

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

<p>IN RE:</p> <p>POSSIBLE EXTENSION OF BOARD JURISDICTION OVER SINGLE LINE FLAT-RATED RESIDENTIAL AND BUSINESS RATES FOR LOCAL EXCHANGE CARRIERS</p>	<p>DOCKET NO. INU-08-1</p>
--	----------------------------

**FINAL ORDER**

(Issued June 27, 2008)

**BACKGROUND AND PROCEDURAL HISTORY**

On July 1, 2005, Iowa Code §§ 476.1D and 476.55 were amended. The amended statutes deregulated retail rates for most local exchange communications services in Iowa except for single line flat-rated residential and business rates. Rates for these services were initially set at the corresponding rates charged by each rate-regulated local exchange carrier (LEC) as of January 31, 2005. The amended statutes then allow for increases to those monthly rates of up to \$1 per year for residential service or \$2 per year for business service, plus inflation, up to specified caps, beginning on July 1, 2005, through June 30, 2008.

Effective July 1, 2008, the retail rate jurisdiction of the Utilities Board (Board) will no longer be applicable to single line flat-rated residential and business service rates unless the Board, during the first six calendar months of 2008, extends its retail rate jurisdiction. Pursuant to § 476.1D, the Board may extend its jurisdiction for not

more than two years and may do so only after the Board finds such action is necessary for the public interest.

On February 11, 2008, the Board issued an order to initiate this proceeding for the purpose of considering whether the Board should extend its jurisdiction over single line flat-rated residential and business local exchange service rates provided by certain telephone companies. A procedural schedule was established and pursuant to that schedule, initial statements of position by interested persons were filed with the Board on or before March 17, 2008, and counterstatements of position were filed on or before April 28, 2008.

Five participants filed written statements of position and four participants submitted counterstatements of position. Participants included Iowa Telecommunications Services, Inc., d/b/a Iowa Telecom (Iowa Telecom), Consumer Advocate Division of the Department of Justice (Consumer Advocate), Iowa Association of Municipal Utilities (IAMU), Frontier Communications of Iowa (Frontier), and Qwest Corporation (Qwest).

An oral presentation in this proceeding was held on May 21, 2008, for the purpose of cross-examining witnesses on their statements and counterstatements of position. Representatives from Iowa Telecom, Consumer Advocate, IAMU, Frontier, and Qwest participated in the oral presentation.

On May 30, 2008, briefs were filed by Iowa Telecom, Consumer Advocate, IAMU, Frontier, and Qwest.

## DISCUSSION

This proceeding is different from previous Board proceedings that considered whether to deregulate certain telecommunications services in specific exchanges.<sup>1</sup> In the previous deregulation proceedings, pursuant to Iowa Code § 476.1D, the Board had to determine whether a service was subject to effective competition before deregulating that service. When making that determination, the Board was charged with considering several market factors including, but not limited to, the following: (1) wireless services, (2) cable telephony services, (3) Voice over Internet Protocol (VoIP) services, and (4) economic barriers to the entry of competitors or potential competitors.

In this proceeding, however, the standard of effective competition is not directly applicable. Pursuant to Iowa Code § 476.1D(1)"c," the Board must determine whether the public interest requires extension of the Board's jurisdiction over single line flat-rated business and residential rates for rate-regulated carriers. Specifically, the statute provides that:

Effective July 1, 2008, the retail rate jurisdiction of the board shall not be applicable to single line flat-rated residential and business service rates unless the board during the first six calendar months of 2008 extends its retail rate jurisdiction over single line flat-rated residential and business service rates provided by a previously rate-regulated telephone utility. The board may extend its jurisdiction pursuant to this paragraph for not more than

---

<sup>1</sup> See In re: Deregulation of Local Exchange Services in Competitive Markets, Docket No. INU-04-1, "Final Order," (issued December 23, 2004) (hereinafter 2004 Deregulation Proceeding); and In re: Deregulation of Single Line Flat-Rate Local Exchange Services in Competitive Markets, Docket No. INU-05-2, "Final Decision and Order," (issued December 5, 2005) (hereinafter 2005 Deregulation Proceeding).

two years and may do so only after the board finds that such action is necessary for the public interest.

Iowa Code § 476.1D(1)"c."

