ALASKA LEGISLATURE COMMITTEE FILES 1995-1996 8672

8681 HOUSE LABOR & COMMERCE

Paralegal I, Range 13	$ 29,736		
Fringe Benefits	11,862		
Total Paralegal I		$ 41,598	
Clerk-Typist III, Range 8	$ 21,996		
Fringe Benefits	7,431		
Total Clerk-Typist III		$ 29,427	
Subtotal Personal Services			$ 337,105
Contractual			
Expert Witness	$ 90,000		
Transcript Cost	5,000		
Subtotal Contractual			$ 95,000
Travel			
Subtotal Travel			$ 6,500
Supplies			
Subtotal Supplies			$ 7,300
Equipment			
Subtotal Equipment			$ 3,100
TOTAL			$ 449,005

This fiscal note does not budget for additional space costs (typically for two years from the agency's budget) or computer support (one-time equipment expense) required to support the positions requested.

Narrative Description of New Position Duties

The Commission recognizes that a bill designed to increase competition ought to result in less need for regulation, rather than more, since regulation is a substitute for competition. However, this bill assigns significant new responsibilities to the Commission and sets much tighter deadlines, backed up by automatic approval if they are not met. This requires the Commission ensure that it has the resources staff to meet the peak demand for regulation.

Hearing Examiner, Part-time

Section 4, Format of Orders

This section would require the Commission to state its conclusions of law in each formal order relating to a telecommunications utility. This requirement, combined with the deadlines for Commission decisions established by other sections of the bill, would require additional support to the Commission in the form of a part-time Hearing Examinor. The judicial approach of allowing parties to propose findings of law would probably delay, rather than accelerate decision-making.

Common Carrier Specialist

Sections 8-11 will require a substantial rulemaking to define the terms "injury" or "detriment".

Section 11. Current law and Commission policy support interconnection to the facilities of one utility by another utility. Upon application by a utility unable to interconnect, the Commission is mandated to order access if the public convenience and necessity would be served and if there is not substantial injury to the owner utility, substantial detriment to its facilities or a safety hazard created. AS 42.05.321(a).

Access to the network is critical to competitors in order to be able to serve all potential customers. However, this section adds a new subsection (c) that switches the default standard. It provides that for telecommunications utilities Commission may require joint use or interconnection only if it "finds that the use or connection will not result in injury to the owner utility or its customers, or in detriment to the services furnished by the owner utility..."

This change would establish the Commission as the gatekeeper for a significant new barrier to entry to telecommunications markets. In order to reconcile these duties with meeting the bill's goal of fair competition, the Commission must be staffed to handle a significant increase in the number of interconnection cases. All utilities are covered by the interconnection statute, not just regulated public utilities.

The anticipated increase in alternative service providers seeking connection would require an increase in the development of new policy and a major increase in case-by-case adjudication. A full-time Common Carrier Specialist would be required.

Utility Tariff Analyst II (full-time and part-time)

Section 6 authorizes price discrimination for new services that, under current law, is prohibited as an unreasonable preference. Telecommunications utilities would offer many new services, each triggering a proposed tariff revision. Of the 69 local exchange carrier (LEC) tariff revisions filed in FY95, the Tariff Section's Tariff Analyst II (UTA II) reviewed 37. These filings comprised approximately 70% of the UTA II's workload. An increase of 50 LEC filings requiring analysis would require 1.0 UTA II's. There are 23 regulated LECs.

The accelerated timetable set out in Section 17 will require review, analysis and decision within 30 days, rather than the 45 days currently allowed for tariff filings. Twelve requests for new services determinations would require .5 full-time equivalent (FTE) UTA II.

Total 1.5 FTE UTA II

Economist II

Section 17 will require the Commission to determine within 30 days, upon request, whether a telecommunications service is subject to competition. This change in the Commission's duties will require additional staff expertise in the form of an Economist.

Section 18 parallels 17 and requires the Commission to determine incremental cost. This will involve a significant rulemaking to define incremental cost and establish Commission policy. For example is incremental cost short-run or long-run? It will require review and investigation of a significant new docket load by an Economist.

Total 1 FTE Economist II.

Paralegal I

This position is required to analyze the additional cases that will result within the established deadlines. Production of the orders required to meet the tighter schedules set in the bill necessitates the creation of this position.

Clark-typist III, Range 8

The Commission requires this clerical support to handle the additional work generated by the new professional staff, as well as to meet the shortened deadlines.

FAX COVER

DATE: 8/8/95

TO: George Dozier, Jr

FROM: Rep. Carl E. Moses (Nancy)

PHONE: 258-8167 **FAX:** 258-1261

 # PAGES (including cover): 5

MESSAGE: Sectional of HB 346

CEM/lb/fax

346

HB ~~384~~ "Telecommunications Act of 1995"

Testimony of Thomas C. Edrington
General Manager/CEO ATU Telecommunications

I am Tom Edrington, General Manager of ATU Telecommunications. Today I am here with Mark Foster and Chip Shooshan to offer testimony regarding HB 346, also known as the Alaska "Telecommunications Act of 1995."

I personally have 25 years telecommunications industry experience working mainly at AT&T General Departments in New York and Pacific Bell in San Francisco. My area of expertise during these years was focused on technology evolution, implementation and the policy impacts that resulted. Mark Foster has been a Commissioner at the Alaska Public Utilities Commission where he acquired a personal familiarity with the workings of regulation in Alaska. Chip Shooshan is with Strategic Policy Research in Bethesda, Maryland and has been involved with telecommunications policy at the national level for many years.

Together, we believe in the importance of this legislative proceeding asit goes about the business of defining Alaska's telecommunication future. Chip will discuss the legislation from the prospective of national public policy events, while Mark will discuss the legislation from the perspective of the Alaskan environment. I would like to offer some observations about the legislation that should be remembered as we dwell on the details of the matter. These are;

1) The legislation is necessary and mainstream
2) Alaska's scope and scale
3) Technology has changed the economics of communications

The legislation is necessary and mainstream

By now it is apparent to almost everyone that we have entered the information age. While information is the consumable product of this age, the communications infrastructure is the system enabled the information explosion. Over the last two decades advances in communications, computer and image technology have forever changed the way we go about our lives and business. Indeed, whole industries and markets have been redefined by technologies (such as PCS, the new wireless technology) which allows easy access to markets that were previously held captive by high entry costs. These changes along with the divestiture of the old Bell System have lead, in large part, to the need to redefine regulation to a more modern role. The pending national telecommunications legislation is one outcome of this process.

The type of legislation contained in HB 346 has been placed into practice in over 30 states starting in 1983 in Iowa. These states contain the large industrial economies of Wisconsin, Illinois, and Michigan as well as other economies such as North and South Dakota, Wyoming, and Minnesota. It is important to remember as the dialog progresses on this bill -- with an undoubted focus on details and differing points of view -- the type of legislation proposed is mainstream and is working in many places in the United States. These are the same states that Alaska will be competing with to attract industry in the future. HB 346 is essential to allowing Alaska to gracefully transition to the new communications infrastructure emerging on the national level.

This type of mainstream regulation is essential for Alaska in preparing for the major changes that are anticipated as a result of national telecommunications legislation that has passed both houses during this current session. This legislation opens markets and allows customer choice for a number of services from local exchange to long distance. Indeed, the market boundaries between

industries such as cable television, wireline, and wireless technologies are becoming meaningless. Into this world where everyone can be in any business, the fundamentals of the communications industry, and it regulation, must change.

However, the national legislation is not blind to differences in state conditions. Thus the federal legislation currently places a strong emphasis on the role of the states in carrying out its intent in the state context. This is a good thing, because Alaska's situation is clearly different in a number of ways from the communications industry in the lower 48.

Alaska's scope and scale

In this room, we are all abundantly familiar with the many ways that Alaska differs from the outside, both in its scope and scale. In scope we are a resource focused economy with a geographic scale that is vast. These facts are integral, unspoken parts of our daily lives and thought process. Alaska, and being an Alaskan, is different.

In considering this bill, the differences of Alaska also apply. Many of the precepts of how to regulate the communications infrastructure have resulted from the titanic struggles between Baby Bell's earning billions of dollars serving multiple millions of subscribers and equally large long distance companies. The investments to compete in these circumstances are immense. For example, the Baby Bells contribute over a billion dollars a year to Bellcore to perform their R&D and software systems maintenance functions.

In Alaska companies such as GCI and ATU have reported 1994 net incomes in the range of 10 million dollars. The entire population of Alaska is under six hundred thousand people, with a concentration of almost half this number in

Anchorage. Alaskans live in towns ranging from middle sized to small towns and tiny villages.

The differences of Alaska have implications for how we choose to regulate. For example, we do not have the economic base to spread out costs that produce marginal value. Further, the economic, and physical, barriers to entry are significantly different in our situation.

Alaska is different in scope and scale from the outside. The realities of our market dynamics may be markedly different from those of Los Angeles, Houston, or Orlando. The automatic application of rules for billion dollar companies may not apply, or be required, with companies more suited to the Alaskan marketplace.

Technology has changed the economics of communications

Changes in technology have been a prime cause of changes in the nature of the communications marketplace. Ten years ago cellular telephones were a novelty, costing over $1,500 a set and $1.00 a minute to use versus today's "free" cellular phones with a six month service commitment and per minute costs of less than 50 cents. The Internet is a reality with a world wide web that didn't exist 5 years ago and now claims twenty million plus users. Our cable television systems are multiple channel, with the promise of interactive capabilities and other communications possibilities on the horizon.

Technology has created a vital, dynamic market place where the customer can choose from a variety of means to meet their communications needs -- and choose they do. Many of the communications users in Alaska have constructed their own communications networks with combinations of equipment ranging from their own satellite systems to leased fiber optic facilities. The fastest growing segment of ATU's business is in T1, a high speed digital facility

equivalent to 24 telephone channels, which customers use to carry their communications over their own private networks in lieu of the standard telephone call network. Recently, companies have paid over 7 billion dollars for PCS radio frequency licensees in order to be able to directly connect to customers as an alternative to the current local wired connection.

The traditional barrier to customer choice represented by "ownership of the wires to the customer" has been obliterated by technology. Indeed, one could well argue that the traditional telephone companies had best adopt the new technologies or be left in the dust by their competitors.

Conclusion

The bill before this group represents a good approach to recognizing the changes in the communications industry while providing the consumer with choice and protection during the transition to a new model of the communications industry. There is nothing radical or extreme in these more modern rules. As we go about determining Alaska's regulatory future by this process, and the issues that this legislation will resolve, ATU feels it is important to remember these points;

1) The legislation is necessary and mainstream
2) Alaska's scope and scale
3) Technology has changed the economics of communications

Finally, regardless of the outcome of the current national legislation, the forces of the technologies and customer demands require this type of change in the regulatory system. We can either manage these changes or be forced to react to them.

Alaska Telephone Association
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(907)563-4000
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Duane C. Durand
President

James Rowe
Executive Director

September 27, 1995

Honorable Pete Kott
Chairman
Labor and Commerce Committee
Alaska State Legislature
Juneau, Alaska 99801

RE: Comments in support of HB 346

Dear Rep. Kott:

On behalf of the Alaska Telephone Association (ATA) I extend my thanks to you and the members of the Labor and Commerce Committee for the opportunity to offer comments in support of HB 346. I also offer my thanks to the sponsor of the bill, Rep. Carl Moses, for his timely introduction of legislation so vital to the economic development of our State.

The Alaska Telephone Association has been actively participating in the telecommunications legislation endeavor at the federal level over the past two years. We have also monitored the continuing transition toward competition in telecommunications in many states. The 22 local exchange companies that comprise the ATA have served the citizens of Alaska by providing modern telecommunications in some of the most challenging locations and environments in the nation. These companies will continue to serve the State as demands, technology and the regulatory environment evolve.

ATA endorses the legislative initiative proposed in the Telecommunications Regulatory Reform Act of 1995. Key aspects of local competition include:

- Universal service at affordable rates.
- Competition is presumed to be in the public interest in large urban markets.
- Competition is presumed not to be in the public interest in rural markets.
- In markets that are competitive, there must be a level playing field.
- Reasonable costs that local exchange providers incur to permit competitors to use the local exchange network should be borne by the competitor(s).

- Regulation in all competitive markets should be minimal.

The providers of local exchange service represented by ATA are dedicated to the highest quality of life, opportunity for economic development and access to all the health, educational and social benefits for all Alaskans that can be delivered through the advent and accessibility of telecommunications.

