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June 2003

Dear Readers,

Welcome to the inaugural issue of *The NRRI Journal of Applied Regulation*. In 2002, The National Regulatory Research Institute ceased publishing *The NRRI Quarterly Bulletin (QB)*. The *QB*—as readers and those of us at the NRRI affectionately knew it—ran from 1979 through 2001. Although it is always sad to see an old friend go, we are pleased to introduce you to the first volume of our new publication, *The NRRI Journal of Applied Regulation*. We hope it is a worthy successor to the *QB*.

In the fall of 2002, the NRRI issued a Call for Papers for a new publication; at that time we were calling it *The NRRI Annual*. We began receiving papers in late 2002 and selected papers for publication early in 2003. As stated in the Call for Papers, the focus of this publication is on research and policy analysis of interest to the regulatory community. Moreover, we are especially interested in papers from state regulatory commissions. Our intent and focus have not changed. We chose to title our new publication *The NRRI Journal of Applied Regulation* for two reasons. First, we wanted a title that more closely reflects the contents and purpose of the publication—we are not publishing an “NRRI yearbook.” Second, we did not want to restrict ourselves to having only one edition per year. Indeed, if we receive a sufficient number of quality papers in response to our next Call for Papers, we would be delighted to publish *The NRRI Journal of Applied Regulation* more frequently than annually.

I have had the honor of being the editor of this maiden voyage of *The NRRI Journal of Applied Regulation*. This edition includes papers from staff of the Florida, Illinois, Puerto Rico, Rhode Island, and Wisconsin commissions; there is also one paper written by NRRI researchers. I thank each author who submitted a paper. I could not have completed this project by myself, however, and I gratefully acknowledge the efforts of my NRRI colleagues, Ken Costello, Lilia Perez-Chavolla and Vivian Witkind Davis, who assisted with the editing of the papers. The design of the cover is due to the work of Nikhil Moro, one of the NRRI's talented graduate research associates. I am also extremely grateful for the efforts and talent of Carmell Brown, who took the papers submitted by the authors along with the edits my colleagues and I provided and produced the finished copy.

We hope you will find these papers to be interesting and useful. Your feedback and comments will make future editions of *The NRRI Journal of Applied Regulation* better.

Sincerely,

Ed Rosenberg, Ph.D.
Editor

TELECOMMUNICATIONS COMPETITION IN THE COMMONWEALTH OF PUERTO RICO

Historical Assessment and Future Prospects

by Javier Rúa-Jovet, Esq.*

Origins and Legal Development of Puerto Rico's Telecommunications Industry

"What hath God wrought?" On Mar. 1, 1859, 15 years after Samuel Breese Finlay Morse sent his famous message through an experimental telegraph line set-up by Congress between Baltimore and Washington,¹ the celebrated inventor kicked off the telecommunications era in the overseas Spanish colony of Puerto Rico when he erected a private line to connect his daughter's estate with his seaside commercial office in Arroyo, a quiet southeastern township.²

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¹ *The History of the Telegraph and Telegraphy* <<http://inventors.about.com/library/inventors/bltelgraph.htm>>.

² Edmundo Disdier, *Telefónica de Puerto Rico, Marcando una Nueva Era* 1-2 (1st ed. 1990) (on file, Univ. of P. R. Lázaro General Library); Ramón Morales-Cortés, *Telecommunications in Puerto Rico*, <<http://www.vii.org/papers/puer.htm>>; Orlando Merced, *Samuel Morse en Arroyo, El Nuevo Día* (Revista Domingo), Aug. 25, 2002, at 13, <<http://adendi.com>>.

By 1882, barely six years after the invention of the telephone apparatus, Mr. Preston C. Nelson, a representative of New Jersey's West India Telegraph and Telephone Company, proposed to establish a telephone system between the capital city of San Juan and the towns of Ponce and Mayagüez.³ Despite the fact that the local Spanish governor, Mr. Miguel de la Vega-Inclán, authorized Mr. Nelson's initiative, the Royal Overseas Government (*Gobierno de Ultramar*) quickly overruled such authorization.⁴

However, just a year later, Alfonso XII, King of Spain, decreed the establishment of a telephone network under a monopoly franchise for his entire kingdom, including the overseas domain of Puerto Rico.⁵ Under the King's 1883 decree, the Government declared its exclusive right "to establish and exploit" Puerto Rico's telephone

³ Disdier, *Telefónica de Puerto Rico*, at 5.

⁴ Id.