Pursuant to this statute, single line flat-rated residential and business service rates are presumptively deregulated as of July 1, 2008, and the Board is not required to make a determination as to whether effective competition exists with respect to those services. While the effective competition standard does not directly apply in this proceeding, the Board must still determine whether continued regulation over single line flat-rated residential and business service rates is "necessary for the public interest." In order to make that determination, the Board should consider whether sufficient competition or market forces are in place to restrain rate increases to levels that are just and reasonable. (Tr. 143-45).

As such, the Board will consider the market forces identified in § 476.1D(1)"b" as they relate to the presence of competition for single line flat-rated local exchange service in Iowa when making its determination regarding whether it is necessary for the public interest to extend the Board's rate jurisdiction beyond June 30, 2008. These market force considerations, while not binding, are instructive to the Board's analysis of the public interest.

The participants in this proceeding presented extensive information, data, opinions, and conclusions concerning the status of competition for Qwest's, Frontier's, and Iowa Telecom's (collectively referred to as the ILECs) single line flat-rated local exchange residential and business services. In addition, IAMU raised a

proposal that advocates implementation of certain pricing controls on single line flat-rated residential and business offerings by the ILECs. In this order, the Board will discuss IAMU's rate limitation proposal first and then will discuss the status of wireline competition and each of the market force considerations individually as they relate to the status of telecommunications competition in Iowa.

#### **1. IAMU's Rate Limitation Proposal**

IAMU states that the Board is charged with protecting the public interest when considering whether to extend its jurisdiction over single line flat-rated residential and business rates. IAMU asserts that the Legislature has given the Board the opportunity to do something unique and IAMU suggests that the Board implement a transitional method of deregulating basic telecommunications services in Iowa.

IAMU's proposal centers on establishing a threshold on the range of retail pricing for single line flat-rated residential and business service offerings by the large ILECs. IAMU is concerned that large ILECs may charge less than the full cost of providing service in one exchange, where they face competition, and cross-subsidize this rate reduction by charging higher rates in another exchange. IAMU wants the Board to establish a systemwide cost recovery standard that would prohibit the ILEC provider from charging an amount outside a given rate spread. (IAMU Brief, p. 2; Tr. 389). IAMU asserts that such a compromise would support competition by preventing predatory pricing by dominant carriers.

Iowa Telecom, Frontier, and Qwest state that IAMU's proposal is inconsistent with the intent of Iowa Code § 476.1D(1)"c" and that the Board has not been given

the authority to impose pricing changes of this nature. Qwest also states that IAMU's proposal would likely require new legislation. (Qwest Brief, p. 2; Tr. 135).

The Board agrees with the ILECs and finds that IAMU's proposal goes beyond the scope of Iowa Code § 476.1D(1)"c" by creating a new form of zone regulation over the retail pricing of single line flat-rated services. Like IAMU, the Board is concerned about the effect that some pricing strategies by the large ILECs may have on small and municipally-owned telecommunications providers. However, Iowa Code § 476.1D(1)"c" does not provide any statutory authority for the Board to implement pricing differential restrictions with respect to single line flat-rated residential and business rates. Therefore, the Board cannot consider IAMU's suggestion as a workable proposal.

## **2. Wireline Competition**

### **Participants' positions**

Consumer Advocate states that according to the most recent Local Competition Report released by the Federal Communications Commission (FCC) in March 2008,<sup>2</sup> competitive local exchange carriers (CLECs) accounted for about 16 percent of the switched access lines provided in Iowa. Consumer Advocate also asserts that based on this recent FCC data, ILECs own or control 93 percent of the end-user switched access lines in Iowa. However, Consumer Advocate notes that the FCC's data includes only a portion of cable telephony that is being provided in

---

<sup>2</sup> In re: Local Telephone Competition: Status as of June 30, 2007, released March 2008.

Iowa because the regulatory status of local telephone service provided by such methods remains undetermined. (Tr. 422-23, 471-73).

Iowa Telecom states that more than 60 percent of its residential lines and more than 80 percent of its business lines have a CLEC, a cable telephony provider, or both as competitive options. Iowa Telecom states that the Board previously determined that conventional CLEC services are close substitutes for single line flat-rated local exchange service in the 2004 and 2005 Deregulation Proceedings. In addition, Iowa Telecom states that some CLECs that provide service in Iowa Telecom's service territory have been making advances in their facilities-based operations and are overbuilding many of Iowa Telecom's exchanges. (Tr. 283-86).

Frontier states that it faces traditional CLEC competitors in its service territory. Frontier states that parts of its service area have been overbuilt by at least one municipality and four other competitive carriers. Frontier claims that these competitors are well positioned to compete for all of Frontier's customer segments in its service area. (Tr. 368).