Thank you.

Very Truly Yours,

James Rowe

Claim of lien

keep in mind the Republic was being attacted from within while the 14th amendment was being proposed, the intent was the artifical "legal?" person 'ie' the corporation would have a perpetual life more so than that of the communist mind.

Also knowing they would become involved by grant of State, the Constituion states in part: "No state shall... make anything but gold and silver coin a tender in payment of debt." thereby invalidating the grant also in what Manner had the artifical person tendered payment for the grant by State!

Charles E. McKee 9/21/1995

RECEIVED
SEP 21 1995
GOVERNOR'S OFFICE

This is a photocopy of the original.

UNITED STATES OF AMERICA)
STATE OF ALASKA) ss.

Charles E. McKee being first duly sworn on his oath deposes and says: I am the claimant named in the foregoing Claim of Lien; I have read the same, know the contents thereof and that the same is true as I verily believe.

Subscribed and sworn to before me this 21 day of September, 1995

[signature]
Notary Public for Alaska
My commission expires
5-30-97

ATU PRESENTATION

ON

THE TELECOMMUNICATIONS

ACT OF 1995

H.B. 346

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SUMMARY OF TESTIMONY OF HARRY M. SHOOSHAN III

ON HB 346, "THE ALASKA TELECOMMUNICATIONS ACT OF 1995"

SEPTEMBER 27, 1995

On the whole, I believe that "The Alaska Telecommunications Act of 1995" provides a sound basis for revamping the Alaska Code to permit efficient competition and will help to usher in an era of "new opportunities" in this state as ATU suggests.

It is a fundamental principle in our free economy that firms respond to incentives. Thus, the incentives provided by the marketplace, or by regulation where necessary as a surrogate for marketplace forces, are important. As the legislature, you have the opportunity to set the direction of public policy in this vital sector and to make certain that regulation provides the right incentives; in this case, incentives to invest, to innovate and to supply quality service at appropriate prices. As competition intensifies, spurred by federal legislation as well as by actions you take here in Alaska, regulation must adapt to the new environment. I believe you can and should move ahead without waiting for the enactment of federal legislation. Nor should you be bound in any way by the specific approaches to the various issues taken in the federal legislation . . . or in legislation adopted by other states for that matter.

As I see it, the proposed Alaska Telecommunications Act of 1995 ("the proposed Act") has three essential components. It seeks to provide for fair competition in establishing terms for interconnection and for access to essential facilities. It provides for streamlined regulation of new and competitive services. And, while retaining traditional rate-of-return regulation, it modernizes the regulatory treatment of investment and depreciation.

I would like to address each of these essential components in more detail.

Interconnection of Competitors

First, the obligation to interconnect should run both ways; that is, it should be symmetrically imposed on all competitors. **Second**, while some parties will undoubtedly urge you to go further by requiring ATU to disaggregate its network, requiring the interconnection of competitors is sufficient to permit local competition. The legitimate needs of competitors should be determined in part by who they are and by their relative positions in all telecommunications markets. Moreover, you should be careful not to destroy what I would term "the economies of the firm" which might be the result of requiring ATU to disaggregate its local network. **Third**, the proposed Act would require that the costs of any modifications or additions needed to facilitate interconnection are borne by the competitors. In principle, this is unobjectionable. **Fourth**, I am unclear about the effect of conditioning interconnection on the absence of "injury to the owner or other users of the facilities" and especially about removing the word "substantial." If the language is read to require the APUC to consider whether competition generally might result in economic harm to a public utility, I am concerned that such language could be used by incumbent firms to block efficient competitors from obtaining interconnection.

Streamlined Regulation

As competition continues to develop, it is appropriate to tailor regulation to fit the new circumstances. This means allowing the incumbent firm to respond when competition exists for a particular service or group of services. The proposed Act's standard for classifying **competitive services** appropriately focuses on the availability of a substitute service and not on how many customers may choose to buy the substitute service (*i.e.*, a measure of market share). The main problem with the latter approach is that it actually penalizes the incumbent firm for being an effective competitor; or put another way, it forces the incumbent to lose share by being unresponsive to customers' needs in order to gain regulatory flexibility. It is also important that firms have the incentive to introduce **new services**. By providing for streamlined regulation of new services, the proposed Act will encourage regulated public utilities to innovate.

Establishing a **price floor** based on incremental cost is supported in the economic literature and consistent with the direction that public policy is going in other jurisdictions. The purpose of a price floor is to provide regulatory (in addition to antitrust) protection against predatory pricing by a firm with market power.

While competitors can be expected to argue that incumbent firms should be kept under tighter rein, I believe the legislation should seek to avoid, to the extent possible, a regime where the competition sets its prices based on the posted prices of the incumbent and where competitors are able to reprice services while tying up the incumbent in the regulatory process. The full benefits of competitive markets will only be realized if regulation is appropriately streamlined. It is important to make these changes now so the regulatory ground rules are clear for all parties in the future. The goal is to have competitors fight it out in the marketplace rather than in the hearing room.

Regulatory Treatment of Investment and Depreciation

The proposed Act would also make important changes in the regulatory treatment of the valuation of property and the depreciation of investment made by public utilities. While it is often said that "hindsight is 20-20," the fact is that firms will not make investments in new technology and new services if they risk having those investments disallowed by regulators after the fact; that is, once the investment has already been factored into rates that the utility is lawfully charging.

While I have not had the opportunity to review the APUC's record in this area, I believe that taking the necessary steps to "unify" the regulatory rules relating to depreciation moves policy in the right direction. These steps are important if incumbent firms are to be permitted a reasonable opportunity to recover the investments they have already made before competition intensifies.

* * *

Overall, I believe "The Alaska Telecommunications Act of 1995" moves public policy in the right direction. It provides for incremental, rather than radical, change and represents a measured approach to modernizing telecommunications regulation in Alaska. As such, the proposed Act is certainly consistent with developments elsewhere and with sound public policy.

STRATEGIC
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TESTIMONY OF
HARRY M. SHOOSHAN III
ON HB 346,
"THE ALASKA TELECOMMUNICATIONS ACT OF 1995"

SEPTEMBER 27, 1995

Mr. Chairman, members of the Committee. I am Harry M. Shooshan, a principal in Strategic Policy Research, a telecommunications consulting firm based just outside of Washington, D.C. I am appearing here this afternoon on behalf of ATU Telecommunications.

Although my complete bio is attached to this testimony, I would like to mention at the outset that I had the opportunity to help develop public policy in telecommunications for over a decade as a Congressional staffer, including six years as chief counsel to what is now the Telecommunications and Finance Subcommittee in the United States House of Representatives. After leaving the Congress, I have worked on issues of competition and regulation for a number of clients in both the private and public sectors. For example, I have just completed a project for the Iowa Utilities Board (the equivalent of the APUC) related to implementation of local competition as mandated by that state's new statute. I have also consulted with the regulatory authority in the United Kingdom. My private-sector telecommunications clients have been primarily local exchange carriers, but I have also done some work with long-distance companies in the United States and Canada on pricing flexibility and regulatory modernization.

I am pleased to have been asked to review HB 346, "The Alaska Telecommunications Act of 1995," and I am delighted to participate in these hearings on such an important measure.

I intend for this testimony to provide a national perspective on this legislation. While I am familiar with the major players in Alaskan telecommunications, I do not appear this afternoon as an

expert on your state and its needs. I consider myself a resource upon which this Committee might draw as you consider the revisions to the Alaska Code proposed in this new legislation.

On the whole, I believe that "The Alaska Telecommunications Act of 1995" provides a sound basis for revamping the Alaska Code to permit efficient competition and will help to usher in an era of "new opportunities" in this state as ATU suggests.

I. Introduction

The only constant in telecommunications today is change. In fact, as one observer noted, the world is changing so fast these days that the person who says it can't be done is generally interrupted by someone doing it. We have come to think of telecommunications, appropriately, as a form of infrastructure which is as critical to today's expanding information economy as roads, airports and shipping channels are to our traditional industrial economy. There have been a number of studies in recent years (some of which I have been privileged to author or coauthor) that have demonstrated beyond doubt that telecommunications matters in supplying tools for economic development. I note that the Alaska 2001 Advisory Committee, chaired by Lt. Governor Ulmer, has nearly completed such a study.

But just as telecommunications matters, so do public policy and regulation. This is because so many of the firms that supply the vital telecommunications infrastructure are regulated. It is a fundamental principle in our free economy that firms respond to incentives. Thus, the incentives provided by the marketplace, or by regulation where necessary as a surrogate for marketplace forces, are important. As the legislature, you have the opportunity to set the direction of public policy in this vital sector and to make certain that regulation provides the right incentives; in this case, incentives to invest, to innovate and to supply quality service at appropriate prices. As competition intensifies, spurred by federal legislation as well as by actions you take here in Alaska, regulation must adapt to the new environment.

As I see it, in the brave new world, the information superhighway will not be some monolithic structure, but rather "a network of networks." Both wired and wireless; terrestrial and satellite. Many of these networks will ultimately be interconnected, with the public switched

network serving as the backbone of the new information superhighway system. The switched network will likely have an important continuing role to play for many customers in providing the on- and off-ramps to the information superhighway.

Furthermore, the lines between industries that have existed in the past as a result of public policy and regulation will increasingly become blurred or will be erased altogether. For example, in the future, the labels LEC, CAP and IXC will be meaningless. We will not think of wireline and wireless as being two different industries, but rather as two different technologies for delivering essentially the same services. Similarly, we are moving to a world where any of a number of companies will be providing video, voice and data, regardless of their origins as cable companies or telephone companies. While the pending federal legislation will speed up this process, I believe these changes will occur whether or not we have a new Communications Act.

Regulatory policy should anticipate these changes and seek to balance the needs of established providers, new entrants and users. In the words of the Alaska 2001 Advisory Committee's draft report to the APUC:

> In markets where competition is found to be in the public interest, state statutes and commission regulations should be amended to provide for an orderly transition to competitive markets in a manner that is fair to all concerned.

I couldn't have said it better.

II. The National Environment

The past few years have been marked by a wide range of activity on the public policy front in telecommunications. This activity includes the consideration, and now likely enactment, of the first complete overhaul of federal telecommunications law in over sixty years.

While a rewrite of the 1934 Communications Act is long overdue, Congress is simply following the lead of a number of state legislatures that have also enacted sweeping new telecommunications laws. These states include Nebraska, Illinois, Virginia, Tennessee, Florida, Iowa, Georgia, Hawaii, Minnesota, North Carolina, New Hampshire, Texas, Utah and Wyoming. In addition to these legislative actions, a large number of state regulatory agencies have acted on their

own to facilitate the transition to competition. Notable among these are New York, Massachusetts, Maryland, Nevada and Washington.

While the details of these initiatives may vary, their goals are the same — to bring regulatory policy up to date and to provide regulatory agencies with the tools they need to cope with rapidly changing markets. The approaches taken in other jurisdictions range from radical (*e.g.*, Nebraska which effectively deregulated telecommunications markets by legislation nearly a decade ago) to more incremental (*e.g.*, Iowa, which left more discretion with the regulatory agency).

The pending federal legislation is far-reaching, although it would leave a great deal of implementation to the Federal Communications Commission (FCC) and to federal/state joint boards consisting of FCC commissioners and state regulators who are selected by NARUC. While there are some important differences between the versions passed by the House of Representatives and the Senate (where Senator Stevens has played a key role in advocating Alaska's unique interests) which will have to be worked out in a conference committee, it is striking how much agreement there seems to be on the direction in which federal policy should go. Both bills remove the lines between industries and open local and long-distance telephone markets to additional competition. Both bills require the interconnection of new entrants, but also provide for streamlined regulation of incumbents. It is also significant that the bills recognize that there are important differences among telephone companies. The bills provide for waivers or modifications of various requirements where they are determined to be economically burdensome or technically infeasible if applied to smaller companies which are not as diversified as the Bell Operating Companies and other large holding companies in terms of geographical coverage or lines of business. It is important to note that ATU would qualify for waivers under either of the two bills; a point to which I will return later in my testimony.

