

Approved: 3-6-96
Date

MINUTES OF THE HOUSE SELECT COMMITTEE ON TELECOMMUNICATIONS.

The meeting was called to order by Chairperson Doug Lawrence at 1:35 p.m. on February 5, 1996 in Room 313-S of the Capitol.

All members were present except: Greg Packer - excused

Committee staff present: Lynne Holt, Legislative Research Department
Mary Ann Graham, Committee Secretary

Conferees appearing before the committee: David Brevitz, Consultant - Kansas Corporation Commission

Others attending: See attached list

Chairman Doug Lawrence called the meeting to order at 1:35 p.m. He announced that he has been considering the possibility of seating two people from the telecommunications industry at the table for the committee to ask questions for the purpose of exploring some of the technical issues. At the adjournment of the meeting he will visit with members of the industry for their view point and suggestions. He also reminded members in the industry of their assignment of selecting issues from the Kansas Corporation Commission competition docket and the Telecommunications Strategic Planning Committee report for a matrix request, to have that in by Friday, February 9, 1996.

Chairman Doug Lawrence had a bill request which would provide uniform property tax rates for all telecommunication providers. Rep. Carl Holmes made a motion it be passed, Rep. Carl Beggs, seconded, motion passed.

The Chairman asked the committee to bring a list of questions to the meeting that they would like to have addressed. He is planning to have a question and answer day by the committee and conferees that have been attending the telecommunication meetings.

The Chair introduced David Brevitz, Consultant for the Kansas Corporation Commission. Mr. Brevitz discussed resale and unbundling matters. With the passage of the Congressional telecommunications bill he briefly digressed to the topic of federal preemption in telecommunications. (See Attachment 1)

Chairman Lawrence reminded the committee of the tour scheduled for Thursday, February 8, 1996, of Sprint in Johnson county, of their long distance network facilities and also of TCI of Kansas Cablevision facilities. A reminder that **HCR 5036**, a Concurrent Resolution urging adoption of the telecommunications vision statement developed by the telecommunications strategic planning committee, will be heard Wednesday, February 7, 1996.

The meeting adjourned at 2:15 p.m.

The next meeting is scheduled for February 6, 1996

SELECT COMM. ON TELECOMMUNICATIONS
COMMITTEE GUEST LIST

DATE: 2-5-96

NAME	REPRESENTING
Glenda Cafar	KCC
Karen Marten Flaming	KCC
Nelson Krueger	Menninger
Bill Sneed	SW BELL
Pat Hubble	SW BELL
Barbara Paschka	Board of Regents
Lena Powers	MCI
Judi Neir	# Classic Communications
Mike Reecht	AT&T
Yonny Miles	KCC
M. Cummings	Classic Communications
Mike Meadham	Ks Cello Telecommunications Assn.
Ken Bahr	Comptel of Kansas
WALKER HENDRIX	CURB
Scott Richardson	SWBT
Tom Bruno	Allet Assoc.
John D. Pingan	SITA
JASON PITJENBERGER	BRAD SMOOT
Bill Drexel	SWBT

SELECT COMM. ON TELECOMMUNICATIONS
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DATE: 2-5-96

NAME	REPRESENTING
BILL RUBE	SWBT
Denny S. Koch	SW BELL TEL
George Barber	RTMC
Rob Hodges	KTA
JEFF FUSSELL	SPRINT
Miggen Griggs	KTA Keeney & Assoc.

SELECT COMMITTEE ON TELECOMMUNICATIONS

Testimony presented by David S. Brevitz, Consultant
Kansas Corporation Commission
February 5, 1996

Mr. Chairman, Members of the Committee:

I am here today to discuss resale and unbundling matters. But in light of the passage of the Congressional telecommunications bill last Thursday, I would like to immediately but briefly digress to the topic of federal preemption in telecommunications. We have had many opportunities since August of last year to address the likelihood of Congressional legislation, and each time we have been optimistic about the chances for passage, based on Washington contacts. It is something of a relief to see the bill finally passed, so there isn't a need for any more prognostications.

Like it or not, state authority over telecommunications has been significantly supplanted by the passage of the Telecommunications Act. The shortest, and ultimately least contentious and wasteful path for Kansas now is to move in concert with the provisions of the Telecommunications Act.