⁵ Id.

service, and private use was possible only by means of franchises or concessions.⁶

As per that royal authority, the colonial governor ordered a phone network for use by the government of Puerto Rico, its dependencies, and the military. By 1885, said network connected 13 local stations and a central station at La Fortaleza, the Governor's residence in San Juan, forming what has been described as "one of the most advanced telecommunications infrastructures in the Spanish Empire,"⁷ Also, by 1893 there were at least 42 privately used telephone lines in service, financed by wealthy landowners and businessmen.⁸ In this connection, it is worth noting that the island's telephone system was (and still is today, as we shall see) characterized by a constant tension between the ideal of governmental ownership and control, versus the private ownership model.⁹ As such, under the Spanish model, telephone service was under a government

⁶ *Id.* at 5, 9.

⁷ Morales-Cortés, *Telecommunications in Puerto Rico*.

⁸ Disdier, *Telefónica de Puerto Rico*, at 6, 9.

⁹ *Id.*

monopoly in which only the richest individuals could afford private lines.

1898-1990: The Monopoly Era

After Spain's defeat in the Spanish-American War, the United States occupied Puerto Rico and soon after acquired legal sovereignty and title over the island as per the terms of the peace treaty signed by both powers.¹⁰ According to Section 32 of the Foraker Act of 1900, a congressional law that established and organized civil government in the island, "all grants of franchises, rights, and privileges or concessions of a public or quasi-public nature," including telephonic franchises, were to be made by an Executive Council, with the approval of the Governor. Also, all franchises granted in Puerto Rico would be reported to Congress, which reserved the power to annul or modify them.¹¹

Fourteen years later, the Porto Rico Telephone Company was founded by the brothers Sosthenes and Hernand

¹⁰ *Treaty of Paris of 1898*, 30 Stat. 1754, 1759; *A Treaty of Peace Between the United States and Spain*, U.S. Congress, 55th Cong., 3d sess., Senate Doc. No. 62, Part 1 (Washington: Government Printing Office, 1899), 5-11.

¹¹ 1 Hist L.P.R.A. § 32; Organic Act of Apr. 12, 1900, c. 191, 31 Stat. 77 § 32.

Behn, who later, in 1920, went on to establish the telecom giant International Telegraph and Telephone Company (ITT), perhaps the first modern multinational company.¹² In that year, ITT absorbed both Porto Rico Telephone and the Telephone Company of Cuba, although each maintained their local corporate names.¹³

According to the government franchise awarded, franchise no. 322, the Porto Rico Telephone Company could build and operate a long distance telephone system and the local system of each town or city included within said permit. The franchise provided that the Puerto Rico Government would have an option to buy the telephone system in the year 1934. However, as we shall discuss, that buyback did not take place.¹⁴ Porto Rico Telephone's franchise covered most of the island, except those areas controlled by the

government's Interior Department by virtue of a statute of Mar. 14, 1907.¹⁵ The Interior Department, eventually erected a telephone system, which comprised the outlying islands of Vieques and Culebra and the mountain town of Caguas.¹⁶ Thus the first developments of the Puerto Rico telecommunications market under the U.S. flag included both heavily regulated private interests (PRTC) and a wholly public, government-owned system, which served different geographical areas (Interior Department).

The passage of the Jones Act,¹⁷ the federal statute that, *inter alia*, granted U.S. citizenship to Puerto Ricans, brought additional regulation into the island's nascent telecommunications scene. From 1917 on, all grants of franchises, rights, privileges, and concessions of a public or quasi-public nature would now be made by a three-member public service commission appointed by the Governor with the advice and consent of the Senate. That Commission was

¹² Disdier, *Telefónica de Puerto Rico*, at 15, 17.

¹³ It is noteworthy that in 1923 ITT entered into the Spanish market and obtained an exclusive contract from Primo de Rivera, the dictator of Spain. From that contract the Spanish Telephone Company, a telecom monopoly was born. Angel Calvo, "Private and Public Ownership in the South European Local Telephone Networks (1877-1923)" (University of Barcelona, Spain) EBHA Conference Helsinki, 2002 <<http://www.valt.helsinki.fi/yhis/ebha2002/papers/calvo.pdf>>.

¹⁴ Disdier, *Telefónica de Puerto Rico*, at 16.

¹⁵ See, *P.R. Telephone Co. v. Tribunal de Contribuciones y Descartes*, 81 D.P.R. 982, FN 11 (1960), 1960 WL 13992.

¹⁶ Disdier, *Telefónica de Puerto Rico*, at 15, 17.