Before giving you my thoughts on the proposed legislation, I want to emphasize the importance of moving ahead here in Alaska. In the first place, there are unique circumstances that exist in this state that should be reflected in telecommunications regulatory policy. This Committee is in a far better position than a Congressional committee in Washington, D.C. (even with Senator Stevens on it) to make certain that these circumstances are addressed in the transition to competition. Secondly, as sweeping as the final federal legislation is likely to be, it retains the concept of dual

jurisdiction. The states will continue to play important roles in developing and administering the competitive policy set out in the legislation. In addition, the states retain complete control in a number of important areas, such as the setting of rates for local service.

You actually may be better off if you have established your own policy in terms of minimizing federal preemption.

Thus, I believe you can and should move ahead without waiting for the enactment of federal legislation. Nor should you be bound in any way by the specific approaches to the various issues taken in the federal legislation . . . or in legislation adopted by other states for that matter. It may be that some of what you do is ultimately superseded by federal legislation or regulation. You cannot determine that outcome. What you can determine is whether or not Alaska has the right public policy for the Information Age. I think the legislation which is before you moves things in the right direction.

III. Putting the Alaska Telecommunications Act of 1995 into Perspective

As I see it, the proposed Alaska Telecommunications Act of 1995 ("the proposed Act") has three essential components. First, it seeks to provide for fair competition in establishing terms for interconnection and for access to essential facilities. Second, it provides for streamlined regulation of new and competitive services. And third, while retaining traditional rate-of-return regulation, it modernizes the regulatory treatment of investment and depreciation.

The proposed Act also provides for discounted rates to schools, health care facilities and other institutions.

In nearly every respect, the proposed Act appears to move Alaska in the direction many other states are already headed. In that sense, it is hardly radical. If anything, the legislation could be characterized as seeking only moderate or incremental change in the status quo. For example, 18 states have abandoned traditional rate-base rate-of-return regulation for some form of price regulation. Another 12 states have paved the way for the adoption of price regulation plans. Some states have adopted even more streamlined regulation than is proposed here. While other states have

taken different approaches to facilitating competition, I believe that the reliance on interconnection in the proposed Act is sound in light of the circumstances that exist in Alaska.

I would like to address each of these essential components in more detail. I will also suggest some areas in which the proposed Act might be improved, including a couple of points that concern me and, at a minimum, should be clarified.

A. Interconnection of Competitors

The existing joint use and interconnection provisions of the Alaska Code provide a good starting place for the implementation of competition. As I read these provisions, telecommunications utilities are already required to provide interconnection to other public utilities as well as to nonutilities where the APUC finds that interconnection to be in the public interest.

I would make four observations about this provision of the Code and about the proposed changes to it.

First, the obligation to interconnect should run both ways; that is, it should be symmetrically imposed on all competitors. If ATU, for example, is obligated to interconnect with a competitor, then that competitor should be required to interconnect with ATU. This symmetrical treatment is important in order to assure the interoperability of competing networks and to ensure that customers of competing providers are able to reach each other.

Second, while some parties will undoubtedly urge you to go further by requiring ATU to disaggregate its network, I am not persuaded that circumstances in Alaska warrant such steps. The critical requirement necessary to ensure competition is interconnection. It is not apparent to me that you need to go beyond that at this time. While other jurisdictions have required unbundling, their rules apply primarily to the Bell Operating Companies and to other large vertically-integrated telephone companies (GTE, Sprint, Frontier, *etc.*). As I noted previously, in pending federal legislation, Congress has provided for waivers of various interconnection requirements for smaller companies that are not similarly situated.

ATU, for example, is not now in the long-distance business. It faces competitors who are large, formidable players in that business, including AT&T and GCI/MCI/BT. These firms operate

successfully in many markets around the world, offer a wide range of services and possess substantial resources that will facilitate their vertical integration into the provision of local telephone service. In fact, these firms have the capability to bypass ATU's network completely to serve a wide range of customers. The legitimate needs of competitors should be determined in part by who they are and by their relative positions in all telecommunications markets. In the current environment in Alaska, requiring the interconnection of competitors is sufficient to permit local competition.

Moreover, you have to be careful not to destroy what I would term "the economies of the firm" which might be the result of requiring ATU to disaggregate its local network. Making "it" easier for competitors to compete may make "it" harder for the incumbent to respond. The imbalance can be even greater where, as here, competitors can rely on their own economies of scope. Removing the legal barriers to entry, providing for access to essential facilities, and requiring symmetrical interconnection are the essentials for permitting expanded competition.

Third, the proposed Act would require that the costs of any modifications or additions needed to facilitate interconnection are borne by the competitors. In principle, this is unobjectionable. However, to the extent that the utility making the modification or addition may also benefit, then it would be appropriate for some of the costs to be shared. For example, local telephone companies benefitted from deploying the digital switches necessary to implement fully "equal access" for long-distance companies. In addition, this language should not be seen as a "blank check" that could lead to increasing the costs of interconnection beyond what is required by prevailing industry practices.

Fourth, I am unclear about the effect of conditioning interconnection on the absence of "injury to the owner or other users of the facilities" and especially about removing the word "substantial." If the intent of the language is to ensure that interconnection itself does not produce technical harm to the incumbent, does not degrade the technical quality of service to consumers and does not require the incumbent to incur costs for which it is not compensated, I think the standard is sound.

However, if the language is read to require the APUC to consider whether competition generally might result in economic harm to a public utility, I am concerned that such language could be used by incumbent firms to block efficient competitors from obtaining interconnection. This would, in my view, be an unfortunate result and, perhaps, an unintended result of this language.

However, there is a fundamental problem with the introduction of competition into a market where incumbent firms are rate-of-return regulated. If a regulated public utility is denied an opportunity to earn a fair return on its investment as a result of competition, the regulators have abrogated an essential element of the traditional social compact. This dilemma is compounded if the regulated public utility is constrained from restructuring its rates in the face of competition and, thereby, from making itself whole.

Other jurisdictions have adopted price regulation as a means of protecting ratepayers, shifting more of the risk to shareholders, and giving the regulated firm at least some latitude to adjust its rates over time.

B. Streamlined Regulation

The streamlined regulatory framework contained in the proposed Act is similar to approaches advanced or adopted in other jurisdictions. At the heart of the changes is a recognition that, as services offered by local telephone companies become competitive, those companies must be able to price such services in a competitive fashion.

The key elements of streamlined regulation in the proposed Act are:

1. A procedure for classifying services (*e.g.*, as "subject to competition"); and

2. Pricing flexibility (including contract pricing) for new services and services subject to competition.

I would like to comment briefly on these important features.

Classification of Services. As competition continues to develop, it is appropriate to tailor regulation to fit the new circumstances. This means allowing the incumbent firm to respond when competition exists for a particular service or group of services. The proposed Act would define a service subject to competition as "a service where a customer may purchase a substitute service from another entity." This is an appropriate standard for classifying competitive services and has been adopted, and is being successfully implemented, in other jurisdictions (*e.g.*, Illinois). It focuses on the availability of a substitute service and not on how many customers may choose to buy the

substitute service (*i.e.*, a measure of market share). The main problem with the latter approach is that it actually penalizes the incumbent firm for being an effective competitor; or put another way, it forces the incumbent to lose share by being unresponsive to customers' needs in order to gain regulatory flexibility.

As I read it, the proposed Act would also permit a public utility to file a request with the APUC to reclassify a competitive service from regulated to deregulated. The filing would have to meet requirements established by the Commission with regard to the treatment of costs and revenues, and the Commission would have 60 days to review the filing and either accept or reject it. This approach provides an appropriate mechanism for ultimately moving competitive services "below the line."

It is also important that firms have the incentive to introduce new services. By providing for streamlined regulation of new services, the proposed Act will encourage regulated public utilities to innovate. Moreover, this approach will prevent a competitor from holding up a new service offering of a rival in order to gain an advantage. While the proposed Act does not define "new service," the term can be presumed to mean a service that is not now being offered. One concern with the classification of new services is that a firm could withdraw an "old" regulated service that is essential to either consumers or competitors and attempt to substitute a new service which it could price as it chooses. As long as a public utility cannot withdraw any comparable existing regulated service without the permission of the APUC, this concern is mitigated, and streamlined treatment of new services is fully justified.

I believe it is also desirable to limit the amount of time the APUC has to consider a classification request. The thirty-day period provided in the proposed Act seems appropriate. This should give the APUC adequate time to make its findings without allowing the process to become bogged down with competitors' objections. Once the Commission has begun to administer this new provision, it can be expected to actively monitor developments in the marketplace. The Commission should generally be well aware of the presence of competitive alternatives and, thus, able to complete its review of a classification request within 30 days. The goal is to have competitors fight it out in the marketplace rather than in the hearing room.

Pricing Flexibility for New and Competitive Services. The proposed Act would permit a public utility to price new and competitive services flexibly, subject to streamlined regulatory treatment. Prices could be set at whatever level the utility — and the market — dictated as long as the price covers the incremental cost of providing the service. Establishing a price floor based on incremental cost is supported in the economic literature and is consistent with the direction that public policy is going in other jurisdictions. The purpose of a price floor is to provide regulatory (in addition to antitrust) protection against predatory pricing by a firm with market power.

The streamlined regulation of competitive services includes shorter notice periods for establishing initial rates (30 days to the Commission and 15 days to the public), shorter notice for changes to existing rates (10 days to the Commission) and the ability to enter into special contracts, subject to filing a notice describing any such contract with the Commission within 10 days after the effective date of the contract. The Commission retains the ability to investigate any rate filing and to fine a public utility for rates that are determined to be below the incremental cost of providing the service in question. Similar streamlining has been adopted by many states over the last 10 years.

While competitors can be expected to argue that incumbent firms should be kept under tighter rein, I believe the legislation should seek to avoid, to the extent possible, a regime where the competition sets its prices based on the posted prices of the incumbent and where competitors are able to reprice services while tying up the incumbent in the regulatory process. Consider the following observation about local competition in the region served by Bell Atlantic made by an executive at Marriott International, Inc. whom I interviewed earlier this year:

> As I see it, there are two problems with [regulation of local competition]: One problem is that the competition fixes their prices based on the level of Bell Atlantic's regulated rates rather than their own costs. The second problem is that Bell Atlantic can't respond competitively to their competition. That is certainly a problem. We have priced access nationwide from competitive access providers for our private-line network. . . . [T]heir pricing is almost universally, *exactly* 10 percent below the Bell Atlantic price. *Exactly* 10 percent. We have written a letter to the Maryland Public Service Commission in which we describe our concerns about these competitive failures. We told the staff of the Maryland PSC that its tariffing regime is a two-edged sword, both edges of which are inhibiting competition: the tariffs restrict the LEC's ability to compete and they simultaneously act as a standard against which the

> alternate carriers fix their prices. We want prices based on true competition among all suppliers, including Bell Atlantic.[1]

This is consistent with the views of nearly 80 private- and public-sector users whom I have interviewed during the last 5 years for a number of studies.

Users want competition. However, they want the existing providers to be free to compete as well. Large users, in particular, highly value special contracts which permit them to make the kind of arrangements with their telecommunications suppliers that they can make with practically every other vendor with which they deal. Moreover, these users highly value the ability to move quickly. As an executive at Safeway, the large grocery retailer, put it:

> When we want to roll something out, we want it to be strategic — fast without announcing a whole lot to the world and, in particular, our competitors. [When our suppliers are regulated] everybody in the world ends up knowing what you are doing long before you are actually able to do it.[2]

The full benefits of competitive markets will only be realized if regulation is appropriately streamlined. It is important to make these changes now so the regulatory ground rules are clear for all parties in the future.

C. Regulatory Treatment of Investment and Depreciation

The proposed Act would also make important changes in the regulatory treatment of the valuation of property and the depreciation of investment made by public utilities. The proposal would establish a rebuttable presumption that once property has been included in rates, it is presumed to be allowed for ratemaking purposes. This approach is becoming standard in utility regulation across the country. Its purpose is to reduce the likelihood of disallowances based on

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[1] *See* John Haring and Harry M. Shooshan III, *Universal Competition in the Supply of Telecommunications Services: Eight Customer Perspectives*, February 8, 1995, p. 36 (interview with Gary L. Helwig, Director of Telecommunications Planning and System Design, Marriott International, Inc.).

