, therefore, approved as filed.

The Attorney General's characterization of the present filing as "cost shifting" is incorrect. This filing, as with the preceding two filings, is not an investigation into cost allocation; it is an investigation into rate structure, and a change in rates shifts revenues, not costs.

C. Business and Carrier Access Services

1. Business Exchange Service, Local Use, Message Telecommunications Service, 800 Service, Direct Inward Dialing, and Terminating Number Screening

a. Company Proposal

The target dial-tone line rate of \$13.00 for business exchange service was implemented in 1991. In this filing, the Company proposed rate changes for business exchange service, local use, MTS, 800 service, direct inward dialing ("DID"), and terminating number screening ("TNS"). ¹⁵

¹⁵ MTS is intrastate long-distance calling service. 800 service allows the 800 customer to be billed for the call rather than the call originator. DID is a service that provides for the direct routing of calls to a particular line, typically within a large organization with a private branch exchange ("PBX"). DID lines are used to make PBX systems comparable to NET's Centrex service. TNS is an optional service which uses database entry to alert operators that collect and third-number calls cannot be

The Company proposed to consolidate the number of usage rates for business unlimited service from four to a single rate, resulting in monthly increases ranging from zero to \$8.07, with the average increase being approximately \$0.28 (Exh. NET-1, at 30). In addition, the Company proposed to increase the rates for PBX unlimited service in order to retain the price relationship of this service with that of business unlimited service (id. at 30-31).

The Company also proposed to reduce the business local use per-message rate in the Eastern LATA from \$0.0603 to \$0.03, or by \$0.0303, in order to move toward the target rate of \$0.01 (id. at 29).¹⁶

NET proposed reductions in the business MTS (MTS Schedule III) rates in the Eastern LATA (id. at 14). Under the proposed changes, the day period per-minute rate would be reduced to \$0.085, and the application of the day-period credit would be reduced from a usage level of 3,000 minutes to 1,500 minutes (id.). The Company also proposed to reduce the per minute credit from \$0.05 to \$0.03 to ensure that the day charges do not fall below the peak period target rate level of \$0.055 per minute (id.).

billed to a particular telephone number.

¹⁶ Each call is charged a per-message rate, which covers the set-up and billing charges for the call.

Regarding 800 service, the Company proposed to establish a target rate of \$16.00 per month for a traditional 800 service line (id. at 32). In addition, the Company proposed to reduce the current monthly rate for a traditional 800 service line from \$25.00 to \$20.00, as the initial step in moving toward the proposed target rate of \$16.00 (id.).

Regarding DID service, the current charge is \$50.00 per trunk equipped for the first ten trunks, and \$31.52 for each additional trunk (id. at 31). In D.P.U. 92-100, the Department established a target rate of \$15.00 per DID trunkline. Id. at 35. In this filing, the Company proposed to move the DID rate toward the target by reducing the current charge for the first ten trunks to equal the current charge for each additional trunk (Exh. NET-1, at 31). In addition, NET proposed to reduce the charge for a group of 100 numbers from \$26.19 to \$1.00, the target rate adopted by the Department in D.P.U. 92-100 (id.).¹⁷

The Company also has proposed to modify its current charges for TNS (id. at 32). The current rate structure consists of a recurring monthly charge, but the Company stated that the marginal costs for the service reflect no recurring costs (id.). Therefore, in order to better reflect underlying costs, the

¹⁷ The Company is concerned that the target rate level of \$1.00 for a group of 100 numbers may need to be increased if, because of the dramatic reduction in this charge, the Company's finite supply of telephone numbers is jeopardized (Exh. NET-1, at 32).

Company proposed to eliminate the monthly charge for TNS and establish a nonrecurring charge of \$50.00 per group of 100 numbers for PBX and Centrex ¹⁸ customers (id. at 32-33).

b. Positions of the Parties

i. The Company

The Company argues that its proposed rate changes for business exchange service are consistent with the Department's principles established in D.P.U. 89-300 and reflect a gradual movement toward target rates, and, therefore, the Department should approve the Company's proposed rate changes (Company Brief at 29-30). The Company also argues that its proposed local usage rates for business service are just and reasonable, and represent movement toward target rate levels, while balancing other factors (id. at 26).

NET asserts that its proposed changes in business MTS rates move rates appropriately toward target rate levels (id. at 16). The Company also contends that its proposed rate changes for 800 service, DID service, and TNS service are reasonable and should be approved as filed (id. at 53).

The Company argues that the Attorney General's proposal to limit rate changes to one third of the difference between current

¹⁸ Centrex service is a business telecommunications system in which the controlling dial switching equipment is located at a telephone company's central office that normally serves the principal premises of a customer.

and target rates is overly simplistic, unsupported by the record, and not consistent with the Department's directives to achieve target rates while also balancing the Department's rate structure goals (Company Reply Brief at 6).

The Company claims that the Attorney General's proposal to increase the threshold for the business MTS credit would move the usage credit in the opposite direction of the target rate and, therefore, should be rejected by the Department (id. at 17). The Company asserts that, contrary to the arguments of the Attorney General, its proposed target rate for 800 service is reasonable and cost-based (id. at 15-16).

In response to OMIS's contention that the nonrecurring charge for TNS should only apply when TNS is ordered as a discrete service, the Company states that it is willing to apply that charge only when TNS is ordered separately (id. at 29). NET states that this change is consistent with the Company's application of a TNS charge for residence and single-line business customers (id.).

ii. The Attorney General

The Attorney General argues that the Department should only approve business MTS and local usage rates which move one third toward the established target rates (Attorney General Reply Brief at 2). In addition, the Attorney General asserts that the Department should not allow the Company to decrease the usage

credit threshold for business MTS service (Attorney General Brief at 9).

The Attorney General argues that the Company's proposed changes in DID and 800 service rates should not be approved because the proposed changes are not equal to one third of the difference between current rates and target rates (id. at 10-11, 16). The Attorney General asserts that the Department should reject the Company's proposed target rate of \$16.00 for 800 service because the cost of 800 service is unsubstantiated (id. at 38-39).

In opposing OMIS's argument that the nonrecurring charge for TNS should only apply when TNS is ordered as a discrete event, the Attorney General argues that there is a cost every time a customer requires TNS on a changed or updated line, and, consequently, the customer should be charged the nonrecurring rate each time TNS is requested (Attorney General Reply Brief at 8-9).

iii. DoD

DoD argues that all of the Company's proposals correctly move the Company's rates toward their cost-based targets (DoD Brief at 6-7). Therefore, DoD recommends that the Department accept NET's proposals without modification (id.). In response to the Attorney General's proposal to require NET to move all business rates one third of the difference between current rates

and target rates, DoD argues that this proposal is neither practical nor beneficial (DoD Reply Brief at 3).

iv. OMIS

OMIS argues that the Company's proposed nonrecurring charge for TNS should apply only when TNS is ordered as a discrete service and not when TNS is requested as part of an order for new, updated, or changed service (OMIS Brief at 3).

c. Analysis and Findings

We find that the rate changes proposed by the Company for business exchange service, local use, MTS, 800 service, and DID represent a reasonable step in moving toward previously or newly established target rates. As previously stated (see Section I.C, supra), the Attorney General's proposal to limit rate changes to one third of the difference between current and target rates is impractical in a revenue-neutral filing. The Company's proposed changes continue the gradual movement of business rates toward the target levels, and those changes are approved as filed.

The Department agrees with OMIS that the nonrecurring charge for TNS should only apply when it is ordered separately, in order to make application of that charge consistent with the method used for residence and single-line business customers. Accordingly, in its compliance filing the Company shall modify the applicable tariff language to provide that the TNS nonrecurring charge shall apply only when the service is ordered

separately.

The Department also finds that the Company's proposed target rate for 800 service is reasonable. The Company's methodology for developing the target rate is consistent with the methodology approved in D.P.U. 89-300, and the target rate is cost-based.

2. Analog Private Line and Special Access

a. Company Proposal

The Company has proposed to further align the rates for analog private line and special access services, offered in the Company's tariffs D.P.U. Mass. Nos. 10 and 15, respectively (Exh. NET-1, at 33). NET is continuing movement toward target rate levels by lowering the initial mileage charge (i.e., the first nine miles) for both private line and special access services from \$4.16 per mile to \$3.42 per mile (id. at 33-34). The reduction constitutes a 33 percent difference between the existing rates for the first and second mileage band (id. at 33).

NET also proposed to move analog channel rates to, or toward, target rates levels, with increases and/or decreases of no more than five percent (id. at 34; Att. D at 2, 5). The Company proposed that the \$2.3 million annual revenue decrease resulting from the proposed reduction in mileage and local channel rates be recovered through increases ranging from one half of one percent to eleven percent per local channel, channel

termination, and special access fixed rate elements (id., Att. D at 2, 8, 10).

