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October 30, 2008

Catrice C. Williams, Secretary
Department of Telecommunications and Cable
One South Station, Fourth Floor
Boston, MA 02110

Re: D.T.C. 07-9, Petition for Investigation under Chapter 159, Section 14 of the Intrastate Access Rates of Competitive Local Exchange Carriers
Initial Brief of the Attorney General

Dear Ms. Williams:

The Attorney General submits this letter as her Initial Brief in the above-captioned proceeding. If current switched access rates are in excess of the range of reasonable rates that could be charged for such services, those rates are unreasonable and must be revised. The Attorney General submits these comments to highlight certain issues that must be addressed in order to reach such a conclusion. The Attorney General expresses no view in this letter as to whether the Verizon has met its burden of proof, but reserves the right to respond in a Reply Brief.

The Department of Telecommunications and Cable ("Department") conducted an evidentiary hearing between September 23 through September 25, 2008 upon Verizon's complaint that intrastate switched access rates of competitive local exchange carriers ("CLECs") providing service in Massachusetts are unreasonable where the CLECs' rate structures yield revenues in excess of Verizon's revenues on an access revenue per minute ("ARPM") basis.

Under G.L. c. 159, the Department is responsible for ensuring "just and reasonable" rates. Section 14 requires that when the Department finds any rate of a common carrier to be "unjust, unreasonable, unjustly discriminatory, unduly preferential," in violation of law, or insufficient to yield reasonable compensation, "the department shall determine the just and reasonable rates" to be charged. The Department has determined that "rates charged by non-dominant carriers for all services and by dominant carriers for sufficiently competitive services are presumed to be just and reasonable due to the disciplining effects of competitive forces."[1]

[1] *Investigation by the Department of Telecommunications and Energy on its own Motion into the Appropriate Regulatory Plan to succeed Price Cap Regulation for Verizon New England, Inc. d/b/a Verizon Massachusetts' intrastate retail telecommunications services in the Commonwealth of Massachusetts*, D.T.E. 01-31 Phase I at 19 (2002), *citing IntraLATA Competition Order*, D.P.U. 1731, at 64–70 (1985).

In order for the Department to reach a conclusion that CLEC switched access rates are unjust and unreasonable, it must first determine that competitive pressures will not drive switched access charges toward their marginal costs in the long run.[2] The CLECs argue that a combination of indirect regulatory pressure through "moral suasion"[3] and the threat of competitive entry when a CLEC obtains excess profits from access charges,[4] will constrain CLEC rates. The CLECs' witness, however, admits that this competitive pressure is not sufficient to drive switched access rates down to marginal costs in the long run.[5]

This does not end the inquiry, because even if market competition does not serve as an adequate proxy for direct regulation of switched access charges, it must determine whether the CLECs' filed rates are unreasonable. The Department has long held that a primary ratemaking goal is economic efficiency, meaning that rates should be cost-based.[6] The basis of Verizon's complaint is essentially that CLECs are charging rates that are several multiples of Verizon's rates, which the Department has determined to be just and reasonable. Establishing Verizon's rate as a just and reasonable benchmark, however, is a different regulatory exercise from determining whether existing filed rates are unjust and unreasonable. In this proceeding, no cost data were submitted that establishes whether CLEC rates are beyond the zone of reasonableness. Further, it is not clear whether Verizon's rate is an appropriate benchmark, given that the cost of providing switched access services may be significantly lower.[7] Before setting Verizon's rate as the benchmark, it would be appropriate to update the appropriate cost studies.

Finally, the Department cannot determine whether modifying switched access rates will result in just and reasonable rates without reviewing the impact on end users. Although several witnesses testified that if markets are competitive, then a reduction in production costs resulting from reduced access rates will result in reductions in retail rates in the long run, the increase in consumer surplus that would result from capping access rates was not quantified; nor was it shown when consumers would benefit. The Attorney General recognizes that it would be difficult to administer a pass-through of savings to end users. However, should the Department grant Verizon's petition, the Department should ensure that end users within Massachusetts benefit from this regulatory action.

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[2] *See Intra-LATA Competition*, D.P.U. 1731 at 25 (1985).
[3] Tr. at 568.
[4] *See* Tr. at 495–496.
[5] Tr. at 569.
[6] D.P.U. 1731 at 19–20.
[7] Tr. at 398–399.

In conclusion, the Attorney General has long supported the existing regulatory scheme, which allows the Department to rely upon market forces when they are more effective than direct regulation in driving rates to marginal cost. Verizon has identified a market failure where direct regulation may be required. However, in order to implement the relief requested, further actions may be necessary, including, conducting an investigation into whether Verizon's current intrastate switched access rates remain cost-based; monitoring and reporting on the current state of competition in Massachusetts to demonstrate whether regulatory actions that affect production costs do translate into retail rate reductions rather than shareholder gains; and ensuring that end users will benefit from the proposed regulatory actions.

Respectfully submitted,

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By: /s/

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COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND CABLE

D.T.C. 07-9

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all parties of record in this proceeding in accordance with the requirements of 220 C.M.R. 1.05(1) (Department's Rules of Practice and Procedure).

Dated at Boston, Massachusetts this 30th day of October, 2008.

/s/

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