The Federal Communications Commission has for a long time been taking actions to promote competition, which either explicitly or implicitly preempt state action to the contrary. As such, the KCC has a great deal of experience and well-founded expectation as to how FCC actions to implement the bill will tend to limit state actions. With its own due process under the Communications Act, since the '70's the FCC has addressed the following matters and either directly preempted state authority or rejected state assertions of authority. These actions have been challenged by the states in court, and with one exception, the states lost.

Deregulation of Telephone Equipment
Deregulation of the provision of Inside Wiring
Non-Regulation of Enhanced Services
Preemption of state authority related to Separations methods and procedures
Preemption of state authority over depreciation rates (reversed in Court)
End-User Charge
Rate Regulation of Radio Common Carriers

I am not suggesting that the KCC opposed these FCC actions at the time, or that the KCC now thinks the direction was wrong--the point is these are areas where state authority was circumscribed by the FCC.

Back to resale and unbundling. As you know, the Commission was charged by SCR 1627 to "encourag(e) development of effective competition for telecommunications services where feasible, including the removal of existing barriers to entry", and to open a docket or dockets to investigate competition. In Phase I of its Competition proceeding, the Commission made findings on resale and unbundling.

Regarding resale, the Commission found that:

--current restrictions on resale and sharing of local service are barriers to maximizing the effectiveness of competition;

--LECs should be required to lift tariff restrictions on resale and sharing where appropriate; and,

--an industry task force should evaluate the restrictions and make recommendations to the Commission for determination in Phase II of the Docket.

The Commission did not decide in Phase I the extent to which resale and sharing barriers exist, and what should be done about them. This, along with the Task Force's identified issues, are left for Commission decision in Phase II.

Regarding Unbundling, the Commission found that non-discriminatory access to certain local service functions and facilities is to be made available at cost-based rates. Unbundling is separate pricing of network components, so that only necessary components may be purchased for use.

To illustrate by way of the most pertinent example, local telephone service today is composed of several network elements, such that it could be unbundled into the local loop, switching, and trunking between switches. There are those that advocate unbundling into much smaller components, as many as thirty or forty.

In its November 1995 cost study decision, the Commission required three components of cost study information that may have implications for unbundling: loop; switch; and trunking between switches.

The Commission has reserved to the Phase II hearings decisions on the extent of unbundling; the timing of unbundling; and pricing.

“Phase II” of the Competition docket was anticipated by the Commission to include the filing of testimony by all parties in the Spring, hearings in the Summer, and Commission decision in the Fall. A procedural order to this effect is being drafted. The scope of the order will now need to account for the passage of the Congressional legislation.

Since the details of resale and unbundling are before the Commission in Phase II, what follows should be taken as a staff perspective.

First, I would like to refer back to a couple things Joe Weber said on Wednesday. He said something to the effect that competition just from a bunch of resellers is not robust competition at all. We agree. If the net result of state policies is only the emergence of resellers, who do not build networks of their own, we don't have the type of competition that guarantees reasonable prices. That would have to be viewed as a policy failure.

We view resale as a transitional mechanism, designed to facilitate competitive entry, and competition. Resale lets a competitor begin marketing service to customers quickly, and further network construction will follow. Resale has worked before to promote the development of competition. Sprint and MCI both relied on resale of AT&T and other facilities to get started in the long distance business. There is no question that they now operate substantial networks of their own.

Competitors need resale as a way of immediately entering markets that require massive capital investment. There is no part of the telecommunications network that is more capital intensive than the local network. Earlier we provided an estimation that local loop plant, just the loop, for the largest company in Kansas is about \$1.3 Billion. Many competitors have a national perspective, and national financial requirements. They are able to choose which states to focus on, and will go to states where the rules are pro-competitive. If the competitor's choice is to spend \$1.3 Billion in Kansas to duplicate the network before competing, versus spending that same amount of money to enter some greater number of other states that allow resale, the choice is obvious--the competitor will move Kansas way down on the list, and focus on competing in other states first.

The capital intensity of the local network is recognized in the Congressional conference committee's report, where it states:

This conference agreement recognizes that it is unlikely that competitors will have a fully redundant network in place when they initially offer local service, because the investment necessary is so significant. Some facilities and capabilities will likely need to be obtained from the incumbent local exchange carrier as network elements pursuant to section 251.