In addition, NET proposed to further restrict its Telpak service (5000 series private lines) (id., Att. A at 5).¹⁹ The proposed restrictions are twofold: (1) if a circuit is removed, another circuit cannot take its place; and (2) spare capacity on an existing Telpak service can not be used (id.).

b. Positions of the Parties

i. The Company

The Company maintains that the rates proposed for analog private line and special access services are just and reasonable, and consistent with the Department's regulatory goals (Company Brief at 45). In addition, NET states that since no party to the case opposed the Company's proposed changes in analog private line or special access rates, they should be approved by the Department as filed (id.).

In response to concerns raised by OMIS regarding NET's Telpak service, NET indicated that it would be willing to modify its proposal by allowing a Telpak customer to consolidate the service without adding to the total number of circuits (id. at 44-45, citing Tr. 2, at 118). The Company maintains that its proposal would satisfy the concerns of OMIS (Company Reply Brief

¹⁹ Telpak is an analog private line service that has been "grandfathered" for existing customers since December, 1982.

at 28).

ii. The Attorney General

The Attorney General argues that the rates for channel charges should be adjusted to eliminate any revenue loss and to ensure revenue neutrality for the proposed adjustments for analog private line (Attorney General Brief at 20). Regarding Telpak services, the Attorney General maintains that Telpak customers should be prevented from moving or consolidating capacity (Attorney General Reply Brief at 8). The Attorney General contends that the Department should discourage continued use of Telpak rather than continuing to make Telpak desirable by allowing the proposed changes sought by OMIS (id. at 9).

iii. OMIS

OMIS asserts that Telpak customers should be allowed to consolidate Telpak service, as users take circuits out of service or migrate circuits from analog Telpak to digital or switched services (OMIS Brief at 5). OMIS claims that without this change, Telpak customers could be required to pay for unused capacity (id.)

c. Analysis and Findings

In D.P.U. 89-300, we directed NET to increase rates for private line channels and related rate elements because generally the rates were below marginal cost, when compared with other rate elements, such as mileage charges, which were well in excess of

marginal cost. Id. at 189. The record in this proceeding indicates that NET is continuing to move rates toward target levels for both analog private line and special access services. The record further indicates that under NET's proposal, the revenue shortfall for private line services would be recovered through increases in all analog local channels and channel terminations. Therefore, we find that the Company's proposal is reasonable.

We agree with OMIS that Telpak customers should be allowed to consolidate service as long as the total number of Telpak circuits is not increased. Accordingly, we direct the Company in its compliance filing to include tariff language that so modifies NET's proposed restrictions on Telpak service.

3. Digital Private Line Services

a. Company Proposal

In this filing, NET has proposed to lower service charges for Superpath 1.5 service ("Superpath")²⁰ to continue the movement toward the target rates established in D.P.U. 92-100 (Exh. NET-1, at 35). Some rate elements have been reduced to target levels, while others have been lowered to continue the transition toward target rates (id.).

The Company also has proposed to set target rates for

²⁰ Superpath is a two-point digital service that provides 24-channel capacity over one facility.

Superpath Fractional T-1 service ²¹ in compliance with D.P.U. 92-100 (id. at 35). NET indicated that the proposed target rates are based on the relationship of the current rates with the existing Superpath rates (id. at 36). The Company also proposed to lower the current rates for Superpath Fractional T-1 in a manner and degree similar to the Superpath rate reductions, in order to maintain the existing price relationships with Superpath (id.).

In compliance with D.P.U. 92-100, the Company proposed to establish a revised Flexpath ²² port target rate of \$209.00 to maintain the current parity between Flexpath and DID, its cross-elastic service (id., Att. D at 13). NET also proposed to lower the current Flexpath port charge from \$465.00 to \$357.00, or 23 percent, reflecting a similar reduction in DID charges (id. at 39; Att. D at 13).

NET also proposed to establish target rates for Digipath Digital Services II ("DDS II") ²³ and reduce overall rates for DDS II by approximately 17 percent (id. at 39-40).

b. Positions of the Parties

²¹ Superpath Fractional T-1 is a digital private line service with an eight- or twelve-channel capacity.

²² Flexpath is a digital service that provides direct inward and outward dialing between a customer's digital PBX and the Company's central office.

²³ DDS II provides single digital channels.

i. The Company

The Company maintains that its proposed rate changes for digital private line services are consistent with Department objectives, maintain current pricing relationships where appropriate, and continue to move toward target rates (Company Brief at 50). Therefore, NET contends that its proposed rates should be approved as filed (id.). Regarding the Attorney General's argument on Flexpath target rates, the Company claims the proposed target rate levels have been established to maintain the current parity with DID service and recover marginal costs (Company Reply Brief at 14).

ii. The Attorney General

The Attorney General argues that the Company has provided no compelling justification to transition rates for Superpath, Superpath Fractional T-1, Flexpath, and DDS II at an accelerated speed, and recommends that these rates be reduced by one third of the difference between present and target rates (Attorney General Brief at 11-15). The Attorney General also claims that NET's proposed target rate of \$209.00 for a Flexpath digital port should be rejected because NET's target rate does not maintain the cross-elastic price relationship between DID and Flexpath (id. at 14).

c. Analysis and Findings

Based on the record, we find that the Company's proposed

rate reduction for Superpath is a reasonable step in moving toward previously established target rates. Further, we find that this rate reduction will maintain the existing price relationship with business toll rates, a cross-elastic service.

The Department also finds that NET's proposed rate reductions for Superpath Fractional T-1, Flexpath, and DDS II are reasonable. The proposed rate reductions for Superpath Fractional T-1 maintain the current rate relationship with Superpath at the proposed rate levels. In addition, we find the Company's proposed target rates for Superpath Fractional T-1 and DDS II to be reasonable and in compliance with the Department's directives in D.P.U. 92-100. Lastly, we find the Company's revised target rates for Flexpath to be reasonable and in compliance with our directive in D.P.U. 92-100 requiring that Flexpath target rates maintain the appropriate pricing relationship with DID.

4. Integrated Services Digital Network Basic Service

a. Introduction

In NET-Integrated Services Digital Network ("ISDN") Basic Service, D.P.U. 91-63-B (1992), the Department found NET's projected costs and cost methodology for ISDN Basic service reasonable for the purposes of that proceeding, and directed the Company, as part of its 1993 transitional filing, to submit a comprehensive marginal cost study for all ISDN Basic rate

elements, including usage. ²⁴ Id. at 44-46. NET also was directed to track the costs and revenues associated with ISDN Basic, and to submit billing determinant data in its annual transitional filings. Id. at 110-111.

b. Company Proposal

NET's filing establishes interim target rates for ISDN Basic, a service that has previously been classified by the Department as basic monopoly, at the same level as the current effective rates for ISDN Basic (Exh. DPU-27). ²⁵ Although the Company filed an updated MCS for ISDN Basic rate elements, NET has not proposed to move the rates closer to marginal costs (id.). The Company stated that a reduction in present rates would not provide for full recovery of all appropriate costs, i.e., embedded and marginal costs (Exhs. NET-4, Tab E28 at 4; DPU-27; DPU-32). Therefore, NET has proposed that, until ISDN costs are stabilized, target rates be set at current rates

²⁴ ISDN Basic voice usage charges are determined by the customer's existing class of local exchange service (Exh. NET-4, Tab E28). Circuit-switched data usage is charged on a per-message, per-minute basis at the same rate as voice usage (id.). ISDN packet-switched data usage rates are priced consistent with the rate levels for NET's existing Infopath service (id., Tab E25, Att. 2) (see Section II.C.5, infra, for a discussion of Infopath packet-switched data usage).

²⁵ In D.P.U. 91-63-B, the Department found that ISDN Basic was a basic, monopoly service that has a potentially far-reaching and significant role in the telecommunications infrastructure of the Commonwealth. Id. at 34.

(Exh. DPU-27).

c. Positions of the Parties

i. The Company

NET maintains that the Attorney General's allegations regarding the rate changes for ISDN Basic clearly misstate the facts (Company Reply Brief at 11). The Company argues that the monthly rates substantially exceed the marginal costs of the service (id. at 11-12). NET contends that although the nonrecurring charges do not exceed the marginal costs in all cases, it is reasonable at this time to use the tariffed rates, approved by the Department in D.P.U. 91-63-B, as interim target rates (id. at 12).²⁶ NET argues that the service is still new and the Company needs to gain experience before reestablishing rates for ISDN Basic (id.). NET rejects the Attorney General's recommendation that nonrecurring rates for ISDN Basic be set closer to cost (id. at 12).

ii. The Attorney General

The Attorney General argues that the nonrecurring charges for the ISDN Basic subscriber line, feature change, and customer premise modem pooling rate elements should be increased to cover the marginal costs of these services (Attorney General Brief

²⁶ NET indicated that it expects to use contribution from Elements 1 and 2 for ISDN Basic cost recovery until the next transitional filing when the Company is committed to undertaking an extensive study of nonrecurring charges (Exh. DPU-36).

at 19-20).

d. Analysis and Findings

The Department stated in D.P.U. 91-63-B, "[ISDN Basic] has a potentially significant impact on the manner in which consumers obtain access to the public telecommunications network and [] it should therefore be considered as 'basic' for the purposes of determining the appropriate pricing" Id. at 83. In determining rates for ISDN Basic in that case, we were guided not only by our telecommunications rate structure goals but also by the fundamental objective of ensuring that customers have the opportunity to derive the maximum benefits from this new technology. Id. at 87.