¹⁷ 1 HIST L.P.R.A. § 38, Organic Act of Mar. 2, 1917 Jones Act § 38, c. 145, 39 Stat. 951, 964.

empowered and directed "to discharge all the executive functions relating to public service corporations, heretofore conferred by law upon the Executive Council and such additional duties and functions as may be conferred upon said commission by the Legislature." The Jones Act also granted the Legislative Assembly of Puerto Rico "the authority to enact laws relating to the regulation of the rates, tariffs, and service of all public carriers in Puerto Rico," and authorized the Public Service Commission (PUC) "to enforce such laws under appropriate regulation."

One significant event that *did not* take place during the year 1934 was the buyback of the Porto Rico Telephone Company by the Government, as provided by section 20 of the company's franchise. In 1925, the Puerto Rico Legislature had passed a law, Act No. 25 of Jun. 9, 1925, whose purpose was to unify the existing private and public telephone systems, if and when the government exercised its buyback option in 1934. But the deadline came to pass without government action. Several years later, by virtue of Act No. 212 of May 12, 1942, the Puerto Rico Communications Authority was created;

the intention was, once more, to merge the island's private and public telephone systems, this time through the exercise of eminent domain. The expropriation did not take place either.¹⁸

At the federal level, this period is distinguished by the passage of the Communications Act of 1934 by Congress.¹⁹ The Communications Act of 1934, which remains the single most important telecommunications legislation in effect, established a Federal Communications Commission (FCC) because the previous federal organization with communications jurisdiction, the Interstate Commerce Commission (ICC) was not devoting sufficient resources and time to telephony, concentrating instead on the railroad industry.²⁰ The 1934 Act established a dual regulatory framework; section 2(a) reserves for the FCC exclusive jurisdiction over interstate communications, while section 2(b) reserves to the states, territories and possessions, jurisdiction over intrastate communications.

¹⁸ See, Norma Santiago, *Telecommunications Historical Highlights*, Business Puerto Rico, Commemorative Issue 2000, at 66.

¹⁹ 47 U.S.C. 151, *et seq.*

²⁰ See, Henk Brands and Evan T. Leo, *The Law and Regulation of Telecommunications Carriers* (Artech House, 1999) §1.1.2 at 5.

Under the legal regime set up by the Communications Act of 1934, the idea of intra-franchise telecommunications competition was considered an abomination.²¹ The intrastate telecommunications market was assumed to constitute a natural monopoly, that is, a market whose demand can best be served by a single company that, while shielded from competitive pressures, is submitted to significant regulation, mainly in pursuit of universal service ends.²²

Market demand for telephone service continued to grow steadily throughout the interwar and post-war periods and the newly renamed *Puerto Rico Telephone Company* (PRTC) set out to meet that demand. In 1922 there were an estimated 9,174 lines in service; by the end of the Second World War, there were more than 19,000. In

²¹ See, Brands and Leo, *The Law and Regulation of Telecommunications Carriers*, fn 19, §1.2.2 at 16 (1999).

²² Harvey L. Zuckman, et al., *Modern Communications Law*, (West, 1999) §12.1 at 912. Generally, "universal service" describes the public policy goal of maintaining residential telephone service fees sufficiently low so that anyone in the United States can afford them, thus boosting nationwide telephone penetration. Artificially low residential fees have been historically sustained by artificially high business rates for virtually the same service. See, *Newton's Telecom Dictionary*, 17th ed., (Flatiron, 2001) at 729.

1955, the total number of phones in service had increased to 50,965 and by 1963 the number had risen to 162,624.²³

In 1969, PRTC had 276,278 lines; however, meeting the constant need for growth was increasingly difficult. By 1974, the PRTC's network had become seriously overburdened. That juncture gave rise to a new government push to buy the telecom company, which culminated in the creation of the Puerto Rico Telephone Authority (PRTA) by means of Act No. 25 of May 6, 1974.²⁴ The Government viewed telephone service as a universal right. It therefore, sought to take on the role of sole service provider in order to achieve that ideal.

The PRTA was founded "in order to establish an efficient communications system to stimulate the economic development of Puerto Rico for the general well-being of the People of Puerto Rico," and bestowed on the PRTA the legal authority to purchase all of PRTC's issued common stock for such purposes.²⁵ In July 1974, the PRTA finally purchased PRTC from ITT

²³ Disdier, *Telefónica de Puerto Rico* at 16, 18, 28.

²⁴ See, 27 L.P.R.A. § 401, *et seq.* (repealed).

²⁵ *Id.*

for 165 million dollars. With the culmination of the transaction, Puerto Rico's entire telephone system effectively became a government-run monopoly.²⁶ At the height of Puerto Rico's monopoly era (circa 1988), the government-controlled holding company (PRTA) owned PRTC's local exchange operations and Telefónica Larga Distancia (TLD), a carrier for international and interstate telecommunications services.²⁷

Deconstruction of a Paradigm and the Rise of the Competitive Ideal: 1990 to Date

The antitrust action brought forth by the federal Department of Justice against American Telegraph and Telephone (AT&T) during the 1970s was the first major shake-up of the

²⁶ However, it was not until 1994 that the government owned Puerto Rico Communications Authority, successor of the island's Interior Department, became effectively fused to PRTC. See, Santiago, *Telecommunications Historical Highlights* at 73.