[2] Haring and Shooshan, p. 12 (interview with Jerry I. Pesterfield, Director, Information Systems, Safeway, Inc.).

retroactive review by regulators. While it is often said that "hindsight is 20-20," the fact is that firms will not make investments in new technology and new services if they risk having those investments disallowed by regulators after the fact; that is, once the investment has already been factored into rates that the utility is lawfully charging. Given the heightened risks resulting from expanded local competition, public utilities that also face the risk of disallowances will be likely to make only minimal, "safe" investments. As a result, consumers who rely on that utility may find themselves with fewer choices in the short run and even declining service quality in the long run. The proposed language would put the burden of proof on the Commission if it chose to disallow such investment for any reason.

Regulation has also controlled the rate at which a utility's investment can be recovered in the prices it charges consumers. This has been accomplished through a set of complicated formulas relating to estimates of how long plant will be "used and useful." Because telephone plant is subject to federal and state regulation (it is used to provide both interstate and intrastate services), the depreciation rules that govern telecommunications utilities in Alaska are set by both the FCC and the APUC. The proposed Act establishes a rebuttable presumption that the rates and methodologies accepted by the FCC should apply to telecommunications utilities in Alaska. In general, the FCC has moved more quickly than the states to adopt depreciation rules that are consistent with changing markets and changing technology. While I have not had the opportunity to review the APUC's record in this area, I believe that taking the necessary steps to "unify" the regulatory rules relating to depreciation moves policy in the right direction. These steps are important if incumbent firms are to be permitted a reasonable opportunity to recover the investments they have already made before competition intensifies.

IV. Summary and Conclusion

Overall, I believe "The Alaska Telecommunications Act of 1995" moves public policy in the right direction. It provides for incremental, rather than radical, change and represents a measured approach to modernizing telecommunications regulation in Alaska. The proposed Act seeks to achieve fair competition, especially in light of the relative capabilities of the major players. It

recognizes the need for streamlining regulation and for ultimately withdrawing it altogether as markets become increasingly compctitive. As such, the proposed Act is certainly consistent with developments elsewhere and with sound public policy.

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Before co-founding Strategic Policy Research, Inc. (SPR), Mr. Shooshan served for eleven years on Capitol Hill. He was chief counsel and staff director of the Subcommittee on Communications, U.S. House of Representatives and was active in congressional efforts to reform the nation's communications laws. After leaving government, he established his own consulting practice and, as a private attorney, participated in the settlement of the Justice Department's antitrust suit against AT&T, subsequently editing a book on the AT&T divestiture.

Mr. Shooshan specializes in communications public policy analysis, regulatory reform, the impact of new technology and the legislative process. He is the author of numerous studies and articles dealing with issues facing the telephone, broadcasting, public broadcasting, cable television and motion picture industries. He is one of the nation's leading authorities on telecommunications infrastructure and its relationship to economic development and to the global competitiveness of U.S. businesses. Mr. Shooshan has testified before several congressional committees, before the Federal Communications Commission (FCC) and several state commissions. He has presented many papers at regulatory conferences, and has spoken frequently to business and government groups.

From 1976 to 1991, he was an adjunct professor of law at Georgetown, teaching regulation and communications law.

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EMPLOYMENT

	STRATEGIC POLICY RESEARCH, INC. — Bethesda, Maryland
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PROFESSIONAL ACTIVITIES

Member, American Bar Association; Forum Committee on Communications Law; Federal Communications Bar Association; Western Economic Association International

TESTIMONIES

Testimony before the Office of the King County (Washington) Hearing Examiner in the matter of Renewal of King County Television Franchises of TCI Cablevision of Washington, Inc. On behalf of King County Office of the Prosecuting Attorney. July 14, 1995.

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"Local Competition: The U.S. Experience." Presented at *Communications, Law and Policy: Current Issues,* a national symposium sponsored by the Law Society of Upper Canada and the Canadian Bar Association. Ottawa, Ontario, Canada. May 6, 1994.

"Regulation and the Market Place in the Convergence Era — Responding to the Needs of the Users and Consumers." *Reinventing State Regulatory Structures in the Convergence Era. What Model Can Work Best? And Why?* An Exchange of Views Conference, Vol. 10, No. 5 of the KMB Video Journal. The Don CeSar, St. Petersburg, Florida. May 2, 1994.

With John Haring. "Cost-of-Capital Adjustments in a Price-Cap Model." Paper prepared for presentation at New Mexico State University, College of Business Administration and Economics, Center for Public Utilities, Current Issues Conference. Santa Fe, New Mexico. March 13-16, 1994.

"Overview — Redefining Universal Service." *Telecommunications Reports* Universal Service Conference. Washington, D.C. February 1, 1994.

"Industry and Washington Updates." *The Future of Interactive Communications*, San Diego Communications Council Conference. San Diego, California. December 16, 1993.

"Reconciling Divergent User Needs and Regulatory Policy." Twenty-Fifth Annual Conference, Institute of Public Utilities. Williamsburg, Virginia. December 13, 1993.

Panelist, "State Regulatory Responsibilities and New Opportunities in the Age of Restructuring and Uncertainty." The KMB Video Journal, The Eleventh Invitational Conference. St. Petersburg, Florida. November 30, 1993.

"Competition and the Obligation to Serve; the Cost of Universal Service." National Association of Regulatory Utility Commissioners, 105th Annual Convention and Regulatory Symposium, "Meeting Consumer Demands as Competition Grows." New York, New York. November 15-18, 1993.

Responder, "Public TV and Public Access: Bringing Home the Electronic Highway." Symposium jointly sponsored by the Lyndon Baines Johnson Library, the LBJ School of Public Affairs, the Public Broadcasting System and the Alliance for Public Technology. Austin, Texas. November 5, 1993.

"Evolving Technology Equals Emerging Competition Squared." Remarks presented before the Ohio Telephone Association, 98th Annual Conference. Cincinnati, Ohio. September 21, 1993.

With John Haring. "The $20 Billion Impact of Local Competition in Telecommunications." Presented at the National Association of Regulatory Utility Commissioners Symposium. San Francisco, California. July 28, 1993.

"Has Traditional Regulation Outlived its Role in Telecommunications?" Presented at New England Conference of Public Utilities Commissioners, 46th Annual Symposium. The Balsams, Dixville Notch, New Hampshire. June 29, 1993.

"A New Public Policy for Changing Markets and Technology." Remarks at the Florida Telephone Association 86th Annual Convention. Belleview Mido Resort Hotel, Clearwater, Florida. June 8, 1993.

"Telecommunications Public Policy: How We Got Here." Panelist at United States Telephone Association Congressional Staff Seminar, *The Public Policy Challenge: Adapting*

Regulation to Changing Markets and Technology. Williamsburg, Virginia. June 3-4, 1993.

Panelist, "The Wireless World and Its Relationship to the Wireline Infrastructure." The KBM Video Journal. St. Petersburg, Florida. April 19-21, 1993.

"Challenging Times . . . Achieving Our Regulatory Goals." Speech presented to GTE Telephone Operations — South Area Key Management Meeting, *Challenging Times . . . Challenging Issues.* Tampa, Florida. March 17, 1993.

"A Competitor's View of Market Opportunities." Panel moderator at United States Telephone Association's National Issues Conference, *Responding to Competition.* Washington, D.C. February 17, 1993.

"Telecommunications Infrastructure: Responding to Customers' Needs." Panelist, KMB Video Journal — Ninth Invitational Conference. Innisbrook Conference Center, Tarpon Springs, Florida. October 29, 1992.

"The Future of Telecommunications in the Information Age." Speech presented to the GTE South Area Public Affairs Conference, *Business As Usual: NOT!.* Haines City, Florida. October 6, 1992.

"Strategy for the 21st Century: Diversifying in a Competitive Marketplace." Presented before the National Association of Broadcasters Television Group Executive Forum, Washington, D.C. October 2, 1992.

"Incentive Regulation: Where, Why and How." Presented before the 15th Annual Conference of Regulatory Attorneys. Columbus, Ohio. May 6, 1992.

"Telecommunications Infrastructure in the 1990s: The Role of the Public Switched Network." Presented before the National Council of State Telephone Association Executives. Colorado Springs, Colorado. May 4, 1992.

"Electronic Highways: Providing the Telecommunications Infrastructure for Pennsylvania's Economic Future (A Study Prepared for the Pennsylvania Chamber of Business and Industry by NERA and Price Waterhouse), Distinctive Features and Key Findings." Presented before the Institute of Public Utilities, Twenty-Third Annual Conference. Williamsburg, Virginia. December 10, 1991.

"The Changing Scene of State Regulation: Trends and Implications." Presented at a public forum conducted by the Wisconsin Public Utility Institute, University of Wisconsin-Madison campus. Madison, Wisconsin. December 6, 1991.

"Understanding the Role of Communications in an Information Economy and Information Society." Presented before the Annual Seminar on Foreign Policy, Junior Council on World Affairs. Cincinnati, Ohio. November 23, 1991.

"The Revolution in Communications and the Challenges for Peace, Democracy and Economic Progress." Presented before the Issues for Business Luncheon sponsored by the Cincinnati Council on World Affairs and hosted by Star Bank. Cincinnati, Ohio. November 22, 1991.

With John Haring. "Economic Policy Analysis of Cable Compulsory License." Presented before the Board of Directors of the Motion Picture Association of America. Los Angeles, California. October 22, 1991.

"Telecommunications Infrastructure: Building the Electronic Highway for the 21st Century." Presented before the GTE Common Ground Workshop. Madison, Wisconsin. October 8, 1991.

"Electronic Highways: Bringing America Together." Presented before the Mid-America Telecom Showcase & Seminar. Kansas City, Missouri. October 7, 1991.

"Cable Television Companies and Telcos: Customers or Competitors?" Presented to Northern Telecom's Business and Consumer Marketing Forum. Tucson, Arizona. October 2, 1991.

"Competition & Change in Europe's Telecommunications Markets." Panel discussion at Third *Economist* Conference. London, England. September 16, 1991.

"Modernizing Regulation: The Incentives for Investment in Telecommunications Infrastructure." Presented before the 69th Annual Convention of the Georgia Telephone Association. Savannah, Georgia. June 18, 1991.

"Telcos and the Information Economy: Meeting the Challenges of the 1990s." Presented before the Wisconsin State Telephone Association, 81st Annual Convention. The Abbey, Fontana, Wisconsin. May 21, 1991.

"Beyond Incentive Regulation: The Challenge Facing Telephone Companies in Competitive Markets." Presented before the Tennessee Telephone Association. Hilton Head, South Carolina. April 11, 1991.

"Benefits of Lifting the MFJ Restriction on Information Services." Remarks before the MFJ Symposium sponsored by the Public Utility Commission of Ohio. Columbus, Ohio. January 25, 1991.

"Worldwide and Domestic Economic Development Through Communications." Presented before the Lt. Governor's Conference on Telecommunications, sponsored by the Indiana Department of Commerce and the Indiana Telephone Association, Inc. Indianapolis, Indiana. November 29, 1990.

"Telecommunications Infrastructure: A Framework For Public Policy Analysis." Remarks prepared for Bellcore's Seventh Issues Management Fall Conference. Florham Park, New Jersey. October 1, 1990.

"Changing Technology and Converging Markets: U.S. Telecommunications in Transition." Presented at The Integration of Telecommunications and Broadcasting Conference sponsored by The Economist Conference Unit. London, England. September 17-18, 1990.

Remarks on Telecommunications Infrastructure. Prepared for the Northeast-Midwest Institute Leadership Council. Washington, D.C. September 13, 1990.

Panel discussion on the nature of the relationship between telecommunications and state economic development. The Council of State Governments' Eastern Regional Conference. Manchester, New Hampshire. July 31, 1990.

With John Haring. "The Demand for Information Services and the Case for Regulatory Reform in Telecommunications." Presented to the Bellcore/Bell Canada Industry Forum. Hilton Head, South Carolina. April 1990.

With Jeffrey H. Rohlfs. "Will Price Caps Correct Major Economic Flaws in the Current Regulatory Process?." Presented at the Twentieth Annual Williamsburg Conference. Williamsburg, Virginia. December 5-7, 1988.

"Exercise of Congressional Influence Vis-à-vis the FCC and Judge Greene: Some Changing Relationships." Presented at the Northern Telecom Law Department Seminar. Pebble Beach, California. May 13-15, 1988.

With Jeffrey H. Rohlfs and Susan W. Leisner. "The Negative Effects of Tax Reform on the Telephone Industry: Making Up the $15 Billion Difference." Presented at the Fifteenth Annual Telecommunications Policy Research Conference. Airlie, Virginia. September 27-30, 1987.