In D.P.U. 92-100, the Department stated that in setting rates and target rates, we must consider carefully the characteristics of each service in order to determine the proper emphasis to place on each rate structure goal. Id. at 60. Further, we noted that "... the Department must weigh several factors, such as market conditions, competitive implications, nature of services, and demand elasticities in establishing target rates for different basic monopoly services." Id. at 61.

In D.P.U. 91-63-B, the Department recognized the difficulty of establishing proper rates for ISDN Basic and the uncertainty about the precise future demand for the service. Id. at 85-86. Because the Department found ISDN Basic to be a basic, monopoly

service, initial rates were set close to marginal costs.²⁷ In this filing, the Company has provided an updated MCS indicating that, overall, the marginal costs have declined, while the nonrecurring costs have increased (Exhs. NET-4, Tab E28; DPU-36).

The record in this case indicates that there has been limited subscription to ISDN Basic. Mindful of the Department's rate structure goals, and given the uncertainty surrounding the demand for ISDN Basic, we agree with the Company that it would be premature to raise ISDN Basic rates at this time. Accordingly, we find that the Company's proposed interim target rates are reasonable. Therefore, we approve the Company's proposal as filed. However, we direct the Company in its study of nonrecurring charges (see n.26, supra) to include an analysis of the nonrecurring costs for ISDN Basic. In addition, the Company shall continue to comply with all applicable directives in D.P.U. 91-63-B.

5. Infopath Packet Switching Service

a. Company Proposal

The Company has proposed to price the nonrecurring and recurring rate elements for Infopath packet switching service

²⁷ In D.P.U. 91-63-B, we approved nonrecurring charges for digital electronic telephone services that did not cover the associated marginal costs. Id. at 58.

("Infopath")²⁸ at current rate levels.²⁹ The Company also has proposed packet-switched data usage charges based on a kilopacket rate structure (Exh. NET-1, at 19).

The Company has proposed target usage rates, and has reduced current usage rates towards target rate levels for Infopath and ISDN Basic packet-switched data usage (Exhs. NET-1, at 19; DPU-25; DPU-33).³⁰ The target rates were developed using the present relationship between packet-switched data usage and business toll service (Exh. NET-1, at 19). The day-period kilopacket rate was converted to a per-minute rate and then compared to the business day toll rate (id., Att. H at 22, 33). This relationship was then maintained to calculate kilopacket target rates (id.).

The Company compared present, proposed, and target rates as follows:

²⁸ Infopath provides synchronous and asynchronous network transport of data packets for high speed transmission through the network (D.P.U. Mass. No. 10, Part C, Section 4).

²⁹ Since the Company has classified Infopath as a basic competitive service, NET has not proposed target rates for the nonrecurring and recurring rate elements (Exh. DPU-23).

³⁰ NET prices its ISDN Basic packet-switched data transport under the same pricing structure as Infopath. See Section II.C.4, supra, for pricing of ISDN Basic.

<u>Infopath Packet Switching Service</u>			
<u>Rate Per Kilopacket</u>			
<u>Present</u>			
<u>Proposed</u>	<u>Target</u>		
Day	\$ 0.70	\$ 0.57	\$ 0.37/peak
Evening	0.65	0.37	0.24/off-peak
Night/Weekend	0.60	0.24	0.24/off-peak

(id. at 33).

b. Positions of the Parties

i. The Company

The Company refutes what it contends are the Attorney General's unsupported allegations that Infopath does not cover its associated marginal costs (Company Reply Brief at 11-12).

ii. The Attorney General

The Attorney General argues that the nonrecurring costs for Infopath do not reflect the total cost of provisioning an Infopath circuit, and, therefore, the Department should increase the rates³¹ to at least the marginal cost level (Attorney General Brief at 18).

c. Analysis and Findings

Contrary to the Attorney General's contention, the record indicates that NET's nonrecurring rates for Infopath cover the associated marginal costs, and, therefore, there is no reason to increase the rates at this time. Accordingly, the Department

³¹ The Department interprets the Attorney General's use of the term "costs" as meaning "rates" (see Attorney General Brief at 18).

finds that NET's proposal to establish nonrecurring rates at current levels for Infopath is reasonable.

Based on the record in this case, we also find that NET's proposal for packet-switched data usage rates is in compliance with the Department's directives in D.P.U. 91-63-B. NET has averaged the respective marginal costs for ISDN-based packet-switched data transport and non-ISDN-based packet-switched data transport. We find that averaging the costs in this instance is reasonable and that NET's proposal satisfies the Department's goal of simplicity. Accordingly, we find that NET's proposal for packet-switched data transport is reasonable.

6. Switched Access Service

a. Introduction

Switched access services are used by other carriers to originate and terminate calls over NET's network. For a carrier to transport a call to or from most customers in Massachusetts, it must pay NET for the use of local loops and central office switching.

Switched access services are the wholesale counterparts of the Company's retail MTS and 800 services, and are targeted to be priced slightly below the retail services. In D.P.U. 89-300, the Department ordered the rates for switched access services and retail services to be linked in order to retain the wholesale/retail pricing relationship between the two services.

Id. at 217.

b. Company Proposal

NET has proposed to move the current switched access rates in the Eastern LATA toward target rate levels, reflecting similar decreases proposed for retail business MTS rates (Exh. NET-1, at 19) (see Section II.C.1, supra). The proposed changes include reducing the day-time originating common carrier line ("CCL") charge by approximately \$0.02, reducing the monthly credit threshold from 3,000 to 1,500 minutes, and decreasing the value of the credit from \$0.05 to \$0.03 per minute (Exh. NET-1, Att. B at 10). In addition, NET proposed to eliminate the premium/non-premium rate structure distinction for the originating CCL (id., Att. A at 14).

c. Positions of the Parties

i. The Company

NET asserts that its proposal to reduce switched access rates complies with the Department's directives in D.P.U. 89-300 (Company Brief at 23-24). Moreover, NET maintains that because none of the interexchange carriers ("IXCs") raised any objection to the Company's proposal to decrease rates for switched access, the Department should approve the proposed changes as filed (id. at 24).

ii. The Attorney General

The Attorney General recommends that the Department approve switched access rates that are one-third of the difference between current and target rates (Attorney General Brief at 17).

iii. DoD

DoD recommends that NET's proposed changes be accepted by the Department without modification (DoD Brief at 7).

d. Analysis and Findings

In D.P.U. 89-300, the Department approved the Company's proposal to link switched access rates to its business MTS rates, in order to preserve the wholesale/retail price relationship and to send the correct pricing signals to customers about the services, which have similar underlying costs. Id. at 216-217. Because of this relationship, any reduction in switched access rates requires a similar reduction in business MTS rates. Id.

Given this pricing structure and the Department's objective to balance its goals of economically efficient pricing and rate continuity, we find that the Company's proposed reduction in the day-time originating CCL charges, and the corresponding reductions in the monthly credit threshold and the value of the credit, are reasonable.

D. Nonrecurring and Service Charges

1. Company Proposal

NET has proposed to establish target rates at the current

tariffed levels for (1) Element 1 and 2 charges,³² (2) restoration of service after disconnection for non-payment, (3) reconnection of service after temporary suspension (e.g., seasonal customers), and (4) premises work charges (Exh. NET-1, Att. H at 23). NET has categorized these rate elements as basic monopoly (Exh. NET-1, at 5-10).

NET used two criteria to determine cost recovery. First, if the current tariffed rate element was equal to or greater than the connection cost,³³ the target rate was set at the existing rate level (id., Att. H at 23). If the current rate element was below marginal cost, the charge was analyzed in conjunction with the associated service, and if the nonrecurring revenue shortfall was recovered from contribution in the monthly recurring rate for the service over the life expectancy of the service, the current tariffed rate was determined to be the target rate level (id.). NET suggested that these charges should have variable target rate levels which are revisited each year to ensure that the charge recovers the connection cost either initially or over the life

³² NET applies an Element 1 service ordering charge for the receiving, recording, and processing of a customer's request for service (Exh. NET-4, Tab E3). An Element 2 central office line connection charge is applied to recover the costs of establishing or changing service in the central office (id., Tab E4).

³³ Connection costs include, but are not limited to, the average customer service representative's time spent on service orders (Exh. NET-4, Tab E3).

expectancy of the service (id.).

2. Positions of the Parties

a. The Company

The Company maintains that the proposed target rate levels comport with the Department's directives, are reasonable, and are consistent with the development of previous target rates (Company Reply Brief at 13). NET contends that the proposed target rates for Element 2 exceed the associated marginal costs of the service on a rate element basis (id.). The Company argues further that the proposed target rates for Element 1 exceed the marginal costs over the life expectancy of the underlying service (id. at 13-14). The Company acknowledges that these target rates should be revisited in each transitional filing to ensure that the rates recover the associated costs (id.).

b. The Attorney General

The Attorney General maintains that NET's methodology for establishing target rates for Elements 1 and 2 is inconsistent with the Department's rate design goals of economic efficiency, fairness, and rate continuity (Attorney General Brief at 9). The Attorney General asserts that these target rates should be increased to cover the marginal costs of the services (id.).