²⁷ *Id.* at 72. Until 1987 an entity comprised of ITT and All American Cable and Radio (AACR) held an international and interstate long distance monopoly in Puerto Rico. The FCC, however, divested that monopoly and AACR eventually sold its Puerto Rico interests to AT&T. Then and there, PRTC formed TLD as a company that would not provide local exchange service, would keep separate accounting books from PRTC, and would compete against AT&T in the international and interstate long distance markets.

serene existence U.S. phone monopolies had been enjoying for close to a century. This action, and its resultant Divestiture Order, brought about the disintegration of the "Bell System" into AT&T and the Regional Bell Operating Companies (RBOCs or Baby Bells).²⁸

However, one thing must not be overlooked about Judge Greene's Divestiture Order: although the modern trend has been towards re-consolidation among the divested RBOCs, the Order paved the way for the birth of competition in the interstate and international long distance markets.²⁹ In this sense, it is fair to say that the Divestiture Order spelled the proverbial beginning of the end of the then unquestioned monopoly paradigm. As such, the stateside success of long distance liberalization, and the consumer benefits brought forth

²⁸ *United States v. AT&T*, 552 F. Supp. 131 (D.D.C.1982) *cert. denied* 460 U.S. 1001. On Jan. 8, 1982 AT&T, under the watchful eye of Judge Harold Greene, signed a Consent Decree with the U.S. Department of Justice in which the parties agreed that by Dec. 30, 1983 AT&T would spin off or divest itself from its 22 RBOCs. Those companies would then form seven regional holding companies (RHCs) (Ameritech, Bell Atlantic, BellSouth, NYNEX, Pacific Telesis, Southwestern Bell (SBC) and US West).

²⁹ After several mergers and acquisitions among the original RHCs, only four RHCs remain, and some even have new names: QWEST, Verizon, SBC and BellSouth. See, <<http://www.fcc.gov/wcb/cpd/Mergers>>.

by competition of private interests in that market, made the idea of privatization acceptable and palatable to Puerto Rico authorities. Also, the cash boon that sale of the governments' telecom assets would bring into the Commonwealth's depleted treasury could fund very important government infrastructure and educational programs.³⁰

In 1990, the Administration of then Governor Rafael Hernández Colón attempted to sell PRTC.³¹ The sale, however, never went through. During the fallout of the ill-fated transaction, government officials stated that they could not sell the company to the highest bidder, Bell South, because the price offered by all bidders was low compared to the sale price expected by the Government, which was close to \$2 billion.³² According to the Administration, the situation of impending war in the Middle East was not conducive to high price transactions, since investors were naturally

conservative. Massive labor protests and a general strike were also very important factors that derailed the sale.³³ In 1992, nevertheless, the Government was able to sell TLD to Telefónica Internacional, a subsidiary of Telefónica de España, the Spanish telephone holding company, albeit with several FCC-mandated facilities ownership and non-discrimination restrictions.³⁴ However, PRTC local exchange operation remained an organization plagued by all the inefficiencies and distorting elements associated with government-owned monopolies.

³³ *Id.* at 12-14.

³⁴ See, Santiago, *Telecommunications Historical Highlights* at 72-73. FCC restrictions require a U.S. carrier, not a foreign company, to retain telecom facilities. In its *Market Entry and Regulation of Foreign-affiliated Entities, Report and Order*, FCC Docket No. 95-22, 11 FCC Rcd 3873 (1995), (Foreign Carrier Entry Order), the FCC explained that as part of its public interest analysis under Section 214 of the Communications Act of 1934, it examines whether effective competitive opportunities exist for U.S. carriers to provide like services in the destination markets of foreign carriers seeking to enter the U.S. international services market through certain affiliations with a new or existing U.S. carrier. Regarding the requirements placed on TLD, see, e.g., *In the Matter of Telefónica Larga Distancia de Puerto Rico, Inc., Review of Nondiscrimination Safeguards, Memorandum Opinion and Order*, File Nos. I-T-C-92-116-AL (Apr. 8, 1997). See, also, alien ownership proscriptions regarding FCC radio and spectrum licenses, contained in Sections 310(a) and (b) of the Communications Act of 1934.

³⁰ See, Act No. 5 of Apr. 10 1990, 27 L.P.R.A. § 401.

