

STATE OF NEW YORK

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Commission Adopts Telecommunications Policy Framework to Address Changing Industry Dynamics

Albany, NY – 4/11/06 – The New York State Public Service Commission today voted to adopt a Statement of Policy and Order that acknowledges the increasing presence of competition in the telecommunications industry by granting incumbent telephone companies the flexibility to respond to competitive forces, while maintaining appropriate protections – including basic service and Lifeline – to ensure consumers continue to have access to quality telephone service at just and reasonable rates. The Commission's policy is designed to encourage infrastructure investment to promote network reliability and preserve the existing network, strengthen service quality and promote the emergence of new services.

Today's decision in the "Competition III" proceeding is a logical progression of the Commission's pro-competitive telecommunications policies that have been developed over the past 21 years. Competition III was initiated to examine issues related to competition resulting from the rapid development of voice and other telecommunications services now being provided over new networks that are different from, and compete with, the traditional wireline network platform. Examples of this "intermodal competition" include digital phone services provided by cable television companies, phone service using Voice over Internet Protocol (VoIP) technology, and wireless service.

"Intermodal competition in the telecommunications industry is no longer a concept or a policy goal; it's a reality," said Public Service Commission Chairman William M. Flynn. "Roughly 90% of New Yorkers now have the choice of at least two alternatives to traditional wireline service, and tens of thousands of customers are choosing these newer services each month to obtain savings, innovative services and other value-added offerings. The reality is that telephone service is no longer a natural monopoly, and this Commission is taking the necessary steps to allow the competitive market to flourish while prioritizing important consumer protections."

In initiating the Competition III proceeding last June, the Commission recognized that technology-based competition is constantly and rapidly changing the nature of telecommunications services by providing consumers with choice and innovative, value-added services. The Commission undertook this comprehensive examination of the policies, rules and practices governing telephone service in New York with the goal of establishing a more flexible and symmetrical regulatory framework that will promote innovation, increase consumer benefits, and encourage economic investment in the state's telecommunications infrastructure. Competition III is the third formal evaluation of telecommunications policies conducted by the Commission since 1989. In each case, the Commission has evaluated changes in the industry and in the market, and has implemented regulatory requirements accordingly.

Historically, telephone companies were monopolies that owned the entire infrastructure needed to place a telephone call, and regulatory oversight was the primary means to ensure that companies charged reasonable prices and delivered adequate service. Today, competitors using their own facilities and networks have dramatically expanded consumers' options for an array of telecommunications services. The Commission today essentially recognized that "Plain Old Telephone Service" likely will not mean a traditional wireline telephone for much longer.

"The regulatory framework for telecommunications services cannot remain static while the industry innovates and evolves. Inaction on the part of this Commission would stifle further innovation by treating a competitive service as if it were still a monopoly service," said Chairman Flynn. "The rules and regulations that have governed this industry for nearly a

century do not adequately address today's competitive environment, which empowers customers with the ability to choose from among several service providers offering a wide array of services. This policy strives to achieve a level playing field for all telephone service providers operating in competitive markets, giving them the flexibility to meet customer needs reliably and at a reasonable cost."

Listed below are some the key findings and decisions contained in today's Statement of Policy and Order:

Status of Competition: Based on the alternatives now available to 90% of New York's consumers, the Commission concludes that the residential market for telephone service is adequately competitive in the regions of the state where those alternatives exist. In New York, there are currently four basic alternatives to traditional wired telephone service: 1) cable or IP-enabled telephony, 2) competitive local exchange carriers (CLEC) that lease parts of the incumbents' (e.g. Verizon or Frontier) facilities to provide service to residential and business customers, 3) wireless, and 4) Voice over Internet Protocol (VoIP) services using broadband networks. However, given the rapid pace of change in the industry, the Commission directed staff from the DPS to monitor the market and report back in one year on any additional action that might be necessary.

Consumer Protections: The Commission required the continuation of current consumer protections and urged companies, including competitive providers that are not subject to the Commission's jurisdiction, to provide similar protections. Further, the Commission directed the DPS staff to develop a new "consumer report" in order to capture useful and objective information that consumers can use to make informed choices about telecommunications service providers.

Service Quality and Network Reliability: The Commission will continue its current approach to ensuring quality service and network reliability. However, going forward, the Commission believes consumers would be better served if the wide range of "intermodal" providers already in the marketplace reported key information (a new "consumer report") rather than continuing certain reporting requirements for only incumbent providers that now represent a shrinking segment of the overall market. Further, the Commission is interested in exploring a shift in focus from end-user standards more appropriate in a monopoly environment to standards that focus on the reliability of various networks. Therefore, the Commission will initiate a separate rulemaking proceeding to examine appropriate changes to streamline service quality regulations going forward.