3. Analysis and Findings

As stated in D.P.U. 92-100, in setting target rates for basic monopoly services, the marginal costs of the service can

and should be used as a guide. Id. at 60. However, the Department also must appropriately balance the Department's rate design goals in setting target rates. Id. The Department acknowledged further that, as the transition process continued on its course toward cost-based rates, the Department would have to continue weighing certain factors, such as the nature of services, in establishing target rates for different basic monopoly services. Id. at 60-61.

Regarding the recovery of any revenue shortfall for nonrecurring revenue elements, the Company's contribution analysis indicates that the monthly contribution from exchange services would allow for recovery of costs associated with Elements 1 and 2 within the first month for most exchange services. Elements 1 and 2 are not independent charges; that is, they are generally incurred when a customer establishes telephone exchange service with NET. Therefore, under NET's proposal, as long as exchange services continue to cover their associated marginal costs and provide a contribution, the costs associated with Elements 1 and 2 will be recovered.

We find that NET's cost recovery proposal is reasonable. Accordingly, the Department finds that NET's proposal regarding target rates for service charges is reasonable at this time, and is, therefore, approved.

III. PAY-TELEPHONE SERVICE

A. Coin Class

1. Introduction

NET provides two types of pay-telephone services: public pay-telephone service, and semipublic pay-telephone service. NET's public pay telephones are provided at the discretion of the Company, and the revenues are generated solely through use of the pay telephone by members of the public. Semipublic pay-telephone service is provided at the request of a location owner, and the location owner is responsible for nonrecurring and monthly charges. NET's Eastern LATA coin, sent-paid calls currently are charged under the Company's MTS Schedule I (Exh. NET-1, at 17). This schedule contains three rate bands, which vary by time-of-day, with rates for initial and additional minutes (id. at 18).

2. Company Proposal

NET proposed to change the rate structure for toll calls placed from its pay telephones in the Eastern LATA (id. at 17).³⁴ The Company proposed to reduce the per-minute charges in the third toll rate band (i.e., 15 air miles and over) to the level of the second toll rate band, thereby eliminating the third rate band (id.).

3. Positions of the Parties

³⁴ The Company's rates for coin-paid calls are already at target in the Western LATA.

a. The Company

The Company argues that the proposed change would move the MTS Schedule I rates closer to the target rate levels established in D.P.U. 89-300 (Company Brief at 21). NET asserts that no party challenged the proposed changes, and, therefore, the Department should approve the proposed change as filed (id. at 21-22).

4. Analysis and Findings

Based on the record, we find that the Company's proposed change to its MTS Schedule I for coin-paid toll calls is reasonable. Accordingly, the Company's proposal is approved as filed.

B. NET's Charges to Providers of Pay-Telephone Service

1. Introduction

Pay-telephone service providers obtain access to NET's network by subscribing to NET's public access line ("PAL") service. The costs and revenues associated with PALs are allocated to the business class. See D.P.U. 89-300, at 271. As a result, any changes to rates and/or rate structure ordered by the Department for the business class directly affect pay-telephone service providers.

However, pay-telephone service providers also are competitors of NET in providing pay-telephone service, and in recognition of the disparity that exists between the rates that

NET charges itself for pay-telephone services and the rates that pay-telephone service providers must pay to NET, the Department found that an adequate level of commission payments to pay-telephone service providers was needed to offset the potential anticompetitive effects of the wholesale/retail rate relationship. Id. Therefore, the Department ordered NET to provide all Department-certified pay-telephone service providers a credit of 20 percent off the total monthly billed amount for each pay telephone that generates monthly revenue for NET of \$100.00 or more. Id. at 273-274. Because of the reductions to business use rates, the Department in D.P.U. 92-100 reduced to \$75.00 the monthly revenue threshold. Id. at 54.

2. Company Proposal

In the instant case, NET has not proposed any specific changes that would affect only pay-telephone service providers, other than the changes proposed for business customers in general, that were described in Section II.C.1, supra.

3. Positions of the Parties

a. The Company

NET asserts that the Department has repeatedly rejected MPA's calls to eliminate the Company's DA charges to pay-telephone service providers and to recover the costs from the general body of ratepayers (Company Reply Brief at 26-27, citing D.P.U. 91-30, at 85; D.P.U. 92-100). The Company contends that

because MPA has not presented any new evidence to warrant changing the structure or level of DA charges to pay-telephone service providers, the Department should reject MPA's request (id. at 27). Moreover, NET argues that MPA's reliance on DA charging policies in other jurisdictions "is interesting but is not dispositive of that issue in Massachusetts" (id.). According to the Company, eliminating DA charges for pay-telephone service providers would be inconsistent with the Department's goals of economic efficiency, fairness, and rate continuity (id.).

In its reply brief, the Company indicated that it would be willing to charge pay-telephone service providers a flat monthly rate of \$5.07 per PAL, provided there is a consensus among the pay-telephone service providers to adopt this plan (id. at 28). The flat rate would be based on the present average DA use billable to PAL lines, after taking into account the free ten-call allowance (id.).³⁵ NET states that this average DA use rate component calculation would be updated on a yearly basis to reflect the changes in calling characteristics (id. n.29).

b. The Attorney General

The Attorney General argues that MPA has not provided new evidence to cause the Department to change its position (Attorney General Reply Brief at 5). In responding to MPA's claim of

³⁵ G.L. c. 159, § 19A, provides that each customer shall receive an allowance of ten direct-dialed DA calls per month, without charge.

anticompetitive behavior by NET, the Attorney General contends that NET's monthly volume credit offsets the potential anticompetitive effects associated with the wholesale/retail relationship between NET and pay-telephone service providers (id. at 6).

c. MPA

MPA argues that it is anticompetitive for NET to charge pay-telephone service providers for DA while recovering DA costs for its own payphones from the Company's other customer classes (MPA Brief at 5-7). In addition, MPA asserts that NET's application of DA charges is not applied uniformly because, while the Company continues to recover the cost from pay-telephone service providers, NET has only just proposed to apply the same charges for DA to IXCs in this filing (id. at 6).

MPA also claims that the application of DA charges to pay-telephone service providers is inconsistent with G.L. c. 159, § 19A, which prohibits the imposition of DA charges to end-users of coin-operated telephones (id.). MPA claims that it was not the Legislature's intent that NET indirectly charge for DA through pay-telephone service providers, and that such charges impose "an unfair burden on NET's competitors" (id. at 7). Moreover, MPA claims that the New York Public Service Commission, faced with the same policy decision, ordered NET's affiliate, New York Telephone Company, to provide DA to pay-telephone service

providers free of charge so that the pay-telephone service providers could provide access to DA without an explicit charge to their customers (id. at 9-11, citing Exh. MPA-12). MPA argues that the Kansas State Corporation Commission and the Florida Public Service Commission ruled that the cost of providing DA to PAL locations should be recovered from the general body of ratepayers (id.). Finally, MPA contends that if the charge for DA were recovered from the general body of ratepayers, the potential impact to the Company's rate base would be minimal (id. at 7-9).³⁶

d. Representative Hodgkins

Representative Hodgkins asserts in support of MPA that it was not the Legislature's intent that § 19A be used by NET to discourage competition by requiring that pay-telephone service providers pay directly for DA charges (Representative Hodgkins Brief at 1). Representative Hodgkins claims that on the contrary the Legislature intended that all DA costs, including those from pay-telephone service providers, be recovered through NET's rate base (id.).

4. Analysis and Findings

³⁶ NET estimated that the revenue loss associated with not charging pay-telephone services providers for DA would be approximately \$295,000 per year, which would translate into an increase of approximately \$0.01 per month, per residential dial-tone line (Exh. MPA-16).

The Department rejects MPA's request to eliminate NET's DA charges to pay-telephone service providers. In previously denying similar requests, the Department stated:

In [our] Order in D.P.U. 89-20, [we] found that the issue of charging for DA and recovery of DA charges from pay-telephones by companies other than NET was moot. There is insufficient evidence in this docket to warrant revisiting that decision

D.P.U. 91-30, at 85; D.P.U. 92-100, at 55 (citations omitted).

In the instant case, MPA has not presented any new evidence sufficient to cause the Department to reverse its well-established policy.

Regarding the Company's response to MPA and the resulting proposal to charge pay-telephone service providers a flat monthly rate of \$5.07 per PAL for DA, rather than a discrete charge per DA call, we find this flat-rate proposal reasonable and consistent with the methodology approved by the Department for developing target rates for residence premium exchange services. Moreover, such a monthly charge should assist pay-telephone service providers in avoiding unnecessary DA charges that result from the inappropriate use of free DA service from pay-telephone service providers.