³¹ *Id.* See, also, Act. No. 63 of Aug. 23 1990, 27 L.P.R.A. § 441 (creating a Telecommunications Regulatory Commission (TRC) that would oversee the privatized PRTC after the sale). The stillborn TRC was eventually dissolved.

³² Disdier, *Telefónica de Puerto Rico*, Part V, at 4, 5.

Around 1995, Lambda Communications, a subsidiary of Centennial Cellular Corporation (hereinafter Centennial) began its incursion into the island's telecommunications market.³⁵ However, the legal regime for competition was not yet in place, so began the first of many legal battles between Centennial and PRTC, dealing mainly with interconnection and construction issues.³⁶ Although Centennial barely pierced PRTC's monopolistic armour, these initial battles foreshadowed the paradigmatic shift that would soon take place all over the United States with the enactment of the Federal Telecommunications Act of 1996.

The Federal Telecommunications Act of 1996, which amended the Communications Act of 1934, fundamentally transformed the statutory

³⁵ Centennial of Puerto Rico was born out of Centennial Cellular Corporation, a company owned by Century Communications, which controlled the enterprise until 1998. On Jan. 7, 1999, CCW Acquisition Corporation merged with the former, thus creating Centennial License Corporation <http://www.centennialpr.com/wireless/quienes_somos.asp>.

³⁶ Centennial was forced to litigate against PRTC in local courts as well as in the Commonwealth's Public Service Commission, which held telecom and CATV jurisdiction before the enactment of Act 213 of 12 September 1996. See, generally, Santiago, *Telecommunications Historical Highlights* at 73.

regime that governed the telecommunications landscape of the United States and its territories.³⁷ The 1996 Act expressed great faith in the idea that competition would produce lower prices and higher quality of service for telecommunications consumers everywhere, while promoting the rapid deployment of new telecommunications technologies.³⁸

One of the most important goals of the 1996 Act was to open the traditionally monopolistic market for local telecommunications services to competition.³⁹ In this sense, Section 253 of the 1996 Act outlawed all State and municipal barriers to entry. In other words, all statutes, regulations or local legal requirements that "may prohibit or have the effect of prohibiting the ability

³⁷ Telecommunications Act of 1996, P.L. No. 104-104, 110 Stat. 56, amending and as codified within the Communications Act of 1934, 47 USC §§151, 251, *et seq.*

³⁸ *Id.*, Purpose Statement, 110 Stat. 56, 56 (1996).

³⁹ See, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, *First Report and Order*, 11 FCC Rcd 15499, 15505-06, para. 3 (1996) (Local Competition First Report and Order), *aff'd in part and vacated in part sub nom. Competitive Telecommunications Ass'n v. FCC*, 117 F.3d 1068 (8th Cir. 1997), *aff'd in part and vacated in part sub nom. Iowa Utils. Bd. v. FCC*, 120 F.3d 753 (8th Cir. 1997), *aff'd in part, rev'd in part, and remanded sub nom. AT&T Corp. v. Iowa Utilities Bd.*, 525 U.S. 366, 119 S. Ct. 721, 142 L. Ed. 2d 835 (1999).

of any entity" to provide inter or intra-state telecommunications where thenceforth illegal.⁴⁰

Although prior law imposed a general interconnection duty on common carriers, Congress now established legal rules that required cost-based nondiscriminatory pricing of interconnection and unbundled network elements. Incumbent local exchange carriers (ILECs) were now required: a) to interconnect their network facilities with the networks of competing telecommunications carriers (CLECs) at "any technically feasible point and on just, reasonable, and non-discriminatory terms," b) to unbundle their services into their constituent network elements, making these elements available to competing telecommunications carriers on a just, reasonable, and non-discriminatory basis, and c) to provide for resale of any of their retail services to other telecommunications carriers at a reasonable discount rate. Furthermore, if the FCC made a legal finding that an RBOC ILEC had taken meaningful and sufficient steps to open local markets in a state to competition, then it could be allowed to enter the

⁴⁰ 47 U.S.C. 253 (a).

manufacturing and/or interstate long-distance market in that state, which would be otherwise unlawful under Judge Greene's Divestiture Order.⁴¹

As a direct result, the Puerto Rico Legislature created a specialized and dedicated body to carry out the local aspects of the 1996 Act's mandate. Unlike most stateside PUCs or Public Service Commissions (PSCs) which regulate several utilities like electricity, gas, water and telecommunications, Puerto Rico opted for an administrative body whose main purpose was achieving the pro-competitive goals set by Congress, while minimizing the hindrance involved in regulating multiple sectors of the economy. As such, Act 213 of Sept. 12, 1996, otherwise known as the Puerto Rico Telecommunications Act of 1996, created the Puerto Rico Telecommunications Regulatory Board (the board).⁴² The board was created with a clear mandate to foster total, equal and fair competition in the Puerto

⁴¹ 47 U.S.C. 271. In addition, Congress extended the scope of the Pole Attachments Act, to grant telecommunications providers, as it already provided for cable TV companies, access to private utility poles (e.g., non-government owned power companies) for a small fee. See, *AT&T Corp. v. Iowa Utilities Bd.*, 525 U.S. 366, 119 S. Ct. 721, 142 L. Ed. 2d 835 (1999).