A recent survey report issued by the Board<sup>3</sup> shows that Qwest serves 78 percent of all wireline connections in its service area. Qwest, however, asserts that the Board's survey report understates the extent of CLEC competition in the Qwest service territory. Qwest offers information indicating that as of December 2007, CLECs are ordering unbundled loops or platform services from Qwest. Qwest

---

<sup>3</sup> See 2007 Telecommunications Market Monitoring Survey for Retail Local Voice Services, (released January 2008) (hereinafter 2007 Survey Report).

states that these wholesale services are used by CLECs to offer local voice services to customers. Qwest also states that many of its wire centers have competitors offering local service through their own facilities. (Tr. 52).

### **Discussion**

The record in this proceeding supports the finding that multiple CLECs are offering wireline services in all or part of each of Iowa Telecom's, Frontier's, and Qwest's service territories and that such services are offered at rates that are comparable to those rates offered by the incumbent carriers. Based on the information provided, it appears that the majority of customers in the ILECs' exchanges can obtain a similar service from a CLEC at a competitive price. The practical result of this level of wireline competition is a restraint on rate increases; it is unlikely an ILEC can raise its single line service rates to an unreasonable level without losing so many customers as to make the rate increase unprofitable. Therefore, based on this record the Board concludes that the current level of wireline competition in Iowa is sufficient to discipline prices in general and provide a competitive incentive for reasonable service quality for most customers.

### **3. Wireless Competition**

#### **Participants' positions**

Consumer Advocate states the Board's 2007 Survey Report shows that there are approximately 2 million wireless connections in Iowa and that wireless carriers provide service to at least 97 percent of the 904 communities in Iowa. Consumer Advocate also states that there are some Iowa communities where there are more

wireless connections than there are wireline connections. (Tr. 445). Consumer Advocate asserts that the increased demand for wireless service by lowans does not change the value that most households and small businesses continue to place on a wireline connection. Consumer Advocate asserts that for most lowans, wireless service is not an economic substitute for a wireline service, but rather serves as a supplement to traditional wireline service. Consumer Advocate states that the ILECs have not provided compelling evidence of the substitutability of wireless service for wireline service in this proceeding.

Iowa Telecom states that wireless service is available throughout all of its service territories and is growing in demand. (Tr. 203). Iowa Telecom estimates that there are at least two competitive alternatives in each of its exchanges. (Tr. 207-09). Iowa Telecom asserts that wireless service is quickly becoming a substitute for wireline service and that a growing number of lowans are abandoning their wireline services. (Tr. 225-26). Iowa Telecom claims that it has seen its number of local calls decline by about 38 percent from 2003 to 2007. (Tr. 260). Iowa Telecom traces this reduction, in part, to wireless substitution.

Frontier states that it faces wireless competition in nearly every market for nearly every customer segment. (Tr. 367). Frontier states that a significant portion of that competition comes from wireless substitution and the displacement of traditional wireline service as younger customers forego ILEC landline services completely. (Id.).

Qwest states that wireless services are available in 98 percent of the communities served by Qwest and that wireless service represents a viable alternative to Qwest's wireline service for a significant (but unspecified) number of its Iowa customers. Qwest also states that wireless pricing is competitive with Qwest's local exchange service, particularly in light of, wireless carriers offering plans that include unlimited minutes that are designed to serve as a substitute for wireline service. (Tr. 74-76).

### **Discussion**

The record in this proceeding is evidence that the national debate continues as to whether wireless service is a substitute or a supplement to wireline service for different customer groups. Nevertheless, the record supports the findings that Iowa consumers are using wireless services in greater numbers and that the increased rate of wireless usage is affecting the wireline service providers; for example, the Board's 2007 Survey Report indicates that wireless connections now exceed wireline connections in Iowa. Iowa Telecom, Frontier, and Qwest have all suffered line losses, which the companies attribute to competitive forces and primarily to wireless competition. Therefore, based on the record before it, the Board finds that the current level of wireless competition in Iowa is a sufficient market force at this time to help discipline wireline prices and ensure reasonable service quality for many customers.