It is for pro-competitive reasons that the Commission has an interest in potentially using resale to some degree to promote the development of competition and customer choice during this transitional stage. If the competitors do not move beyond the resale stage, which isn't at all expected, the Commission can take further steps at that time.

Furthermore, as the Committee has heard, stranded investment is a significant concern. This issue will no doubt be raised to the Commission in the Phase II hearings this summer. The use of resale should help to mitigate stranded investment. With resale, some loops will continue to generate resale revenue even though the customer is with another company.

Joe Weber also indicated to you that one of the key issues in resale is pricing. We agree. In New York, the discounted price to resellers is 95% of retail. In many other states, competitors argue that it should be 60%. What is the right resale price? This issue will be before the Commission in Phase II.

The TSPC report leaves to the telephone company the decision of whether or not to permit "resale" and "unbundling" of its facilities by a competitor to a customer. Resale and unbundling will have the effect of accelerating competitive choice, so it is not rational to expect the incumbent telephone company to voluntarily permit resale and unbundling. The KCC and the Congressional legislation require a reasonable level of resale, and non-discriminatory access to unbundled network elements to be provided.

It is something of a paradox that in fully competitive markets, resale restrictions are unenforceable, but we are debating the use of resale restrictions to supposedly get us to fully competitive markets. Resale restrictions are enforceable only if a) the company has enough market power that if it says "no resale", there will be none, or b) there is legal or regulatory prohibition of it. In competitive markets, resale is a non-issue.

Many other states are, or intend to use resale as a transitional tool to the development of local competition. For example, a recent comprehensive decision on competitive matters by the Washington Utilities and Transportation Commission (Docket UT-941464, November 1, 1995) includes the following:

the record supports the conclusion that retail competition through a strong resale market may indeed be an important step in the long term development of local competition.

USWC (US WEST, one of the regional Bell companies) shall allow resale of unbundled loop and other transport service, except that residential service may not be resold as business service and local call termination may not be used to deliver toll traffic.

Also, the Illinois Commerce Commission just a few weeks ago certificated a SWB subsidiary as a reseller in the Chicago metro area. SBMS Illinois received a certificate to provide and resell local exchange service. Initially, SBMS Illinois is expected to resell a number of services provided by the incumbents. SBMS will be the first to offer integrated cellular and land line service in competition with Ameritech, another of the regional Bell companies.

As food for thought then, perhaps the resale policy determination should be that resale restrictions in Kansas should be no greater than the least restrictive conditions pertaining in other states.

A related point is that the Bell Operating Companies, freed by Congressional legislation to enter the InterLATA long distance markets, will no doubt do so initially via resale to compete while they are constructing networks of their own.

The topic of unbundling is very closely related to the resale issue. The primary issues are a) the depth of unbundling--how many separate network components and functions should be unbundled; and b) pricing of the unbundled components. These issues are set for Commission decision in Phase II.

Again, many states are unbundling network components, or intend to. For example, please consider the following from the Washington Utilities and Transportation Commission order cited above:

Unbundling allows customers greater opportunity to choose between a diversity of products, services and companies. Unbundling also allows for efficient use of the public switched network, reduces the likelihood of inefficient network over-building, and ensures that competition is not held hostage by being bundled with bottleneck functions.

Allowing for the access to and resale of unbundled parts of the incumbent's network allows for those parts of the local exchange market that can support competition to move forward with competition without being held back by those parts of the market still characterized by monopoly.

At this time, the Commission is satisfied with a first level of unbundling that includes an unbundled loop and an efficient line side interconnection.

This case confirms the Commission's belief that incumbent LECs will see the benefit to unbundling, not only for advantages associated with freeing itself up to compete more effectively but also in maximizing the use of its network and the resulting revenues associated from that use.

In closing, it is clear to us that some reasonable level of resale and unbundling will be quite helpful in meeting the directive of SCR 1627 to promote the development of effective competition. The Commission is well able to decide based upon record evidence and hearing what is reasonable to implement that intent of SCR 1627.

Joe Weber said the Congressional Act will "preempt but not invalidate" their proposed framework on resale. Preemption is invalidation. We have enough experience at the KCC with the FCC's use of its preemptive powers to advise that this Committee be very cautious of doing anything that begs for preemption. Restricting resale and unbundling does so.