⁴² 27 L.P.R.A. § 265, *et seq.*

Rico telecommunications market. Constituted as a three-member panel, the Board is empowered with quasi-legislative powers to enact rules and regulations and also operates as a quasi-judicial, adversarial, deliberative body capable of receiving and resolving inter-company and consumer-to-company complaints.

Another watershed development in the local market during this era took place on Apr. 7, 1997, when the Administration of Governor Pedro Rosselló announced a new plan to privatize PRTC and Celulares Telefónica, its wireless division. Privatization, as a way to dispose of outdated or inefficient enterprises, while providing an influx of capital and a correlative reduction in government costs, mirrored in many ways the neo-liberal "deregulatory" ideal which prompted the enactment of the Federal Telecommunications Act of 1996 and the local Act 213.⁴³ In other words, it assumes that subjecting telephone service provision to the rigors of market competition will increase efficiency. But

⁴³ See, generally, Donald F. Kettl, *Reinventing Government, A Fifth-Year Report Card*, The Brookings Institution, CPM Report 98-1 (September 1998), <<http://www.brook.edu/dybdocroot/gq/cpm/government.pdf>>.

that would occur only if the company behaved as a private enterprise, not a politicized government agency.

The Puerto Rico Legislature moved quickly and enacted Act No. 54 of Aug. 4, 1997 to authorize the sale. After a competitive bidding process, a consortium led by GTE Corporation won controlling interest in PRTC.⁴⁴ Even though massive labor strikes ensued, the government finalized the acquisition on Mar. 2, 1999.⁴⁵ It was now time to test the new paradigm.⁴⁶

Behavior of the Puerto Rico Telecommunications Market after the Introduction of Private Competition and Impressions on its Prospects

In following the spirit expressed in both the Federal Telecommunications Act of 1996 and local Act 213, the board has strived to utilize competition and market forces as the primary setter of

⁴⁴ Verizon, the largest ILEC in the nation, is now the majority shareholder of PRTC. Verizon was formerly known as Bell Atlantic Corporation. It began doing business as Verizon Communications on Jun. 30, 2000, when Bell Atlantic Corporation merged with GTE Corporation.

⁴⁵ See, generally, Santiago, *Telecommunications Historical Highlights* at 74, 75.

⁴⁶ It is quite encouraging to note that the new administration of Governor Sila M. Calderón has proven to be on the free-market side of the equation, as it has decisively opposed recent legislative rumblings aimed at regaining government control of PRTC through stock repurchase or even expropriation.

prices, terms, availability and conditions of telecommunications services. However, board intervention has been required to rectify market imperfections, perhaps resulting from vestigial monopolistic practices. For example, the board recently issued a final "Resolution and Order on Reconsideration" on the *PRT Tariff K-2* case.⁴⁷ In this case, the board reviewed the legality of the switched access service rate charged to long distance companies by PRTC for the use of its network in originating and terminating intra-island long distance calls. Two companies, Sprint and Centennial (although others later joined) argued that Tariff K-2 (named after the page in which the rate is found in the documents filed by PRTC) was not cost-based and thus violated local Act 213.

Although presently under review at the Circuit Court Appeals of the Commonwealth of Puerto Rico,⁴⁸ the "Resolution and Order on Reconsideration" held that intra-island access and termination rates would be set based on non-hypothetical forward-

looking cost methodologies, which in turn had the direct effect of lowering the composite two-way tariff rate from a per-minute average of 0.93563 cents to 0.021489 cents. The Board determined that historical prices associated with plant or infrastructure already in place were unrelated to true cost and should not influence current pricing decisions. If upheld by the reviewing court, the ruling will be incrementally implemented along a three-year phase-in. Besides reducing the composite two-way rate, the board also granted a \$67,971,175 true-up-conferred directly on end-users on a per-consumer basis—as reimbursement for the monies overcharged.