#### **4. Cable Telephony**

##### **Participants' positions**

Consumer Advocate states that the Board's 2007 Survey Report reveals that cable telephony is not a significant source of competition to the large, well-established ILECs in Iowa. Consumer Advocate asserts that based on the total ILEC and CLEC retail local service connections reported to the Board, slightly less than 3 percent are based on cable telephony, which translates to fewer than 45,000 cable telephony customers in Iowa. (Tr. 429). Consumer Advocate also states that the uneven and geographically-limited deployment of cable telephony and the relatively slow adoption of the service by consumers undermines any characterization of cable telephony as an interchangeable option to basic voice service. (Tr. 431). Moreover, Consumer Advocate asserts that cable companies typically do not offer single line flat-rate local exchange service at rates that compete with those of the ILECs.

In contrast to Consumer Advocate's position, Frontier states that cable providers are offering voice services in over 60 percent of Frontier's service area. (Tr. 367). Qwest states that according to the Board's 2007 Survey Report, cable telephony is available in 58 percent of Qwest's Iowa communities. Qwest contends that the 2007 Survey Report understates the number of cable telephone companies and the coverage of cable telephony. Qwest states that by its own estimates, there are three cable companies that are providing telephone service to 79 percent of Qwest's wire centers, which represent 96 percent of Qwest's access lines. Qwest also states that the Board's 2007 Survey Report shows that cable telephone

connections have increased more than 300 percent since the Board's previous survey report, which was released in March 2006.<sup>4</sup> Qwest asserts that this growth will continue and will provide significant competition for Qwest and other ILECs in Iowa.

### **Discussion**

Based on the information in this record, cable telephony is available in communities throughout Iowa and is becoming a more popular option for Iowa consumers. The Board acknowledges Consumer Advocate's statement that cable companies are not typically offering single line flat-rated local exchange service as a stand-alone service at rates that are competitive with the ILECs. However, the Board agrees with Qwest that the growth of cable telephony as evidenced by the Board's 2005 and 2007 Survey Reports is a continuing trend and will likely increase as a market force that will help put additional price constraints on ILECs to ensure just and reasonable rates in communities where cable telephony is available.

## **5. Voice over Internet Protocol (VoIP)**

### **Participants' positions**

Consumer Advocate asserts that a competitive and affordable broadband platform does not yet exist for Iowa consumers and therefore intermodal alternatives to local exchange service that rely on broadband access, such as VoIP, cannot be considered competitive substitutes for basic local exchange service. Consumer

---

<sup>4</sup> See Second Statewide Telecommunications Competition Survey for Retail Local Voice Services in Iowa, (released March 2006).

Advocate states that because of the fact that VoIP requires a broadband connection, it remains out of reach for those Iowa consumers seeking rates comparable to those charged by the ILECs for single line flat-rated stand-alone service. (Tr. 480).

Iowa Telecom asserts that digital subscriber lines (DSLs) are available in each of Iowa Telecom's exchanges and that cable modem or CLEC-provided DSL service is available in exchanges that account for more than 70 percent of Iowa Telecom's access lines. Iowa Telecom also states that some form of competitive broadband offering, either through cable modem, CLEC-provided DSL, or wireless satellite service, is available to more than 90 percent of Iowa Telecom's access lines. (Tr. 210). Iowa Telecom also states that stand-alone VoIP service is available in every Iowa Telecom wire center and that it has begun to place a downward pressure on prices for conventional voice services.

Frontier states that it is also facing competition from VoIP providers in its service territory. Frontier states that while many of its customers do not currently consider VoIP as a service option, the availability is nevertheless a competitive market force that impacts pricing decisions throughout Frontier's market. (Tr. 367).

Qwest states that VoIP is a rapidly growing technology that represents a competitive alternative to traditional wireline telephone services in Qwest's service territory. Qwest asserts that there is a ubiquitous presence of broadband connections in Iowa and, as such, anyone with available high-speed Internet access can add VoIP services for a low incremental cost. (Qwest Brief, p.4).

### **Discussion**

Based on the information presented in this proceeding, VoIP is becoming increasingly available throughout Iowa and is growing as an option in telecommunications service. The Board understands Consumer Advocate's position regarding the requirement that VoIP users have a broadband connection. The Board recognizes that purchasing a broadband connection just for VoIP service is not likely to be cost-effective for Iowa consumers who are seeking rates comparable to those charged by the ILECs for single line flat-rated stand-alone service. However, according to Qwest's testimony, high-speed Internet access is now available to more than 90 percent of Iowans and many Iowans are availing themselves of that technology for non-telephony purposes. For these customers, the proper focus is on the incremental cost of VoIP plus broadband. Based on the information in this record, VoIP is becoming a more popular option for Iowa consumers and is growing as a market force that may put additional price constraints on ILECs to ensure just and reasonable rates in the near future.