Basic Services: The Commission recognizes that the prices set for this service are not properly aligned with the associated costs borne by the service providers, ultimately jeopardizing their ability to continue providing them on an ongoing basis. To address this, the Commission will permit incumbent providers, if they so choose, to gradually adjust the prices for basic service to

reflect their actual costs in order to promote network reliability and assure the continued provision of universal basic service. The Order requires the continuation of "basic" telephone service, with two options available to consumers: flat rate and message rate basic service where currently offered. Under the flat rate option, which includes unlimited local calling, Verizon is authorized to increase the monthly charge by \$2 per year up to a cap of \$23. Frontier of Rochester is authorized to increase its monthly charge for flat rate service by \$2 per year for two years, at which point the company would need further Commission review to continue to increase the cost of flat rate service beyond two years. Under the message rate option – which consists of a monthly "access line" charge plus a charge for each local call – both Verizon and Frontier of Rochester will have the option to increase the monthly access charge component by no more than \$2 per year for two years. The companies are limited to one rate change each year for basic service and must file a tariff for Commission approval before any change in rates becomes effective. Incumbent companies that do not face the same level of competitive pressures that Verizon and Frontier of Rochester face will be required to justify to the Commission any proposed rate increases for basic service.

Pricing Flexibility: In order to allow Verizon-NY and Frontier of Rochester to be more responsive to price competition offered by intermodal carriers, they are granted unlimited pricing flexibility for all non-basic services (i.e. three-way calling, voicemail, caller ID) with a few exceptions. However, the Commission will require that non-basic service prices be uniform throughout the company's territory. Smaller companies would be granted pricing flexibility if they can demonstrate to the Commission that competitive forces in their service territory warrant such flexibility.

Level Playing Field: The Commission concluded that incumbents' provision of wholesale services to competitors is not sufficiently competitive to warrant the relaxation of continued price and service regulation, especially for monopoly bottleneck facilities.

Commissioner Thomas Dunleavy said, "The information economy requires widespread access to flexible telecommunications applications that facilitate economic development and investments in jobs from the private sector. Achieving that objective requires a level playing field where all telecommunications providers have the proper market-based incentives to invest in infrastructure. Today's decision adheres to the principle of universal service while building on the basic principles that regulation should reflect market conditions and, where feasible, competition is the most efficient way to ensure the provision of quality telecommunications services at reasonable rates, "

Commissioner Leonard A. Weiss said, "This Commission is keenly aware of the need to protect consumers who might not be in a position to take advantage of competitive offerings. Today's Statement of Policy and Order strikes an appropriate balance between protecting those

customers and providing incumbent providers the opportunity to recover costs associated with providing service."

Commissioner Patricia Acampora said, "There is no doubt that the choices available to consumers in the competitive market are expanding, but certain protections must be preserved. I am pleased with the provision of this Statement of Policy and Order directing staff to work with other agencies to identify opportunities for improving Lifeline enrollment and outreach to eligible customers."

Commissioner Neal Galvin said, "The Commission recognizes that service quality is vital and that maintaining the integrity of the traditional telephone network is critical. We will continue to monitor service quality aggressively, but this Statement of Policy and Order also is an invitation to all service providers to work with the Commission on the issue of network reliability."

Procedural Background and Public Input

The Order Initiating Proceeding and Inviting Comments in the Competition III proceeding was issued on June 29, 2005. Based on initial comments from interested parties, DPS staff issued for comment a White Paper on September 21, 2005, and 27 parties filed comments by the October 28, 2005 deadline. In addition, staff conducted seven public statement hearings and educational forums around the state during September and October to enable members of the public to comment on the White Paper. Speakers at these events included members of the New York State Assembly and New York City Council, representatives from chambers of commerce and other business and economic development groups, members of the Communications Workers of America, representatives of for-profit and non-profit enterprises, representatives of organizations that provide assistance to low-income individuals, and a representative of the Attorney General of New York State. Staff also conducted four round table discussions to explain the proceeding and seek input from individual consumers, business people, community-based organizations and government agencies in areas of the state where competitive choices may be limited.

The Commission will issue a written decision detailing today's vote. The decision in Case 05-C-0616, when available, can be obtained from the Commission's Web site at <http://www.dps.state.ny.us> by accessing the "Commission Documents" section of the homepage. The Commission's Order also can be obtained from the Commission's File Office, 14th Floor, 3 Empire State Plaza, Albany, NY 12223 (518-474-2500).