"Mass Media and the First Amendment: Separate but Unequal." Presented to the Association for Education in Journalism and Mass Communication 1984 Convention. Gainesville, Florida. August 1984.

Remarks prepared for the CBA Legislative Workshop. 1984.

Remarks prepared for the National Commission on Free and Responsible Media. Washington, D.C. February 28, 1984.

"Local Distribution in the New Telecommunications Era: Nature and Extent of Regulation." Presented to the Workshop on Local Access: Strategies for Public Policy. Ad Hoc Committee on Access. Chase Park Plaza Hotel. St. Louis, Missouri. September 14-17, 1982.

"Cable and Enhanced Services: Legal and Regulatory Barriers." Presented to EASCON '81. Washington, D.C. November 18, 1981.

"From the Crystal Ball to the Real World." Presented to the 1981 Convention of the Associated Press Managing Editors. Toronto, Ontario, Canada. October 20, 1981.

"A New Federalism: Federal/State Regulation in the Competitive Era." Presented to the Seventh Annual Rate Symposium of the Institute for the Study of Regulation. Kansas City, Missouri. February 9, 1981.

Remarks prepared for the Technical Committee on Media of the White House Conference on Aging. New York. January 14, 1981.

September 22, 1995

Executive Summary

Mr. Chairman, Members of the Committee
Thank you for this opportunity to discuss HB 346.

My name is Mark Foster. I served in the consumer and engineering seats on the Alaska Public Utilities Commission from 1990 through the end of 1993. I was President of the Western Conference of Public Utility Commissioners and Chair of the Telecommunications Committee.

Since then I have been involved in a variety of consulting engagements including natural gas feasibility studies, electric generation and transmission studies, and work for GCI, ATU and commercial customers.

Today, I appear on behalf of ATU.

Overall, HB 346 represents an incremental first step:
- away from a "command and control" regulatory structures based on *statutes which have remained substantially unchanged since the 1970's*
- toward the 1990's where telecommunications *markets* are becoming increasingly competitive, and legislators and regulators across the country are streamlining regulation to create incentives to invest.

This bill streamlines the regulatory *process* in an attempt to provide for fair competition and allow competitors to fight it out in the marketplace, not in the hearing room.

As a former Commissioner, I find one of the more troubling aspects of regulation is the question of cost effectiveness. I am familiar with cases where the regulatory process led to hundreds of thousands and in some cases millions of dollars being spent on staff, consultants and lawyers to fight pitched hearing room battles that yielded few benefits.

This regulatory burden is ultimately paid for by all of us through higher rates and regulatory incentives which *discourage* innovation and investment.

Given Alaska's unique geography and our increasing connection to a global economy, reforms aimed at reducing regulation and providing a vital robust telecommunications sector are vital.

This bill takes some important steps along that path by:

- reducing unnecessary regulation
- allowing *consumers* and not the government to pick winners and losers

What is does not do:

- It does *not* guarantee competitive outcomes; it reduces regulation and lets the market determine the winners and losers.
- It does *not* guarantee that rates will remain unchanged; as competitive markets emerge, rates that have historically been subsidized are likely to experience upward pressure.

The legislation provides opportunities for success and failure for both competitors and consumers.

Sectional Highlights

Consistent with the legislature's approach in long distance competition, the *proposed legislation provides the APUC with discretion and flexibility to deal with changing circumstances.*

Section 2. Findings
These findings are based in part on the findings the legislature developed in 1990 in conjunction with long distance competition. (AS 42.05.800)

Section 3. Common Carrier
This section is amended to make it consistent with other sections of the statute concerning rates -- the "just and reasonable" standard.

Section 4. AS 42.05.191. Format of Orders
This amendment requires the commission to *format* its orders to clearly state its factual findings and legal conclusions. This is common practice at many state commissions. It provides the public with a better understanding of the basis of the Commission's decisions.

Section 6 & 7. AS 42.05.301 & 306 Discrimination in Service/ Discounts for Public Purposes
§301(a) is the general rule against *undue* discrimination in service.

§301(b) allows the utility to offer a new service on a trial basis to selected customers. This allows the utility to do field testing (engineering and marketing) of new services to target groups prior to any requirement to provide the new service to all customers.

§306(b) allows the utility to offer reduced rates to schools, universities, libraries, health care facilities, museums, public broadcast stations, public safety facilities, and other public institutional communications users.

I am concerned that the existing statutes effectively preclude the utility from offering discounts to schools for Internet access lines. Keep in mind, that if the school cannot otherwise afford the service, by offering the service at a discount, the utility can spread its fixed overhead over more customers and all ratepayers benefit.

Section 8 & 9: AS 42.05.311(a) Joint Use & 311(b) Interconnection:
There are two basic questions in these statutory provisions:

1. Under what conditions should joint use and interconnection be allowed?
2. Who should pay for the changes involved?

Who should pay? The language proposed here in 311(b) simply copies the existing language from 311(a) and states that the entity requesting modifications should pay for those modifications.

Under what conditions should joint use and interconnection be allowed? The proposed amendment would allow interconnection when the interconnection was not detrimental to the utility, existing customers or existing services.

Sections 10 & 11. AS 42.05.321 Commission role in settling interconnection disputes.
In the event of disputes over interconnection, the Commission may intervene to:

- require interconnection when the interconnection is not detrimental to the utility, its existing customers or existing services and
- settle disputes over price.

Section 12. AS 42.05.361 Filing and Inspection of Contracts:
In general, all rates and contracts offered by a utility are required to be on file with the APUC. In competitive markets, this allows competitors to not only see the move of the regulated utility *ahead of time*, but allows them to use the regulatory process to slow down and in some cases render ineffective legitimate competitive activity and first mover advantages.

The proposed change would allow a utility to negotiate and execute a contract for competitive services prior to disclosing the terms and conditions to the APUC and competitors. This would allow a practice that is similar to those in place in Colorado and Wisconsin.

This is especially important where a regulated utility is in competition with an unregulated entity. The unregulated entity can change prices and negotiate contracts without any requirement for *prior approval* by a third party. This amendment would bring regulated and unregulated firms closer to parity in competitive markets.

Section 13. AS 42.05.391 Discrimination in Rates:
In general, the statute prohibits "undue discrimination." This standard allows for "due" discrimination, i.e., discrimination based on some defensible rationale.

The proposed language explicitly identifies practices that are considered allowable as "due discrimination."

This section provides *explicit* statutory authority to the Commission to support policies developed under the old "liberally construed" authority which must now be reexamined under the "reasonably implied" authority passed last session by the Legislature.

Service subject to competition
This establishes the allowable price floor at the incremental cost of providing service to protect monopoly customers against cross-subsidy and protect competitors against predatory pricing. Examples of this practice include:

- Homer Electric Association re: Kenai Peninsula Refineries
- Alaska Electric Light & Power re: Juneau Area Mining Projects of Affiliated Interests
- Alascom re: Private Line and Special Contracts
- Local Exchange Carrier re: Special Access
- ATU re: competitive services (voice mail, centrex)

In summary, the Commission has historically allowed utilities to price down to the incremental cost when a service was subject to competition. The proposed language would provide explicit authority for that practice.

New service
Where new services are introduced, this would allow them to be priced at or above their incremental cost. Under the old regulatory regime, new services

were priced on a fully distributed cost basis, which may have been too high to develop a new market. Consequently new services may not have reached their full revenue potential or in some cases even introduced. By allowing pricing flexibility, the utility can take advantage of price points where more customers will purchase the service. This provides a "win-win" situation for the utility. It generates more revenue and a higher contribution toward common costs which helps keep other rates lower than they would have been otherwise.

This provides the utility with an incentive to introduce new services and develop new markets.

Waive the nonrecurring charges

The Commission has routinely granted requests to waive the nonrecurring charges for nonessential services as part of a promotional offering. Matanuska Telephone Association has often waived the sign-up fees for custom calling features (call forwarding) as part of a promotion to get more customers to sign up for these value-added features. This amendment would provide explicit statutory authority for that practice and expand it to include competitive services.

New service on a trial basis to selected customers

This would explicitly provide statutory authority to allow utilities to offer new services on a trial basis to selective customers. This will encourage the introduction of new services and products and greater experimentation by the utility in its efforts to meet the needs of its customers.

Sections 14 & 15: AS 42.05.411 New or revised tariffs for Services Subject to Competition:

Firms need flexibility to respond to the marketplace. To be *provided an opportunity to compete*, firms simply cannot wait for the regulatory process to churn through paperwork under old outdated time frames.

The proposed timeframes for competitive services provide modest reductions from existing statutes and are reasonable in light of what the

Commission adopted for the Alaskan long distance market and what has been in place in other states since the mid-1980s in some cases.

Section 16. AS 42.05.421(a): Suspension of tariff filings.
These sections limit the time period that the APUC can hold a filing in "suspension" before it is either rejected, modified, or approved.

The proposed language would limit that period to *six* months for rule changes.

It would limit revenue requirement and rate design to *six* months before the interim requested rate went into effect, and *twelve* months before the permanent rate went into effect.

The basic time frames have not changed in this section. The Commission's authority to extend the time a filing can be held in "suspension" is eliminated.

This is particularly important given the Commission's history. Under the existing statutes, the Commission's authority to suspend a filing five times, constituting a 22-month suspension was upheld in court. This is an unreasonable regulatory burden for any firm, especially in light of the pace of change in telecommunications markets today.

Section 17. AS 42.05.426 New or Competitive Services.

Subject to Competition Determination
In respond to a utility request, the Commission is required to make its determination about whether a service is subject to competition within 30 days of the filing. If a service is subject to competition, this still gives competitors at least 30 days notice that a utility is seeking flexibility in a particular market.

Is this enough time for the Commission to make a determination? Based on historic practice, this appears to be within the reasonable range.

The Commission has already made determinations about the competitiveness of telecommunications markets. Examples special access, Centrex, and voice mail markets. These determinations did not take a lot of time. Keep in mind, the burden still rests with the utility to make its case by filing information which demonstrates to the Commission that a service is subject to competition.

Just and Reasonable Findings

The Commission still has *six* months to make its findings regarding the appropriateness of the terms and conditions of a new or competitive service.

Request for Deregulated Treatment

The utility may file to offer a service that is subject to competition as a deregulated service. The Commission is required to adopt regulations governing the reclassification of a service from regulated to deregulated.

Section 18. AS 42.05.436 **Rates** for New or Competitive Services.

This section requires that the rate for a new or competitive service shall be at or above the incremental cost of providing the service to ensure that the service makes a contribution toward common costs.

If the Commission, after investigation and hearing, finds that a rate is below the incremental cost of service, it is *required* to ask the utility to defend itself against a fine for offering the service below cost!

This risk of fines and public notoriety provides the utility with a powerful incentive to price services above their incremental costs; protecting customers from cross-subsidy and competitors from predatory pricing.

Section 19. AS 42.05.441 Valuation of property

The new subsection (d) establishes a rebuttable presumption that once property has been included in rates, it is presumed to be allowable for ratemaking purposes.

This provides an incentive for the Commission and intervenors to make their case about whether a particular investment should be included in rates

when it is first included in a rate case. When an item is first included in a rate case, the utility still carries the burden of proof to justify the item as reasonable. After an item has been allowed into rates, the entity seeking to exclude an item from rate base carries the burden of proof.

This keeps the utility from continually having the carry the burden of proof to justify items that it has previously justified.

Section 20. AS 42.05.471 Depreciation Rates

This subsection establishes the rebuttable presumption that the depreciation rates and methodologies accepted by the Federal Communications Commission are reasonable. The costs involved in keeping different books for both the State and Federal regulators is not likely to be worth the effort. Nonetheless, intervenors still have the opportunity to challenge the FCC regulation and demonstrate another system will benefit the public.

Section 21. AS 42.05.671 Competitively Sensitive Information

This explicitly requires cost and marketing information for new and competitive services to be treated as privileged records that are not generally available for public inspection, except for "in camera" review.

Section 22. AS 42.05.990 Definition of Subject to Competition

A new definition is added to establish the legal standard for when a service is considered competitive. When a customer has an opportunity to purchase a substitute service from another entity, the service is considered competitive.

This is consistent with several Commission decisions:

Alascom Private Line
ATU Voice Mail
ATU Centrex

In addition, the Commission has allowed rate flexibility for special access for several LECs.