Accordingly, we direct the Company in its compliance filing to establish a flat monthly DA charge of \$5.07 per PAL, and remove its tariffed per-call rate for PALs. Because a flat monthly DA charge could potentially eliminate unnecessary DA

calls and, thus, lower the cost of DA, we direct the Company to include language in its compliance tariff indicating that the flat monthly DA charge will be reviewed and updated each year in January to reflect actual DA use from PAL locations.

IV. OTHER ISSUES

A. Lifeline/Link-Up

1. Introduction

Lifeline, adopted by the Federal Communications Commission ("FCC") in 1985, provides that the FCC will waive an amount up to the interstate subscriber line charge ("SLC") for eligible residence customers in any state if the state regulatory commission requires a reduction by the LEC of an equal amount of intrastate telephone charges. See NET-Lifeline/Link-Up, D.P.U. 89-57, at 1 (1989) (Order Opening Investigation). The SLC is currently \$3.50 per month. Thus, the Lifeline program provides low-income subscribers with a \$7.00 per month discount off of the total recurring monthly charge for residence service (exchange service rate plus the SLC). Link-Up, adopted by the FCC in 1987, provides low-income subscribers with a 50 percent reduction in the nonrecurring charge for installation of telephone service, up to a maximum of \$30.00 per subscriber. Id.

Eligibility for the Lifeline and Link-Up programs is determined based on participation in at least one of the following six assistance programs: Medicaid; Supplemental

Security Income; Emergency Aid to the Elderly, Disabled, and Children; Food Stamps; Fuel Assistance; or Aid to Families with Dependent Children. Id.

On September 15, 1992, the Department approved a Stipulation between NET and the Attorney General in D.P.U. 92-100, which focused primarily on improving NET's informational and outreach efforts for its Lifeline and Link-Up programs. Id. at 4-7. The Stipulation requires NET to: (1) provide annual training to its employees about Lifeline and Link-Up; (2) update its internal practices to instruct customer service representatives to supply information on these programs; (3) include basic information about these programs in its white pages directory; (4) continue utilizing annual bill inserts to notify residential customers about these programs; (5) limit sales efforts regarding optional services directed at subscribers of these programs; (6) expand its internal sales incentive programs to include incentives for the subscription of eligible customers to these programs; and (7) conduct a study to examine the feasibility and costs of expanding eligibility for these programs. Id. at 6-7, citing Stipulation ¶¶ 1, 2, 3, 6, 9, 10, 12.

NET did not propose any modifications to its Lifeline or Link-Up programs in this filing (Exh. DPU-11), and the Department endorses the continued operation of these programs.

The current rate for a residence dial-tone line is \$7.42; therefore, a Lifeline participant who subscribes to residence measured service, which is the Company's least expensive residence exchange service, is subject to a monthly charge of \$3.92.³⁷ In this Order, the Department has approved the Company's proposal to increase the residence dial-tone line rate to \$9.91 per month (see Section II.B.1.d, supra). Therefore, a Lifeline participant who subscribes to residence measured service will be subject to a monthly charge of \$6.41.³⁸

2. Positions of the Parties

a. The Company

In response to the Attorney General's request for an increase in the Lifeline discount, NET argues that the evidence in this case shows that such an increase is unwarranted at this time (Company Reply Brief at 21). The Company asserts that its

³⁷ Only four percent of Lifeline participants in Massachusetts currently subscribe to measured service (5,628 Lifeline measured service customers divided by 151,799 Lifeline participants) (Exh. AG-75; Exh. NET-5, Tracking Reports at 34).

³⁸ For Lifeline participants subscribing to measured service, the increase in the residence dial-tone line rate approved in this filing represents a 64 percent increase in the monthly charge (increase of \$2.49 divided by current Lifeline rate of \$3.92). We note, however, that approximately two-thirds of Lifeline participants subscribe to local unlimited service (Tr. 4, at 34), and the average increase for these Lifeline customers will be only 17 percent (average increase of \$1.96 divided by average current Lifeline rate of \$11.39).

Lifeline program is consistent with FCC requirements (id. at 22). In addition, the Company contends that the present discount adequately promotes the Department's goal of universal service by providing eligible residence customers with an affordable means of access to telephone service (id.).

The Company claims that it maintains one of the highest telephone penetration rates among LECs nationwide since the introduction of the Lifeline program in 1990 (id.). NET points out that the Massachusetts penetration rate in 1992 was 96.8 percent, which represented an increase from the 1991 penetration rate of 96.4 percent (id. at 23). The Company argues that this high penetration rate is evidence that universal service currently exists in Massachusetts, and that the Attorney General's suggestion for increasing the discount to further promote universal service is, therefore, unnecessary (id. at 22-23).

The Company also asserts that the method proposed by the Attorney General for increasing the Lifeline discount is unjustified (id. at 23). The Company contends that allocating the cost of the Lifeline discount across all rate classes contradicts the terms of the Stipulation (id.). NET notes that the Stipulation provides that an increase in the monthly Lifeline discount must be offset by increases in the residential dial-tone line rate (id. at 24).

In response to the Attorney General's recommendation that the Department adopt a percentage discount factor, similar to that used by the Department for subsidizing low-income customers of electric and gas utilities, to increase the level of the Lifeline discount, the Company argues that there is no record evidence to support adoption of a discount factor (id.).

b. The Attorney General

The Attorney General argues that the Lifeline discount should be increased by an amount equal to any approved increase in the rate for residence local unlimited service (Attorney General Brief at 5). The Attorney General asserts that the increased discount will reduce barriers faced by low-income telephone users in securing and maintaining access to the telephone network (id. at 7, citing D.P.U. 92-100, at 5).

The Attorney General maintains that the Department has ordered substantial subsidies for low-income customers of gas and electric companies and argues the Department's treatment of the Lifeline and Link-Up programs should mirror its practice toward these other utilities (id. at 7-8).

The Attorney General also contends that the cost of the Lifeline and Link-Up discounts should be allocated to all customer classes, excluding sufficiently competitive services, based on a rate base allocator (id. at 8). The Attorney General argues that the Lifeline program benefits all classes of

customers, and, therefore, all classes of customers should subsidize the cost of the program (id. at 6-7). The Attorney General claims that the Department has required this cost-recovery approach for subsidies of low-income gas and electric customers (id. at 7-8).

The Attorney General argues that the Company should continue its ongoing efforts to notify eligible customers of the Lifeline program (id. at 8).

3. Analysis and Findings

The Lifeline program in Massachusetts has been developed, in conjunction with the previously mentioned federal programs, to assure universal service in the Commonwealth, one of the Department's six rate structure goals for telecommunications.³⁹ See D.P.U. 89-300, at 11-12. In D.P.U. 89-300, the Department stated, "universal service means that the rate structure for telecommunications companies ensures rates that allow basic telecommunications services to be obtained by the vast majority of the state's population." Id. at 12. Because the transition to cost-based rates requires significant increases in traditionally underpriced residence exchange rates, the Department has carefully monitored the effects of the transition to ensure that it does not negatively impact universal service.

³⁹ We note that to date the Department has not expanded the Lifeline program beyond the initial federal requirements for state participation.

However, we cannot just assume, prima facie, as the Attorney General does, that increases in exchange rates necessarily make telephone service unaffordable for low-income customers.

The primary intent of the rate-restructuring is to remove the subsidies inherent in the pricing of NET's services that prevent the full benefits of the increasingly competitive telecommunications marketplace from reaching all customers. Therefore, in order for any subsidy to be increased in the transitional process, we would have to be reasonably certain that increasing the subsidy is absolutely necessary to preserve our rate structure goals. ⁴⁰

The Attorney General has offered no evidence indicating that telephone service is not affordable at the rates proposed by the Company, coupled with the Lifeline discount. According to the Company, since the introduction of the Lifeline program, NET has achieved one of the highest telephone penetration rates for LECs nationwide. We also note that there has been no statistically significant change in the Massachusetts telephone service penetration rate in the years 1989 to 1992 (see Section I.C, n.4). Thus, we find that through 1992 the transition to cost-based rates has not negatively impacted

⁴⁰ We note that because this is a revenue-neutral filing in a process that seeks to equalize rates of return among customer classes, any increase in the Lifeline discount must be paid for by additional increases in the residence dial-tone line rate.

universal service, and that the current proposed increase is unlikely to have an adverse impact on universal service.⁴¹

Therefore, we find that there is no basis for modifying the Lifeline program in this filing, and that it would be premature for the Department to order such a change, particularly when increasing the subsidy runs counter to our objective of reducing the subsidies in NET's rates.

Additionally, even if the Department had concluded that an increase in the residence exchange rate raised universal service concerns at this time, we are not persuaded that increased support through the existing subsidy scheme would necessarily be the best possible way of solving the problem. The same competitive forces that are the reason for the Department's overall rate restructuring policies will tend to undermine the existing universal service support mechanism as well.⁴² Alternative means of raising the necessary funds to maintain universal service have therefore become more urgent as local competition increases in Massachusetts.