The *PRT Tariff K-2* case involved a long and drawn out litigation process, which not only continues at the intermediate appeals level but will probably end up in Puerto Rico's Supreme Court. At the national level, this type of litigation has been the norm rather than the exception, fueling a substantial choir of voices arguing that the legal reforms brought forth nationally

⁴⁷ *Lambda Communications, Sprint International v. PRTC (Tariff K-2)*, Case No. 97-Q-0003 (97-Q-0001), <<http://www.irtpr.gobierno.pr>>.

⁴⁸ *Lambda Communications, Sprint International v. PRTC*, KLRA 2002-00178/KLRA2002-00192.

by the 1996 Act and locally by Act 213 failed to deliver.⁴⁹ In this sense, as John D. Windhausen Jr., President of the Association for Local Telecommunications Services (ALTS) has noted, "the Bell companies have appealed virtually every decision by the FCC and the states to enforce the Telecommunications Act."⁵⁰

Thus, the *PRT Tariff K-2* case in many ways typifies the national aftermath of the 1996 statutory paradigm shift. In fact, the current term of the U.S. Supreme Court will finally settle three consolidated sets of cases whose outcomes will determine significant questions regarding the costs of local telephone services. One of these cases, *Verizon Communications, Inc. v. F.C.C.*, has already been handed down.⁵¹ In that case, the Supreme Court upheld FCC norms enacted under

⁴⁹ See, e.g., Young, Dreazen & Blumenstein, "Familiar Ring: How Effort to Open Local Phone Markets Helped the Baby Bells: An Aggressive SBC Thrives Under New Regulation; A Trend to Oligopolies," *The Wall Street Journal*, Feb. 11, 2002 at A1.

⁵⁰ Stephen Labaton, "Slew of Supreme Court Cases to Focus on '96 Telecom Law," *The New York Times*, Oct. 1, 2001 at 2, <<http://www.nytimes.com/2001/10/01/technology/01TELE.html?pagewanted=print>>.

⁵¹ *Verizon Communications, Inc. v. F.C.C.*, 535 U.S. 467, 122 S.Ct. 1646, 152 L.Ed.2d 701, 70 USLW 4396, 2 Cal. Daily Op. Serv. 4078, 2002 Daily Journal D.A.R. 5139, 15 Fla. L. Weekly Fed. S 233 U.S. May 13, 2002.

the Telecommunications Act of 1996, which call upon state utility commissions like the Board to set rates⁵² for lease of network elements charged by ILECs to CLECs, on a forward-looking basis. In other words, the rate review process shall operate without regard to the incumbents' historical or past investment in infrastructure. The Court also held that (a) the methodology chosen by the FCC to set rates for lease of network elements to CLECs is not inconsistent with the plain language of the 1996 Telecommunications Act and is not unreasonable; and (b) the Act does not preclude the FCC from requiring ILECs to combine leased elements of their networks at the request of CLECs, who cannot combine them themselves.

The decision re-affirms the 1996 Telecommunications Act and restores confidence in the competitive telecommunications model. The Supreme Court's opinion considers and discards Bell Companies' allegations, not dissimilar to local arguments marshaled during the *PRT Tariff K-2*

⁵² Under Article 7 of Puerto Rico Act 213, that type of board action is only permitted pursuant a formal complaint. In other words, the board cannot perform *sua sponte* review or examination of whether or not a company's rates, tariffs or charges are based on cost. See, 27 L.P.R.A. § 269f(b).

case, to the effect that the TELRIC⁵³ standard does not allow for a fair return on their investment. The Supreme Court also ratified the FCC's combination rules. This aspect of the decision will undoubtedly promote facilities-based competition because it enables CLECs to combine their own technology and equipment with pre-existing ILEC infrastructure.

Unquestionably, competition in local telecommunications markets has taken longer than expected to take root. Policymakers and competitors have fostered unreasonable expectations or "over-promised" results regarding the speed and breadth of local competition development.⁵⁴ But if we accept the thesis that the onslaught of litigation was a fundamental cause which slowed the local and federal enforcement of the Telecommunications Act of 1996, then no one but our legal system is really to blame. However, litigation and judicial review of statutes and agency action is

⁵³ Total Element Long Run Incremental Cost or TELRIC is a method for determining what phone service should cost, based on the true cost of equipment and labor, not counting the embedded or "historical" cost. See, *Newton's Telecom Dictionary*, 17th ed., 2001, p.692.

⁵⁴ See, David S. Turetsky, "Change in the Telecommunications Industry," 197 *New Jersey Lawyer* 35 (June 1999).

a fact of life of the legal systems of Puerto Rico and the United States.⁵⁵ Unlike the so-called "deification of statutes" and the legislative supremacy which characterizes European civil law systems, in a common-law country such as the United States the final arbiters of what the law is sit on the benches of the Supreme Court, not in the hallowed halls of Congress.⁵⁶ Thus, competition has been slow to develop because the rules set by Congress in 1996 have been subjected to litigation ever since their enactment.