Providing flexibility to the Commission to examine markets as they become competitive is the best way to meet the goal of drafting legislation that will stand the test of time and not become obsolete or unduly advantage one party over another. Attempts to develop a detailed definition which reflects the fashion of the day are more likely to generate future requests for statutory modifications.

Summary

Because telecommunications utilities supply a critical service for most sectors of the economy, the performance of the telecommunications sector has an important influence on the performance of the entire economy.

The performance of the telecommunications sector, in turn, is influenced heavily by the regulations imposed on the utility firms.

Progress on regulatory reform for telecommunications is long overdue in Alaska. Without regulatory reform, the performance of the entire economy may well be diminished.

Overall, this bill represents an incremental first step toward:

- streamlining regulations
- providing positive incentives to the industry to invest in new and competitive markets
- providing protections for consumers and competitors.

Thank you.

I am happy to answer any questions you may have.

Mark A. Foster

P.O. Box 200587
Anchorage, Alaska 99520
(907) 272-0207

EXPERIENCE

1994-current	**Mark A. Foster & Associates (MAFA)** Juneau and Anchorage, Alaska *Principal*
1990-1993	**Alaska Public Utilities Commission** Anchorage, Alaska *Commissioner*
1989	**Salem Technical Services/Raytheon Support Services** Anchorage, Alaska *Senior Engineer*
1986-1989	**Engineering Department, City of Fairbanks** Fairbanks, Alaska *Engineer II, Engineer I*
1984-1986	**Ebenal General, Inc.** Fairbanks, Alaska *Vice President, Project Manager*

EDUCATION

1983-1987	**University of Alaska, Fairbanks** Graduate studies in Arctic Engineering and Operations Research
1983	**Stanford University, B.S., Civil Engineering**

PROFESSIONAL LICENSE

Professional Civil Engineer, State of Alaska, CE 7742

PROFESSIONAL EXPERIENCE

MARK A. FOSTER & ASSOCIATES
Principal — 1994-current

Consultant specializing in regulatory, engineering, and economic analysis of utility and pipeline proposals. Clients have included utilities, business customers, government and non-profit agencies.

Engagements include:
Local Telephone Company Regulatory Support
Long Distance Telephone Company Access Charge Review
Natural Gas Utility Feasibility Studies
Electric Intertie Feasibility Studies
Electric Generation and Transmission Reconnaissance Studies

ALASKA PUBLIC UTILITIES COMMISSION
Commissioner — 1990-1993

Appointed by Governor, confirmed by the Legislature. Served in consumer and engineering seats on the Commission. Responsible for rate and quality of service oversight of telecommunications, electric, water, sewer, and refuse utilities and pipeline carriers throughout Alaska.

Telecommunications Highlights

As a Commissioner, I was actively involved in the following dockets:

Interexchange Carrier Competitive Market Structure
Interexchange Carrier Special Contracts/Private Line Services
Local Exchange Carrier Rate Cases & Certification
Extended Area Service (EAS)
Telecommunication Relay Services
Privacy Principles
Cable TV Rate & Service Regulation
AT&T/Alascom Joint Services Agreement

Professional Activities

President, Western Conference of Public Service Commissioners
Chair, Western Conference Telecommunications Committee
National Association of Regulatory Utility Commissioners Finance and Technology Committee
Liaison, NARUC Staff Subcommittee on Technology

LEGISLATIVE TELECONFERENCE NETWORK

SIGN-IN SHEET

50795

SPONSOR: House Labor + Commerce — P.M.

SUBJECT: HB 346 - Telecomm. Utilities

START/END TIME: DATE: 9/27

PLEASE PRINT

	Name/Representing		Address	Zip	Phone No.	Testify	Observe	Bill No.
1.	[illegible]	APUC	1016 W 6th #400	99501	276-6222	[illegible]	[illegible]	346
2.	Bob Lohr	APUC	" " "	99501	276-6222		X - Will answer questions	346
3.	Greg Berberich	MTA	1740 S CHUGACH	99645	745-9466		X	346
4.	Tom Edrington	ATU	600 Telephone Ave	99503	564-1415	X		346
5.	Mark Foster	ATU	P.O. Box 200587 Anchorage	99520	272-0207	X		346
6.	Dwight Ornquist	APUC	1016 W 6th #400	99501	2766222			346
7.	TIM BENINTENDI / REP. C. MOSES		716 W. 4TH AVE # 660, ANC	99501	258-8167	X		346
8.	JAMES BOWE	ATA	4341 B ST. SUITE 304	99503	563-4000	X		346
9.	KRISTI JUMPER	AT&T Alascom	210 Bluff Drive Anch. AK	99501	264-7035		X	346
10.	Ted Moninski	AT&T Alascom	" " " " "	"	264-7876	X		346
11.	[illegible]	GCI	2550 Denali St Anch Ak	99503	265-5545	X		346
12.	Steve Hamlen	United Utilities	5450 A Street	99511	273.5210	X		346
13.	Ray Gillespie	AK-Alascom	9478 RIVERBEND CT JUNEAU AK 99801	99801	463-2325		X	346
14.								
15.								

HB

363

RESOLUTION

WHEREAS the continued long-term health of Alaska's economy is reliant on the strength and vitality of our residential housing market; and

WHEREAS the primary source of funding for home loans is through nationally established secondary markets; and

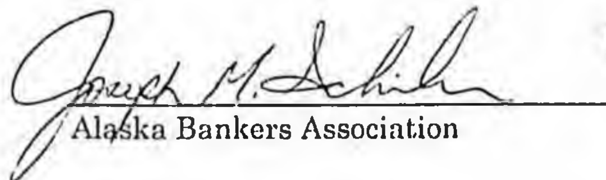
WHEREAS all citizens of the state benefit through lower interest rates and lower costs when the home lending industry is fully competitive; and

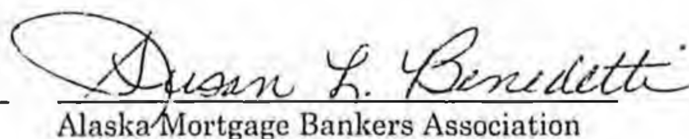
WHEREAS the House State Affairs Committee and Labor and Commerce Committee have been provided substantial written and oral testimony opposing the passage of House Bill 363 "Interest on reserve accounts";

THEREFORE, THE UNDERSIGNED ASSOCIATIONS HEREBY RESOLVE that any minimal benefit to the consumer by providing interest on mortgage reserve accounts and/or additional reserve account disclosures are far outweighed by the detrimental effect of reduced competition and a local as well as a national market place forced to adjust their home loan pricing to accommodate the increased cost.

IT IS FURTHER RESOLVED that recently enacted federal regulations impose more than adequate requirements on mortgage loan servicers to prevent over escrowing of funds for the payment of taxes and insurance and to ensure complete disclosure to the customer.

IT IS FURTHER RESOLVED that it is the unanimous desire of the home lending community that CS H.B. 363 "Interest on reserve accounts" not be passed due to the profound negative effects the law would have on the housing industry and the Alaskan consumer.


Alaska Bankers Association


Alaska Mortgage Bankers Association

03/20/96

National Bank of Alaska

Mortgage Loan Department P.O. Box 107025 Anchorage, Alaska 99510-7025 (907) 257-3434 Fax (907) 257-3412
1500 W. Benson Blvd. Fourth Floor Anchorage, Alaska 99503-3656

February 27, 1996

Pete Kott, Chair
Norm Rokeberg, Vice Chair
Labor and Commerce Committee

Re: CS for House Bill 363

Dear Representatives Kott and Rokeberg:

CS for House Bill 363 would require banks to pay interest on the reserve accounts held for payment of taxes and insurance on mortgage loans. Part of the testimony on HB 363 before the House State Affairs Committee was a letter from Craig Ingham, President of Mt. McKinley Bank in Fairbanks. We are in agreement with Mr. Ingham's letter. We cannot emphasize enough the negative impact this legislation could have on the mortgage banking system in Alaska.

An issue not raised by Mr. Ingham, but of importance, is whether this legislation would be binding on servicers based outside Alaska. If Outside institutions are affected, they will then choose whether it is worth their while to continue to service loans originated in Alaska. If they choose to continue buying loans, they may reduce the amount they pay local lenders for the loans. One large Outside purchaser of mortgage loan servicing has advised us they are just completing an extensive internal cost analysis, and they have concluded that they will pay .30 basis points less for loans in states which require interest on the reserve accounts. This cost will, of course, be passed on to the consumer in the form of higher fees or higher interest rate. On a typical $100,000 loan, a consumer could be paying $300.00 at closing to gain back a very small amount of taxable interest income per year.

Some lenders will choose not to do business in Alaska. Many lenders suffered large losses in the mid-eighties real estate recession; any negative impact on income may well be enough to influence a decision to not purchase Alaska mortgages. Borrowers benefit from a competitive environment for mortgages and would be the losers if Alaska loans become unattractive to Outside lenders.

If Outside servicers would not be required to pay interest, then Alaska servicers will have a state-mandated higher cost of doing business than companies with headquarters outside Alaska. This uneven playing field could influence Alaskan lenders to 1) discontinue mortgage lending operations, or 2) sell loans on a servicing-released basis to Outside companies which are not affected by the law or 3) move the servicing operations outside the state of Alaska. These three events all lead to lost jobs for Alaskans.

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The current version of the bill requires payment of interest by "banks" (mortgage companies and credit unions are large originators of mortgage loans but are not mentioned in this bill) for reserves "in excess of those required to be held by federal regulations". Federal regulations do not require banks or other mortgage lenders to hold reserves; RESPA (Real Estate Settlement Procedures Act) does prohibit lenders from holding excess funds in reserve accounts. The secondary market has set the standard on holding reserve accounts for taxes and insurance as a way of reducing risk on the loans; not all borrowers have the financial discipline to set aside savings to meet the large payments needed for taxes and insurance on an annual basis.

Fourteen states have passed legislation regarding interest on reserve accounts. Most of the laws were passed in the 1970's and 1980's and were in response to some abuses. We are not aware of any complaints of abuses in Alaska. The most recent state law was passed in 1992.

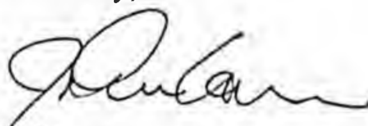
Congress addressed the treatment of reserve accounts on a national level, and passed an amendment to RESPA in 1994 which became effective in 1995 and which affects all servicers of mortgage loans. The amendment to RESPA requires implementation of aggregate analysis of reserve accounts which replaces the previously used single-item analysis. The law is specific in how a lender can treat reserves, when a lender is allowed to pay funds out of the reserve account, and how much funds can be accumulated; it requires reimbursement to the borrower of funds in excess of that allowed by the federal formula. The law has specific disclosure and reporting requirements.

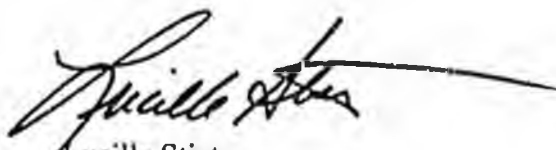
Nationwide, lenders implemented the RESPA changes in 1995; results are not known, but many lenders feel more borrowers will have a shortfall in the reserve account after payment of annual taxes. This will result in lenders making, in effect, interest free loans to borrowers on the shortfall as lenders advance funds to pay the taxes (and insurance) and receive reimbursement from the borrower over a period of time.

This bill appears aimed at a problem that does not exist. We strongly recommend a do not pass on this bill.

If there are any questions, of if we can provide further information, please feel free to call on us.

Sincerely,





John Carman
Vice President

Lucille Stietz
Sr. Vice President

Not Constituents

15646 Southpark Loop
Anchorage, Ak. 99516
Jan. 3, 1996

To: Rep. Con Bunde
Fax 4653871
Re: Escrow Account Interest

Dear Mr. Bunde:

After reading the following article, (Bottom Line, Volume 17, Number 1; Jan. 1, 1996) I wondered if this issue is one that might involve legislative action. As I have not called any lender other than our own (City Mortgage) I don't know if this policy differs among the Alaskan lenders. At any rate, I cannot un[illegible]erstand why any lender is entitled to earn interest on this money.

I wish you a successful legislative session.

Sincerely,

Carol C. Lewis

Carol C. Lewis

• **Get refunds and reduced payments from your escrow/impound account.** This is a separate account held by the mortgage lender that you pay into each month for the property taxes and hazard insurance the lender pays for you. It is called an "impound account" in California and the West. New federal rules introduced in 1995 say that lenders...