⁴¹ It is also worth reiterating that the lower toll rates that will result from this Order will benefit those low-income customers who make toll calls, and thereby reduce the impact of the increase in exchange rates on their bills.

⁴² The Department does not believe the treatment of low-income discount programs of telecommunications companies need be consistent with that of other utilities, as suggested by the Attorney General, because market development and the level of competition in the telecommunications industry is different from that in the electric and gas industries.

New approaches to paying for universal service that are more consistent with competition have been suggested and are receiving initial consideration in some other states. The Department intends to explore these alternative approaches in the near future in conjunction with its continuing oversight of competitive developments in the Commonwealth. It may be that a more efficient universal service funding mechanism can be devised that is more consistent with competitive forces. We expect to explore this issue in greater depth in the near future.

However, as we approach the target residence dial-tone line rate of \$15.00 per month, it is necessary that the record in the two subsequent transitional filings contain more specific evidence regarding the impact of the transitional process on universal service and the affordability of telephone service for low-income customers. Therefore, the Company is hereby directed to review its Lifeline program, and to report the results of the analysis, as described below, and propose any modifications in or before its next transitional filing. If we determine as a result of this information that adverse effects on universal service or other undesirable outcomes are likely to occur as a result of further increases in residence exchange rates, the Department will consider whatever adjustments are necessary to solve the problem.

In its review of the Lifeline program, the Company shall

review and report on the following issues: (1) telephone penetration rates among low-income residents in Massachusetts; (2) usage characteristics of current Lifeline participants; (3) expected affordability of phone service for low-income customers at target rates; (4) Lifeline programs or other universal service funding mechanisms in other states; and (5) telephone penetration rates among low-income residents in other states.

B. LATA-wide Unlimited Calling Plan

1. Introduction

In D.P.U. 92-100, the Department directed the Company to develop a new residential premium service that would provide for unlimited calling within a LATA with no time-of-day or call duration restrictions. Id. at 20. In that Order, the Department stated that "the price for [the] service shall be a flat monthly rate", and "[t]he proposed rates for [the] service shall be cost-based and such rates shall be consistent with the Department's approved methodology for premium target rates set in D.P.U. 89-300." Id.

2. Company Proposal

In the instant filing, NET proposed to introduce a LATA-wide unlimited calling plan for the Western LATA only (Exh. NET-1, at 7-8). According to the Company, it did not propose a plan for the Eastern LATA because it does not have

experience with unlimited LATA-wide calling plans and can only estimate the use characteristics of potential customers (id. at 9). The Company stated that "the history established by introducing significant change first in the Western LATA, and thereby creating a laboratory, has been useful and should be applied again for this new offering" (id. at 8).

According to the Company, based on June, 1992 calling data, 93 percent of the residential customers in the Western LATA averaged less than two hours of direct-dialed, intraLATA toll calls per month (Exh. NET-1, Att. C at 30). Only seven percent of the residential customers in the Western LATA averaged more than two hours of direct-dialed, intraLATA toll calls per month (id.). NET indicated that its proposed LATA-wide calling plan is designed for customers who average more than two hours of toll usage within the Western LATA because customers who average less than two hours of usage currently have more economic alternatives available to them, such as residence direct-dialed toll service or the two-hour LATA-wide calling option (Exh. NET-1, at 8). The Company estimates that approximately 50 percent of the customers who average over two hours of toll usage will select the proposed unlimited LATA-wide calling plan (id.). The proposed rate of \$29.80 per month includes the dial-tone line rate of \$9.91, plus the local usage component of \$6.94, plus the toll usage component of \$12.95 (id.).

3. Positions of the Parties

a. The Company

The Company argues that it needs to test the unlimited LATA-wide calling plan in the Western LATA first because usage rates in the Eastern LATA have not yet reached their target levels, and introduction of a LATA-wide calling plan in the Eastern LATA would thus create confusion among customers in the Eastern LATA (Company Brief at 37-38). In addition, the Company stated that it has no prior experience with an unlimited LATA-wide calling service, and the revenue impact of using estimated usage would be more severe for the Eastern LATA compared to that for the Western LATA (id.). NET maintains that its decision to test the plan in the Western LATA is consistent with the practice established for the transitional process regarding target rate structure and rate design (id. at 38). The Company contends that because no party has directly objected to the Company's proposal and because it is in compliance with the Department's directives in D.P.U. 92-100, the Department should approve NET's proposal to introduce an unlimited LATA-wide calling plan in the Western LATA (id. at 41).

b. MCI

MCI maintains that the proposed LATA-wide calling plan is "anticompetitive, is contrary to the Department's long-held rate design goals of economic efficiency and fairness, and is not

necessary" (MCI Brief at 2). Therefore, MCI claims the plan should be rejected by the Department (id.). MCI argues that the plan is anticompetitive because it bundles monopoly services, such as dial-tone and unlimited local usage, with services subject to competition, such as intraLATA toll (id.). Moreover, MCI contends that since the Department has consistently maintained a rate differential of \$0.008 per minute between NET's toll and access services, the proposed unlimited LATA-wide calling plan violates that rate relationship, because some customers who subscribe to the service would have "an effective price that is less than the price of access" (id. at 3). In addition, MCI asserts that the proposed plan is not consistent with the Department's goals of economic efficiency and fairness, because some customers with greater than average usage would be paying less than the cost of the service while other customers with less than average usage would be subsidizing those customers with greater than average usage (id. at 4-5). MCI also claims that NET has not shown that there is a market for the plan (id. at 6).

According to MCI, the fact that the Department required NET to introduce this plan should not be dispositive of the issue since the Department did not have evidence on the record in D.P.U. 92-100 sufficient to approve a LATA-wide calling plan, and MCI did not have the opportunity to comment on the issue in that

proceeding (MCI Reply Brief at 2).

c. Mr. Ziegler

Mr. Ziegler contends that competition is fostering the introduction of various low-cost monthly calling plans, such as NET's proposed LATA-wide calling plan (Ziegler Brief at 1). Mr. Ziegler maintains that a similar calling plan should be introduced in the Eastern LATA (id.).

4. Analysis and Findings

Based on the record in this case, we approve as filed NET's proposal to introduce a residence unlimited LATA-wide calling plan in the Western LATA. We are not persuaded by MCI's arguments that NET has not identified a market for the service and that the proposed plan is not consistent with the Department's goals of economic efficiency and fairness. In D.P.U. 92-100, the Department stated that the Company "may propose additional service options for customers if a market for such services is identified, and as long as the rates for any such services are cost-based." Id. at 20. The record indicates that NET has identified a market for the plan (i.e., residential customers in the Western LATA with greater than two hours of intraLATA toll usage). Moreover, NET's proposed rate for the plan is consistent with the Department's directive in D.P.U. 92-100 requiring that such rates be consistent with the Department's approved methodology for premium target rates set in

D.P.U. 89-300. Notwithstanding this finding, we note that the Company failed to comply fully with the Department's directive in D.P.U. 92-100, by initially limiting its unlimited calling plan to the Western LATA. Therefore, we direct NET to propose an unlimited calling plan in the Eastern LATA in its next transitional filing.

C. Removal of Exchange and Access Tariff Prohibitions

1. Company Proposal

NET proposed to modify its Tariff No. 15 ("access tariff") to allow large customers to subscribe to most features and functions available only in the access tariff (Exh. NET-1, at 20).⁴³ The Company also proposed to: (1) continue the requirement that Feature Group A be available from an IXC's Point of Presence; (2) introduce a \$600 minimum monthly charge per location, per Feature Group; (3) provide automatic number identification ("ANI") only to IXCs and cable television providers; (4) allow only IXCs to subscribe to access tariff DA service; and (5) allow IXCs to subscribe to most services in the exchange tariff (id. at 21-24). In addition, the resale of unlimited business exchange service, unlimited Flexpath, and unlimited Centrex service would be available only to non-carriers (id. at 24).

⁴³ Currently, only carriers can purchase services from NET's access tariff and are prohibited from taking services under the Company's "exchange tariff," D.P.U. Mass. No. 10.

2. Positions of the Parties

a. The Company

NET maintains that its proposal to remove tariff restrictions prohibiting end-users from subscribing to its access tariff and carriers from subscribing to its exchange tariff complies with the Department's directive in D.P.U. 89-300 (Company Brief at 53). NET argues that in the past it did not open the access tariff to end-users and the exchange tariff to carriers because of concerns about "tariff shopping" and administrative costs to the Company (id. at 54, citing Exh. NET-1, at 21). The Company claims that removing tariff restrictions is appropriate at this time because rates in both tariffs are close to their respective target rate levels (id. at 53-54). Moreover, NET claims that removing the restrictions is consistent with the Department's goals of economic efficiency, fairness, and rate continuity (Company Reply Brief at 5).