However, if *Verizon Communications, Inc. v. F.C.C.*, is an omen of things to come, local telecommunications competition could be on the verge of revitalization. Once the rules are firmly in place and become

⁵⁵ Puerto Rico's "private" law is contained in a Romanic Civil Code inherited from Spain (who, in turn received it from Napoleonic France). "Public" law (Constitutional, Administrative and Procedural Law) is based on the U.S. model. Thus Puerto Rico, not unlike the state of Louisiana, can be described as a mixed jurisdiction, in which both civil and common law traditions co-exist. Other prominent examples of mixed jurisdictions include Quebec and Scotland. See, Liana Fiol Matta, "Civil Law and Common Law in the Legal Method of Puerto Rico," *American Journal of Comparative Law*, 40 (1992): 783-816.

⁵⁶ See, John Henry Merryman, Davis S. Clark and John O. Haley, *The Civil Law Tradition: Europe, Latin America, and East Asia*, (Charlottesville, VA: Michie, 1994): 707-708.

generally immune to judicial attack, then federal and local authorities will be free to enforce them. In today's marketplace, the debate focuses not on whether competition is positive or negative but on whether ILECs are perpetuating their vestigial monopoly power through a lack of compliance with statutory and regulatory initiatives designed to open local telephone markets.⁵⁷

Despite its recent economic woes, the telecommunication's industry is a \$600 billion market that is not going to go away. According to the FCC's latest numbers for the U.S. and its territories, the CLECs' national market share grew 93% over the one-year period of January to December of 2000. In addition, at least one CLEC was serving customers in 56% of the Nation's zip codes, and about 88% of U.S. households reside in these zip codes.⁵⁸

Puerto Rico boasts around 1.5 million wireline telephones. Although PRTC remains by far the dominant local exchange carrier, Centennial continues

⁵⁷ See, generally, Turetsky, "Change in the Telecommunications Industry."

⁵⁸ *Federal Communications Commission Releases Latest Data on Local Telephone Competition*, <<http://www.fcc.gov/ccb/stats>>.

its CLEC operation. In addition, six companies compete in the island's long distance⁵⁹ and wireless markets.⁶⁰ The wireless market, alone, has experienced close to three hundred percent growth during the past five years. These numbers will continue to rise, specifically with the deployment of blossoming technologies such as digital subscriber line (DSL) services, coaxial cable modems, internet telephony⁶¹ and third generation (3G) wireless systems.⁶² There is also space for growth in landline service. Island penetration lies at around 74.6%, quite

⁵⁹ These are: AT&T, Sprint, TLD of Puerto Rico, PRT Long Distance, MCI and Primus Communications.

⁶⁰ These are: AT&T wireless, Sprint PCS, Movistar, Cingular Wireless, Verizon Wireless and Centennial. There are approximately 1,500,000 wireless phones in use in Puerto Rico. In Puerto Rico, 54% of families own wireless phones, around 1.6 units per home.

⁶¹ Liberty Cablevision of Puerto Rico has launched a limited cable telephony trial with voice-over-Internet Protocol (VoIP) provider Net2Phone with hopes of expanding the service throughout the island. The move would make Puerto Rico the first U.S. jurisdiction to host a large-scale cable-based VoIP system. <http://currentissue.telephonyonline.com/ar/telecom_nephone_launches_voip>; <<http://web.net2phone.com/about/press/news/20020701tvinsite.asp>>; <http://www.broadbandweek.com/news/020701/020701_telecom_3.htm>.

⁶² 3G technologies allow for text and digitized audio and video transmission at speeds up to 2Mbps, in a stationary wireless service and at 384kbps in a mobile environment. This makes services such as fast wireless Internet and real-time video-conferencing possible and marketable.

lower than the level experienced stateside, which is over 94%.

Conclusion

One hundred and forty three years have passed since Puerto Rico joined the telecommunications era. The rise and fall of the monopolistic-paradigm on the island echoed the analogous legal and socioeconomic world-view changes occurring stateside and around the world. Federal and local statutory reform was a fundamental step forward in the movement towards local telecommunications competition.

Although, the realization of a competitive local exchange market has been slower than anticipated, there is reason to expect change. The legal rules enshrined federally in the Telecommunications Act of 1996 and in the Puerto Rico Act 213 are just now being tested by the courts. If recent Supreme Court action foreshadows prospective judicial trends, a world in which telecommunications companies prompt technological progress, while battling for customers in an open market, could be on the verge of a renaissance.