...cannot require more than two months' payments as a cushion. Some now require cushions of four months or more, which is illegal.

...must send you a statement early in the year projecting how much escrow payments could increase. A year-end statement will compare projected and actual payments.

...must consider money already in the account when calculating the monthly payment for the coming year—resulting in lower payments for most home owners.

Strategy: Find out how much is in your escrow account by checking your monthly statement or calling your lender. If the lowest balance during the year is more than twice your monthly payment—principal, interest, taxes and insurance—complain to the lender.

• **Make sure you're receiving legally mandated interest.** Millions of consumers don't receive interest on their escrow accounts, though they should.

Important: Financial institutions in California, Connecticut, Iowa, Maine, Maryland, Massachusetts, Minnesota, New Hampshire, New York, Oregon, Rhode Island, Utah, Vermont and Wisconsin are now required to make interest payments. The rates range from 1.0% to 5.25%, and payments are usually made annually.

On an average balance of $2,000, 5% interest comes to $100 a year—[illegible]

RESOLUTION

WHEREAS the continued long term health of Alaska's economy is reliant on the strength and vitality of our residential housing market; and

WHEREAS the primary source of funding for home loans is through nationally established secondary markets; and

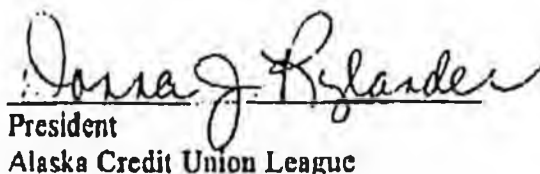
WHEREAS all citizens of the state benefits through lower interest rates and lower costs when the home lending industry is fully competitive; and

WHEREAS the House State Affairs Committee and Labor and Commerce Committee have been provided substantial written and oral testimony opposing the passage of House Bill 363 "Interest on reserve accounts";

THEREFORE, THE UNDERSIGNED ASSOCIATIONS HEREBY RESOLVE that any minimal benefit to the consumer by providing interest on mortgage reserve accounts and/or additional reserve account disclosures are far outweighed by the detrimental effect of reduced competition and a local as well as a national market place forced to adjust their home loan pricing to accommodate the increased cost.

IT IS FURTHER RESOLVED that recently enacted federal regulations impose more than adequate requirements on mortgage loan services to prevent over escrowing of funds for the payment of taxes and insurance and to ensure complete disclosures to the customer.

IT IS FURTHER RESOLVED that it is the unanimous desire of the home lending community that CS H.B. 363 "Interest on reserve accounts" not be passed due to the profound negative effects the law would have on the housing industry and the Alaskan consumer.



President
Alaska Credit Union League

REPRESENTATIVE CON BUNDE
CO-CHAIR HEALTH, EDUCATION
& SOCIAL SERVICES
VICE-CHAIR RULES

Alaska State Legislature
House of Representatives

DURING SESSION:
STATE CAPITOL, ROOM 108
JUNEAU, ALASKA 99801-1182
1 (907) 465-4843

DURING INTERIM:
716 WEST 4th AVENUE
ANCHORAGE, ALASKA 99501-2133
1 (907) 258-8168

SPONSOR STATEMENT

HOUSE BILL 363
"An Act requiring banks to pay interest on money in reserve accounts held in connection with mortgage loans."

In 1974 Congress found that many lenders were maintaining bloated escrow accounts with a year or more of excess escrow payments in them. Lenders called this excessive amount a " cushion", but were unable to justify the need for such excess. In response, Congress enacted the Real Estate Settlement Procedures Act (RESPA) which prohibits lenders and mortgage servicers from requiring consumers to maintain more than an extra two months' worth of the yearly amount necessary to pay taxes and insurance premiums. Some escrow accounts do not have more than two months' payments available. However, the accounting system used by the institution holding the escrow account may cause the account to be seriously over the two month ceiling set by RESPA.

Lenders often invest escrow funds for the short term and use the profits as their institution sees fit. The consumer that pays into the escrow account gives the use of their money to the bank and gains nothing. Therefore the institutions that hold escrow accounts have an incentive to ignore RESPA and bloat their accounts in order to maximize profits.

HB 363 requires banks (lending institutions) to pay interest on money in escrow reserve accounts. The interest paid shall be credited to the principal balance of a mortgage or paid directly to the borrower.

It is time for lending institutions to give consumers a better deal. I urge the committee to recommend the passage of this legislation.

FISCAL NOTE

No. 1
Bill Version: CSHB 363(STA)
(H) Publish Date: 2/21/96

STATE OF ALASKA
1996 LEGISLATIVE SESSION

Revision Date:
Title: Interest on Mortgage Escrow Accounts

Department: Commerce and Economic Development
BRU: Banking, Securities and Corporations
Component: Banking, Securities and Corporations

Sponsor: Representative Bunde
Requestor: Representative James

COMPONENT SERIAL NO. 1233

Expenditures/Revenues (Thousands of Dollars)

OPERATING EXPENDITURES	FY 97	FY 98	FY 99	FY00	FY 01	FY 02
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL EXPENDITURES	0.0	0.0	0.0	0.0	0.0	0.0
CHANGE IN REVENUES	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE (Thousands of Dollars)

FUND SOURCE	FY 97	FY 98	FY 99	FY00	FY 01	FY 02
1002 Federal Receipts						
1003 GF Match						
1004 General Fund						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY 96) cost: $ 0.0

POSITIONS

POSITIONS						
FULL-TIME						
PART-TIME						
TEMPORARY						

ANALYSIS: (Attach a separate page if necessary)

Prepared by: Willis F. Kirkpatrick, Director
Division: Banking, Securities and Corporations
Phone: 465-2521
Date: 1-12-96

Approved by Commissioner: William L. Hensley
Agency: Commerce and Economic Development
Date: 1-12-96

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COMMITTEE COPY

STATE INTEREST ON CROW ACCOUNT LAWS

pplies To	Interest Rate	Institutions Covered	Exceptions-- Payment of Interest Not Required	Notes
ALIFORNIA				
oans after 1/1/77	2%	All	♦ Loans made prior to effective date ♦ Moneys required by a state or regulatory authority to be placed by a lender other than a bank in a noninterest bearing demand trust fund account on loans after 1/1/80.	♦ Funds must be kept in the state. ♦ Escrow accounts on single-family, owner-occupied dwellings are optional, subject to five exceptions that protect the lender's security interest. ♦ Benefits from deposit on funds in interest bearing accounts above 2% shall accrue to to lender. ♦ Applies to institutions that make or purchase loans.
ONNECTICUT				
oans prior to 10/1/92 oans 10/1/92-9/31/94 oans on/after 10/1/94	5.25% 4.00% 5.25%	All	♦ Contract entered into before 10/1/75 and specifically disclaims interest on escrow. ♦ Violates Federal law or regulation. ♦ Servicing performed by company unaffiliated with lender, on contracts before 10/1/75, if servicer does not earn a return from investment of the escrow accounts. ♦ Loans executed between 10/1/77 and 1/1/89 and held for sale not more than 1 year by a servicer unaffiliated with purchaser; or loans executed on or after 1/1/89 and held for sale, servicing released, not more than 6 months by such servicer.	♦ If contract is prior to 10/1/77 and specifies 2%, a higher rate may not be required.
)WA				
oans on/after 7/1/82	Passbook Savings rate	State chartered banks, savings loans, credit unions, and industrial loan companies.	♦ None	♦ A lender may not require, as condition of a loan, that the borrower's funds be deposited so as to increase the yield to the lender; however, a lender may require a borrower to deposit money without interest in an escrow account to pay taxes and insurance.

Applies To	Interest Rate	Institutions Covered	Exceptions-- Payment of Interest Not Required	Notes
MAINE				
All loans	3%	Financial institutions & credit unions that are state or federally chartered with the principal office in the state; & supervised lenders.	♦ Prohibited by Federal law or regulation.	♦ If the loan or note requires an escrow account, the mortgage deed must contain provisions for payment of interest, effective 1/1/92. ♦ May charge fee for administration of escrow account but interest can not be reduced by such service charge.
MARYLAND				
Loans after 5/31/74	Greater of passbook savings rate or 3%	Banks, savings banks, and savings and loans	♦ Does not apply if loan is purchased by an out-of-state by an out-of-state lender through FNMA, GNMA, or or FHLMC and the out-of-state lender elects to service the loan. ♦ If the mortgage contract does not require the payment of interest, the purchaser of the loan does not have to pay interest. ♦ Financial institutions regulated by OTS. ♦ Mortgage and escrow account are assigned from an exempt lender that made the loan to nonexempt lender. ♦ Uses direct reduction method of applying tax and insurance payments.	♦ Applies to state chartered lending institutions doing business in the state that make mortgage loans and create, or are the assignee of, an escrow account.
MASSACHUSETTS				
Loans after 7/1/75	Determined by mortgagee annually	All	♦ If lender can demonstrate a net loss from the investment of escrowed funds in its annual report, the Commissioner of Banks may grant an exemption from paying interest on escrow accounts. Exemption is good for only one year. ♦ Federally chartered thrifts with regard to loans on 2- to 4-unit residences and loans executed prior to 6/16/75.	♦ Applies only to escrow of real estate taxes.

Applies To	Interest Rate	Institutions Covered	Exceptions-- Payment of Interest Not Required	Notes
MINNESOTA				
All loans	5%	All	♦ Escrow account is mandatory under Federal law or regulation. ♦ Conventional loan with original LTV greater than than 80%. ♦ Loans insured by HUD, VA, FmHA.	♦ Mortgagee may offer options to an escrow account. ♦ Conventional loan: under $100,000 & is not authorized by OTS or OCC or eligible for purchase by FNMA or FHLMC. ♦ Administration fee prohibited.
NEW HAMPSHIRE				
All loans	2.5%	Banks & mortgage companies	♦ None	♦ Applies to banks and to companies in the business of making loans for acquisition purposes that require, or accept monies for, an escrow account. ♦ Rate set biannually at 1% below mean interest rate paid on passbook savings accounts by state banks.
NEW YORK				
All loans	2%	All	♦ Violates Federal law or regulation. ♦ Loans made prior to 4/1/74 that have an express disclaimer not to pay interest. ♦ Servicing contract before 4/1/74 does not permit company to receive return on investments from escrowed funds.	♦ Insurance drafts received as compensation for damage to a residence and deposited in escrow are included under interest requirements. ♦ Rate set annually. ♦ Administration fee prohibited.
OREGON				
All Loans	4.5%	All	♦ Loan is over $100,000. ♦ Loan or loan servicing is sold within 1 year to unaffiliated out-of-state purchaser and loan origination documents state Oregon law does not require lender to pay interest. ♦ Violates Federal law/regulation. ♦ Loans prior to 9/1/75; however, if federal law does not prohibit or is silent concerning payment of interest, then interest must be paid on all loans of federally and state chartered institutions.	♦ If loan agreement, executed between 9/1/75 & 10/1/77, is inconsistent with the statute or silent concerning an escrow account, the rate prior to 10/1/77 applies. ♦ Service charge prohibited.

pplies To	Interest Rate	Institutions Covered	Exceptions-- Payment of Interest Not Required	Notes
HODE ISLAND				
ll loans	4%	All	♦ Loans insured by FHA, VA, FmHA or a private mortgage insurer licensed to do business in the state.	♦ Prohibits charge for ascertaining whether taxes have been paid.
TAH				
ll loans	5.25%	All	♦ Account required by government insurer or or guarantor. ♦ Original LTV is greater than 80%. ♦ Violates Federal law or regulation.	♦ Mortgagee may offer options to an escrow account. ♦ Service charge prohibited.
ERMONT				
ll loans	5% or, for institutions that offer savings accounts, the savings account rate	All	♦ If lender requires escrow account because borrower has failed within past year to pay taxes and insurance on time. ♦ Federal institutions and agencies, if not permitted by Federal law.	♦ Funds must be kept in federally insured depository institution.
ISCONSIN				
ans or extensions 11/1/81	5.25%	Banks, credit unions mutual savings banks	♦ Funds held by third party in non-interest bearing account. ♦ FHA, VA, or FmHA loans ♦ Institutions regulated by the OTS.	♦ Parties may agree to waive all or part of interest if greater than 75% of lender's interest is sold to unaffiliated third party who holds the escrow funds.
31/83		Adds mortgage bankers, savings banks, & savings and loans.		