3. Analysis and Findings

As part of its filing in D.P.U 89-300, NET proposed for the first time to allow end-users to purchase intrastate switched access services. Id. at 220. However, in D.P.U. 89-300, the Department rejected NET's proposed changes because the Company proposed to price end-user switched access services differently from carrier switched access services. Id. at 222-223. In that case, the Department stated that "the Company's failure to

support its assumptions about the cost differences between carrier and end-user switched access leads the Department to reject the proposition that switched access rates should vary between the two customer groups." Id. at 223.

We find that NET's proposed changes satisfy the Department's concerns raised in D.P.U. 89-300. Except for certain reasonable limitations imposed for the purchase of access services, as described above, end-users would be able to subscribe to switched access services at the same terms and conditions as carriers. We also find that the Company's proposed restrictions for end-users subscribing to switched access services and carriers subscribing to exchange services are reasonable. Accordingly, the Department finds that the Company's proposed changes to the access and exchange tariffs are reasonable.

D. Percent of Interstate Usage

1. Company Proposal

NET proposed to introduce requirements that IXC's report their Percent of Interstate Usage ("PIU") for originating 700 access service, and modify the audit provisions of the access tariff by indicating that a maximum of 12-months back-billing (or credit) would result for audit findings and that customers would be liable for the audit costs if the audit showed a five percent or more discrepancy from reported use (Exh. NET-1, Att. A at 14).

The Company indicated that the PIU modifications would not involve any changes in NET's rates for access services (Exh. NET-1, at 23).

2. Positions of the Parties

a. The Company

NET argues that the proposed PIU changes for 700 access service and the associated changes in audit provisions are consistent with the present usage reporting requirements for IXC's for other access services, such as 800 and 900 access services (Company Reply Brief at 25-26). The Company contends that the proposed 700 access reporting changes also are consistent with the Department's telecommunications goals (id. at 26).

b. MCI

MCI maintains that the Company's proposed PIU changes have not yet been implemented in NET's other jurisdictions (MCI Brief at 7). In addition, MCI claims that at present NET's 700 access service traffic is insignificant, accounting for only about one-tenth of one percent of all access minutes originating in Massachusetts during 1992 (id. at 8). Therefore, MCI recommends that the Department deny the proposed changes "until a need arises to justify the cost of additional reporting requirements" (id.).

3. Analysis and Findings

Based on the record, we find the Company's proposal to implement originating intrastate 700 access service reporting requirements to be reasonable because the proposed change would make 700 access reporting requirements consistent with the reporting requirements already in effect for 800 and 900 access services. Accordingly, the Department approves the proposed changes as filed.

E. Cellular and Paging Services

1. Introduction

Radio common carriers ("RCCs") (i.e., cellular and paging companies) must use NET's network facilities to transport traffic between wireless customers and telephone users on NET's network. Currently, the interconnection arrangements between NET and RCCs are provided under contract, with rates and charges the product of negotiation between NET and the RCCs (Exhs. NET-1, at 27; DPU-3). The four types of interconnection arrangements that NET presently provides to RCCs are:

- Type 1 interconnection, which can be either an analog or digital connection, provides a trunkside connection between a cellular carrier's switch and a NET central office. When Type 1 is provided using an analog connection, the service is provided using a trunk equipped with DID service. When provided as a digital connection, Type 1 uses NET's Flexpath Service. Type 1 interconnection can be used for either incoming (landline-to-mobile) or outgoing (mobile-to-landline) calls (Exh. DPU-1).

- Type 2A interconnection is a trunkside connection between a cellular carrier's switch and the Company's tandem switching system. Type 2A is provided as a two-way service, similar to Type 1 (id.).
- Type 3B interconnection, typically used by paging companies, is an analog connection similar to Type 1 (i.e., a trunk equipped with DID). This type of connection is restricted to incoming calls only. Flexpath Service is used when Type 3B is provided as a digital service (id.).
- Type 3A, also used by paging companies as an incoming-only service, is provided as a trunkside connection directly to an NET end office (id.).

2. Company Proposal

NET proposed to offer RCCs interconnection to its network under the applicable tariff terms and conditions for DID, Flexpath and/or switched access services (Exh. NET-1, at 27-29).⁴⁴ NET stated that RCC interconnection services are provided over the same type of facilities as exchange and access services (id.).

3. Positions of the Parties

a. The Company

The Company maintains that the features and functions of the services, traditionally offered under contract to cellular and paging companies, are comparable to switched access, Flexpath and DID services (Company Brief at 59). The Company contends

⁴⁴ See Section II.C.3, Digital Private Line Services, supra regarding the pricing of Flexpath Service, Section II.C.1, regarding DID, and Section II.C.6, regarding switched access services.

that tariffing also is necessary since the distinctions among customers (i.e., cellular, paging, IXC's) have become blurred, making it impractical to treat these services differently, and to segment the market by tariff or contract (id. at 59-60). NET maintains that its proposal is consistent with the Department's goals in that it enables the Company to charge all telecommunications providers for the same interconnection services at the same tariffed rates (Company Reply Brief at 5).

b. Telmarc

Telmarc contends that NET's proposed tariffed rates constitute a substantial reduction from the rates currently provided by contract to RCCs; therefore, Telmarc states that it does not object to approval of this change at this time (Telmarc Brief at 1).

4. Analysis and Findings

The Department finds that the Company's proposal to charge RCCs switched access and Flexpath/DID tariffed service rates in lieu of contract interconnection prices is consistent with the Department's goals of economic efficiency, fairness, and simplicity. We find that NET's proposal to make all terms, rates, and conditions of interconnection to the Company's network the same for cellular and paging companies will ensure fair and impartial treatment to all RCCs. ⁴⁵ Based on these findings, we

(continued...)

approve the Company's proposal as filed.

F. Classification of Monopoly and Competitive Services

1. Introduction

In D.P.U. 92-100, the Department directed NET to classify its services as either monopoly or competitive, and then as either basic or auxiliary. Id. at 63. Consequently, a particular service may fall into one of four classifications: basic monopoly; basic competitive; auxiliary monopoly; or auxiliary competitive. Id. at 58.

Monopoly services are those which only can be provided by NET, at least for the foreseeable future, whereas competitive service may be provided by alternate means. Id. at 59. Basic services include network components, such as access, switching, and transport. Id. Auxiliary services are not necessary to transmit information between points in the network but still

⁴⁵(...continued)

⁴⁵ The federal Omnibus Budget Act of 1993 contained, among other things, provisions for the preemption of state regulation of rates and market entry of commercial mobile services. We note that, as a result of that Act, the FCC is proposing to create a new regulatory framework for all mobile services. See Implementation of Sections 3(n) and 332 of the Communications Act/Regulatory Treatment of Mobile Services, GN Docket No. 93-252, Notice of Proposed Rulemaking, FCC 93-454 (released October 8, 1993). The FCC has tentatively concluded that for commercial mobile services, LEC provision of interconnection and the type of interconnection provided by the LEC are inseverable. Therefore, the FCC is proposing to preempt state regulation of the right to interconnect and the type of interconnection for intrastate services. However, the FCC does not propose to preempt state regulation of the rates for interconnection.

provide benefit. Id. at 61.

The Department also directed the Company to propose a target rate for any service that is classified as basic monopoly. Id. at 63-64.

2. Company Proposal

The Company submitted a classification of its services as monopoly or competitive, and basic or auxiliary (Exh. NET-1, at 44; Att. H). The Company stated that it used prior Department decisions as a guideline for classifying its services (Exh. NET-1, at 45-46). The Company also indicated that it viewed the classification of services as a starting point primarily to provide guidance in the pricing of new services, and that the proposed classifications were not intended as a permanent classification (id. at 47).

3. Positions of the Parties

a. The Company

The Company argues that the classification scheme is intended only to serve as a guideline for discussion (Company Reply Brief at 17-18). According to NET, the proposed classifications reflect a current assessment of the Company's services based on the Department's definitions of service classifications and market factors (id. at 18).

NET argues that as various market factors evolve, service classifications will need to be changed (id.). The Company

states that its classification is presented only as an illustration of service classifications at a particular point in time (id. at 18 n.19). Therefore, the Company believes its classifications are reasonable at this time and expects that the classifications will need to be changed over time (id.).

In response to the Attorney General's allegation that the Company has failed to meet its burden of proof in demonstrating a service as competitive, the Company states that it is not proposing to reclassify any of its services as "sufficiently competitive" for rate class purposes (id. at 17-18).

b. The Attorney General

The Attorney General argues that the Company has failed to meet its burden of proof in classifying its services as monopoly or competitive (Attorney General Brief at 39). The Attorney General asserts that the Company must submit detailed cost information for a service to be classified as sufficiently competitive (id. at 41, citing IntraLATA Competition at 38). The Attorney General asserts that the Company has failed to provide the necessary information to review whether the services listed as either basic or auxiliary competitive meet the criteria for classification (id.).

The Attorney General argues that only two services, Centrex and Intellidial, should remain classified as competitive (id.

at 42)).⁴⁶ The Attorney General argues that NET's services should be classified as monopoly until the Company can provide the required supporting documentation to prove that any services other than Centrex and Intellidial are sufficiently competitive (id.).