## **6. Economic Barriers to Competition**

### **Participants' positions**

Consumer Advocate states that ILECs often create competitive packages that bundle additional services with single line flat-rate local exchange service for a discounted rate. Consumer Advocate expresses concern that ILEC competitors will find it difficult to compete with the ILECs' bundled services. In addition, Consumer Advocate states that the availability of bundled offerings may create an economic

incentive for ILECs to raise the rates for basic local exchange service in order to encourage migration to bundled offerings and subsidize the ILECs' provision of bundled and new services. (Tr. 490-91). Consumer Advocate asserts that Iowa consumers who subscribe to no additional features cannot reasonably be expected to substitute bundled services for basic local exchange service. (Tr. 491).

Iowa Telecom states that there are competitive packages available to Iowa Telecom customers at rates that are close to the rates paid by basic local exchange service customers. Iowa Telecom asserts that many of its customers currently purchasing basic service also purchase other features and therefore these customers could become packaged service customers if the unbundled single line rate were to increase. Iowa Telecom states that the availability of services from CLECs, cable providers, and wireless carriers to Iowa Telecom's customers demonstrates the existence of appropriate market forces and results in Iowa Telecom attempting to provide competitive options to its customers.

Frontier states that it, like Iowa Telecom, is concerned about the competitive vulnerability of its single line customers. Frontier states that it is more concerned about losing its single line voice customers to competitors offering bundled services such as video and VoIP or cable telephony, than it is about losing its customers that already have bundled service packages furnished by Frontier. (Tr. 373-74). Frontier states that all of its customers have benefited from this kind of competition in its markets.

### **Discussion**

Iowa Telecom and Frontier agree that the availability of services from CLECs, cable providers, and wireless carriers to Iowa consumers demonstrates the existence of appropriate market forces and results in ILECs offering more competitive options to their customers. The Board acknowledges Consumer Advocate's concern that the availability of bundled offerings may create an economic incentive for ILECs to raise the rates for basic local exchange service in order to encourage migration to bundled offerings and subsidize the ILECs' provision of bundled and new services, but the record in this proceeding does not support that anticipated outcome. Rather, it appears that sufficient market forces are in place at this time in the form of wireless, VoIP, and cable offerings to constrain prices overall. The Board anticipates that increasing competition will provide incentive to all carriers to create new bundles, packages, or other service offerings to attract customers. This should be viewed as a benefit of the competitive marketplace, rather than a detriment.

### **ANALYSIS**

Pursuant to Iowa Code § 476.1D, single line flat-rated local exchange residential and business rates are presumptively deregulated effective July 1, 2008, and the Board can overcome that presumption only if it has demonstrated that the extension of the Board's jurisdiction over prices for single line flat-rated services is necessary for the public interest.

The Board finds that the record in this docket supports the determination that sufficient market forces exist throughout Iowa to constrain the price of single line flat-rated residential and business rates in general. The record shows that competitive offerings from CLECs, wireless carriers, and cable providers are available in much of the state and most Iowa consumers have a choice of telecommunications service providers. The record also shows that each of the rate-regulated ILECs has lost access lines, which appears to be an indicator of the competitive forces within the market. The Board finds that based on the evidence of the continued loss of access lines by all three rate-regulated ILECs in Iowa, the findings in the Board's 2007 Survey Report, and the evidence provided by Qwest, Frontier, and Iowa Telecom, there is sufficient evidence to support a finding that there are competitive choices for basic telecommunications services in most of Iowa and such competition will allow the market to discipline future general rate increases and ensure that such prices remain just and reasonable overall.

For the foregoing reasons, the Board finds that the record in this case is insufficient to overcome the presumption of deregulation and that an extension of the Board's jurisdiction pursuant to § 476.1D is not necessary for the public interest.

**ORDERING CLAUSE**

**IT IS THEREFORE ORDERED:**

The single line flat-rated residential and business rates shall be allowed to sunset pursuant to Iowa Code § 476.1D"c," effective July 1, 2008, as described in this order.

**UTILITIES BOARD**

/s/ John R. Norris

/s/ Krista K. Tanner

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary

/s/ Darrell Hanson

Dated at Des Moines, Iowa, this 27<sup>th</sup> day of June, 2008.