In addition, the Attorney General recommends that the Department periodically review the costs for sufficiently competitive services to ensure that ratepayers do not subsidize these services in the future (id. at 43). The Attorney General asserts the cost information for Centrex and Intellidial are outdated, and the Company should be required to provide updated information showing that the current rates cover the cost to provide the service (id. at 43).

4. Analysis and Findings

We find that NET's classification of services in this filing is in compliance with the Department's directives in D.P.U. 92-100. Id. at 63-64. In that case, the Department directed the Company to classify its services as monopoly or competitive, and basic or auxiliary, for two reasons: (1) to serve as a guide for the pricing of new services; and (2) to ensure that all basic monopoly services have cost-based target

⁴⁶ The Department has previously declared Centrex and Intellidial to be sufficiently competitive for rate class purposes. See NET-Centrex, D.P.U. 85-275/276/277 (1985); NET-Intellidial, D.P.U. 88-18-A (1988).

rates. Id. at 58-64. Therefore, the Department does not consider NET's classification of some services as competitive to be a rate group classification for determining the proper degree and form of regulation.

In response to the Attorney General's recommendation that the Department should review the costs and rates of NET's Centrex and Intellidial services, we note that there is no evidence on record indicating that NET's rates for these competitive services are not fair and reasonable. The Department has established a mechanism for regulating the rates of sufficiently competitive services (see IntraLATA Competition at 39), ⁴⁷ and we have seen no evidence indicating that NET is unfairly competing in pricing its Centrex and Intellidial services. Therefore, we do not recognize a need to alter our current regulation of NET's sufficiently competitive services.

V. COMPLIANCE FILING AND TRANSITIONAL FILINGS

A. Compliance Filing

When NET filed its proposed tariffs on June 14, 1993, the Company requested that the rate changes be implemented no earlier than April 14, 1994. We find that this date will allow for adequate customer notification regarding the rate levels and

⁴⁷ In IntraLATA Competition, the Department stated that if an entire service class is determined to be sufficiently competitive, it may find that prices set by the market are fair and reasonable. Id. at 39.

structural changes ordered by the Department. Therefore, NET shall file all rates and charges required by this Order for effect April 14, 1994, in a compliance tariff to be filed no later than fourteen days from the date of this Order.

Because of the complexity of the changes, and the number of customers potentially affected, adequate customer notice is important. Customer notification must, among other things, include the following information: (1) the increase to the residence dial-tone line rate; (2) the decreases in the residence and business MTS rates; (3) the decrease to the business local message rate; (4) increases in premium service rates; and (5) the availability of a LATA-wide calling plan for Western LATA customers. This information shall be distributed to customers in the form of a bill insert to be reviewed by the Department. Since extensive information is provided in the white pages of its telephone directories, NET shall submit to the Department for review and approval the sections of those directories pertinent to any rate changes ordered herein. In addition, the Company shall submit to the Department for approval its schedule for printing and distributing its directories.

B. Transitional Filings

As indicated in Section I.C, supra, the Department remains fully committed to the rate structure goals and cost methodologies that formed the basis of the Department's decision

in D.P.U. 89-300, D.P.U. 91-30, and D.P.U. 92-100. In addition, we remain committed to the timetable established in D.P.U. 92-100 for completion of the transitional process in two additional filings. Thus, in its 1994 and 1995 filings, NET shall continue to file revenue-neutral tariffs that move rates toward target levels. As required by the Department for this proceeding, the Company in its 1994 filing again must submit full supporting documentation for its proposed rate changes. See D.P.U. 89-300, at 50, 433-440; D.P.U. 91-30, at 95; D.P.U. 92-100, at 80. In addition, we also direct the Company to include in the next filing a summary chart of present, proposed, and target rates for any rate that the Company proposes to modify in the filing.

We note that even though we continue to require the Company to file COSS and MCS as supporting documentation for its proposed rate changes, the sufficiency of the Company's cost methodologies has been consistently upheld for purposes of these transitional filings.⁴⁸

⁴⁸ The Department hereby places parties on notice that it will not allow intervenors to address through extensive discovery, direct and/or cross-examination, and briefs the issue of NET's cost methodologies, except to the extent a party challenges NET's cost studies as not being in compliance with the methodologies established in prior Department Orders.

VI. ORDER

Accordingly, after due notice, hearing, and consideration,
it is

ORDERED: That the revisions to tariffs D.P.U. Mass.
Nos. 10 and 15, filed by New England Telephone and Telegraph
Company on June 14, 1993, are disallowed; and it is

FURTHER ORDERED: That New England Telephone and Telegraph
Company shall file a new schedule of rates and charges in
compliance with the directives contained in this Order for effect
April 14, 1994; and it is

FURTHER ORDERED: That New England Telephone and Telegraph
Company shall submit its compliance filing within fourteen days
of the date of this Order; and it is

FURTHER ORDERED: That with its compliance filing, New
England Telephone and Telegraph Company shall submit supporting
documentation demonstrating that such rates and charges comply
with this Order; and it is

FURTHER ORDERED: That New England Telephone and Telegraph
Company shall serve, by same or next-day delivery, a copy of the
Company's compliance filing on all parties and participants to
this case who request such copy within ten days of this Order,
and parties and participants shall have seven days from the date
of the filing to submit comments to the Department as to whether
the Company's filing complies with the Department's directives;

and it is

FURTHER ORDERED : That New England Telephone and Telegraph Company shall provide notice to its customers of these changes by means of a bill insert that shall have been first reviewed and approved by the Department's Telecommunications and Consumer Divisions. The Company shall include said bill insert with the first cycle of the Company's bills that incorporate the rates authorized by this Order.

FURTHER ORDERED : That New England Telephone and Telegraph Company shall comply with all other directives contained in this Order.

By Order of the Department,

VII. CONCURRING OPINION OF COMMISSIONER BARBARA KATES-GARNICK

In its Order, the Department granted the Company's request for a 64 percent increase in the charge for residential dial-tone line service for some Lifeline customers. By implementing this additional charge without a corresponding, or any, adjustment in the Lifeline discount, my fellow Commissioners fail to consider fully the financial burden upon Lifeline customers who are least able to pay. I would allocate the slight additional expense equitably upon those residential customers more able to pay.

This issue creates a dilemma for me. I am supportive of the broad goals of the transition towards cost-based rates, which has been underway since 1989, and the movement towards equalized rates of return among customer classes. I also recognize that over time competition promotes efficiency and choice, both positive outcomes for consumers. However, underlying the concept of the transition itself is the notion that implementation of equalized rates of return must take place gradually so that customers do not experience rate shock and the goal of universal service remains intact.

Regulators should not make decisions based only on economic textbooks. Our policies must be sensitive to the impact of actions upon all ratepayers. In the march towards competition, my fellow commissioners, by failing in this case to take any real action to moderate the rate impact upon a particular segment of

low-income customers, have made a rather harsh social calculation. Although options in this case are limited, I advocate mitigating the economic hardship placed upon Lifeline customers without unduly burdening the rest of the residential class.¹

This Order increases the rates for some Lifeline participants to \$29.88 a year or by 64 percent. Whether one views this increase in either percentage or dollar terms, I submit that the result is a financial burden that could have been alleviated merely by adjusting the dial-tone rate for other residential customers. The result would be an additional \$1.56 per year for approximately 2.3 million lines.² Although adding

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- 1 Although the Attorney General argues that the Department should require NET to spread the increase among all rate classes (Attorney General Brief at 7), this argument is somewhat compromised by the Stipulation signed between the Attorney General and the Company, which provides that an expansion of Lifeline and Link-Up ought to be offset by an increase in residential dial-tone rates (Stipulation at 8).
- 2 The record in this case indicates that there are 151,799 Lifeline customers in Massachusetts (Exh. NET-5, Tracking Reports at 34). Therefore, increasing the Lifeline monthly discount by \$2.00 (i.e., enough to cover the average monthly increase in the residence local unlimited rate) will represent an additional monthly cost for Lifeline of \$303,598 ($\$2.00 \times 151,799$). Not including the Lifeline participants, there are 2,336,518 residence lines subject to such an increase ($2,488,317 - 151,799$) (Exh. NET-1, Att. G at 1). Dividing the additional monthly cost by the number of residence lines subject to the increase yields an additional increase per residence line of \$0.13 a month (continued...)

an additional amount to the telephone bills of residential ratepayers is certainly not an appealing situation, it eases the burden placed on customers who participate in this joint federal/state program. Therefore, with a slight additional charge on all members of a rate class, the poorest do not shoulder an unreasonable burden.

Because of the uncertainty about the impact of their approach on telephone penetration rates, my colleagues have ordered an extensive review of the Lifeline program. In my view, this could prove to be an expensive study of dubious value. As I have stated, my approach would be act now to mitigate the impact.

As we move into a more competitive world, whether in telecommunications or in energy, the Department must balance the interests of all consumers. In this decision, my colleagues have moved too far in one direction.

Respectfully,

Barbara Kates-Garnick
Commissioner

(...continued)

(\$303,598/2,336,518), or \$1.56 a year.