Historical Note

St.1972, c. 412, § 1, was approved June 5, 1972, and by section 2 made applicable "to contracts entered into on and after the effective date of this act".

Library References

Mortgages ⟹298(1). C.J.S. Mortgages § 445 et seq.

RENEWAL OF MORTGAGE NOTES

Caption editorially supplied

§ 60. Interest Rate Increases

Whenever any mortgage note secured by a first lien on a dwelling house of three or fewer separate households occupied or to be occupied in whole or in part by the mortgagor provides for installment payments of principal, with or without interest, that will not amortize the outstanding principal amount in full by the maturity of such note, no increased rate of interest shall be imposed as a condition of renewing the note unless such increased rate of interest is not greater than one half of one per cent more than the rate charged on the note immediately before such maturity and the term of such renewal note is not less than five years.

Added by St.1973, c. 115.

Historical Note

St.1973, c. 115, was approved March 27, 1973.

Library References

Interest ⟹33. C.J.S. Interest § 36.

REAL ESTATE TAX DEPOSITS WITH MORTGAGEE

Caption editorially supplied

§ 61. Payment of interest by mortgagee; exemption; profit or loss statement; report

A mortgagee doing business in the commonwealth and holding a first mortgage or lien on a dwelling house of four or fewer separate households occupied or to be occupied in whole or in part by the mortgagor who requires advance payments, deposits or other security

by said mortgagor for the payment of real estate taxes on mortgaged property, shall pay interest to said mortgagor on any amounts so paid or deposited in advance. Interest shall be paid at least once a year at a rate and in a manner to be determined by the mortgagee.

Mortgagees required to pay such interest shall file annually with the commissioner of banks a statement showing the amount of net profit or loss from the investment of said deposits. Mortgagees showing a net loss from these investments may file with said commissioner a request for an exemption from the requirement that interest be paid to mortgagors. The commissioner shall maintain as a public record an annual report of interest rates paid to mortgagors as required by this section during the preceding annual period. The report shall list the mortgagees granted exemptions under this section during the preceding annual period.

Added by St.1973, c. 299, § 1.

Historical Note

St.1973, c. 299, § 1, was approved May 21, 1973.

Section 2 provided: "The provisions of section sixty-one of chapter one hundred and eighty-three of the General Laws, inserted by section one of this act, shall take effect on July first, nineteen hundred and seventy-five, and shall apply only to advance deposits for the payment of real estate taxes on mortgaged property made on or after that date."

Library References

Mortgages ⚷200(3).

C.J.S. Mortgages § 235.

§ 62. Payment of taxes to city or town by mortgagee; due date

Any mortgagee who requires the prepayment of taxes for real estate located in the commonwealth shall pay to the city or town wherein the property is located the full amount of taxes due on or before the date upon which said taxes become due provided that the mortgagor has paid said amount to the mortgagee. If the mortgagor has not paid the full amount of taxes due before said date, the mortgagee shall pay to the city or town wherein the property is located all amounts which have been paid to him by the mortgagor. Such mortgagee may make such payments by presenting notes issued by the city or town in anticipation of revenues, if the treasurer of the city or town has agreed to accept such notes in payment of real and personal property taxes as provided in section four B of chapter forty-four.

Added by St.1974, c. 104. Amended by St.1976, c. 4, § 30.

enforce any other obligation including the costs and expenses incurred in any enforcement authorized by law.

The provisions of this section as added by Chapter 1430 of the Statutes of 1970 shall only affect loans made on and after January 1, 1971.

The amendments to this section made at the 1975–76 Regular Session of the Legislature shall only apply to loans executed on and after January 1, 1976.

(Amended by Stats.1975, c. 784, p. 1780, § 2; Stats.1984, c. 890, § 3.)

Historical Note

1976 Amendment. Substituted 10 days for 5 days in which the borrower may [illegible] a delinquency without a late charge, inserted "as of [illegible] Chapter 1430 of the Statutes of 1970" in the penultimate paragraph, and added last paragraph.

1984 Amendment. Substituted in the first paragraph of subd. (a) "other than a loan made pursuant to Division 9 (commencing with Section 22000), Division 10 (commencing with Section 24000), or Division 11 (commencing with Section 26000)" for "other than a loan made pursuant to Section 22466"; and inserted in subd. (e) "or her" following "his".

Law Review Commentaries

Commentary reaches the economic trust deed. (1977) 52 S. Bar J. 203.

Notes of Decisions

In general 1
[illegible] 2

1. In general

Purported settlement of class action brought by borrowers against savings and loan association was not valid insofar as it purported to deal with validity of clause in association's mortgage form permitting it to raise interest rates whenever its interest rates paid to depositors were increased where such clause was outside scope of amended complaint, class representatives did not define class to include persons making claims as to said clause and did not purport to represent such class, and where court was not informed of pendency of other action against association raising validity of said clause. Trensky v. Los Angeles Federal Sav. and Loan Ass'n (1975) 121 Cal.Rptr. 637, 48 C.A.3d 134.

2. Estoppel

Debtor's failure to object to late charges during relief from stay proceedings and his failure to raise defense of lender's failure to send delinquency notice as required under this section did not estop debtor from raising defense, where matter of validity of late charges never became issue in relief from stay proceeding, section clearly provided that in order for lender to assess late charges lender must comply with notice requirements, and lender knew he had never sent notice and did not rely on any conduct of debtor to his injury. In re Blain, Bkrtcy.S.D.Cal.1986, 60 B.R. 748.

§ 2954.6. Mortgage insurance; cancellation rights; notification

(a) If private mortgage insurance or mortgage guaranty insurance, as defined in subdivision (a) of Section 12640.02 of the Insurance Code, is required as a condition of a loan secured by a deed of trust or mortgage on real property, the lender or person making or arranging the loan shall notify the borrower whether or not the borrower has the right to cancel the insurance. If the borrower has the right to cancel, then the lender or person making or arranging the loan shall notify the borrower in writing of the following:

(1) Any identifying loan or insurance information necessary to permit the borrower to communicate with the insurer or the lender concerning the insurance.

(2) The conditions that are required to be satisfied before the mortgage insurance may be subject to cancellation.

(3) The procedure the borrower is required to follow to cancel the private mortgage insurance or mortgage guaranty insurance.

(b) The notice required in subdivision (a) shall be given to the borrower upon close of escrow or as soon thereafter as the lender or person making or arranging the loan knows or should know the requirements for cancellation of the private mortgage insurance or mortgage guaranty insurance. The notice shall be provided without cost to the borrower.

(c) This section shall not apply to any mortgage funded with bond proceeds issued under an [illegible]ture requiring mortgage insurance for the life of the loan nor to any insurance issued pursuant [illegible] 4 (commencing with Section 51600) of Division 31 of the Health and Safety Code.

(Added by Stats.1988, c. 640, § 1.)

§ 2954.8. Impound accounts; payment of interest; restrictions; exceptions; application

(a) Every financial institution that makes loans upon the security of real property containing only a one- to four-family residence and located in this state or purchases obligations secured by such property and that receives money in advance for payment of taxes and assessments on the property,

for insurance, or for other purposes relating to the property, shall pay interest on the amount so held to the borrower. The interest on such amounts shall be at the rate of at least 2 percent simple interest per annum. Such interest shall be credited to the borrower's account annually or upon termination of such account, whichever is earlier.

(b) No financial institution subject to the provisions of this section shall impose any fee or charge in connection with the maintenance or disbursement of money received in advance for the payment of taxes and assessments on real property securing loans made by such financial institution, or for the payment of insurance, or for other purposes relating to such real property, that will result in an interest rate of less than 2 percent per annum being paid on the moneys so received.

(c) For the purposes of this section, "financial institution" means a bank, savings and loan association or credit union chartered under the laws of this state or the United States, or any other person or organization making loans upon the security of real property containing only a one- to four-family residence.

(d) The provisions of this section do not apply to any of the following:

(1) Loans executed prior to the effective date of this section.

(2) Moneys which are required by a state or federal regulatory authority to be placed by a financial institution other than a bank in a non-interest-bearing demand trust fund account of a bank.

The amendment of this section made by the 1979-80 Regular Session of the Legislature shall only apply to loans executed on or after January 1, 1980.

(Added by Stats.1976, c. 25, p. 40, § 1. Amended by Stats.1979, c. 803, p. 2765, § 1.)

Historical Note

1979 Amendment. Inserted in subd. (d)(2) following "moneys which are" the words "required by a state or federal regulatory authority", and added the last paragraph.

Section 2 of Stats.1979, c. 803, p. 2765, provided:

"The provisions of this act shall become operative only if Proposition No. 2 is approved by the voters on November 6, 1979." [Proposition 2 was approved Nov. 6, 1979.]

§ 2954.9. Loans for residential property of four units or less; right to prepayment

(a)(1) Except as otherwise provided by statute, where the original principal obligation is * * * a loan for residential property of four units or less, the borrower under any note or evidence of indebtedness secured by a deed of trust or mortgage or any other lien on real property shall be entitled to prepay the whole or any part of the balance due, together with accrued interest, at any time.

(2) Nothing in this subdivision shall prevent a borrower from obligating himself, by an agreement in writing, to pay a prepayment charge.

(3) This subdivision does not apply during any calendar year to a bona fide loan secured by a deed of trust or mortgage given back during such calendar year to the seller by the purchaser on account of the purchase price if * * * the seller does not take back four or more such deeds of trust or mortgages during such calendar year. Nothing in this subdivision shall be construed to prohibit a borrower from making a prepayment by an agreement in writing with the lender.

(b) Except as otherwise provided in Section 10242.6 of the Business and Professions Code, the principal and accrued interest on any loan secured by a mortgage or deed of trust on owner-occupied residential real property containing only * * * four units or less may be prepaid in whole or in part at any time but only a prepayment made within five years of the date of execution of such mortgage or deed of trust may be subject to a prepayment charge and then solely as herein set forth. An amount not exceeding 20 percent of the original principal amount may be prepaid in any 12-month period without penalty. A prepayment charge may be imposed on any amount prepaid in any 12-month period in excess of 20 percent of the original principal amount of the loan which charge shall not exceed an amount equal to the payment of six months' advance interest on the amount prepaid in excess of 20 percent of the original principal amount.

(Added by Stats.1974, c. 1069, p. 2280, § 1. Amended by Stats.1975, c. 763, p. 1775, § 2; Stats.1977, c. 579, p. 1825, § 22; Stats.1979, c. 391, p. 1468, § 1.)

Historical Note

1974 Legislation.

Section 2 of Stats.1974, c. 1069, p. 228[illegible], provided:

"This act shall be applicable only to loans secured by mortgages or deeds of trust executed after January 1, 1975."

1975 Amendment. Redesignated former subds. (a) to (c) as paragraphs (1) to (3) of subd. (a), inserted "Except as otherwise provided by statute" in subd. (a)(1), substituted "This subdivision" for "Subdivision (a) of this section" in subd. (a)(3), and added subd. (b).

Section 3 of Stats.1975, c. 763, p. 1776, provided:

"This act shall be applicable only to loans secured by mortgages or deeds of trust executed after January 1, 1976."

Additions in text are indicated by underline; deletions by asterisks * * *

Notes of Decisions

Savings bank investments 3
Trust company charter, acceptance of 1
Unclaimed accounts, interest on 2

---

1. Trust company charter, acceptance of

Charter of Real Estate Trust Co. may be accepted and authorization certificate issued by State Banking Department. 1937, Op.Atty.Gen. 306.

2. Unclaimed accounts, interest on

A by-law adopted with the approval of the Banking Board, permitting a savings bank to discontinue the payment of interest or dividends on "unclaimed accounts" which have remained so for a period of fifteen years, and after a written report thereof has been made to the Superintendent of Banks, would appear to be consistent with provisions of this chapter. 1941, Op.Atty.Gen. 375.

3. Savings bank investments

Securities or obligations in which the Banking Board may authorize investment under subdivision 1(f) of this section and in which savings banks may invest under subdivision 19 of section 235 include the interest bearing obligations of private or municipal corporations whether or not they are of a class for which specific tests are provided in section 235. 1944, Op.Atty.Gen. 202.

§ 14–a. Power of the banking board to prescribe rate of interest

1. It is hereby declared to be the policy of the state of New York that for the period ending September first, nineteen hundred seventy-one the rate of interest provided in section 5–501 of the general obligations law shall be adjusted by the banking board in response to changed economic conditions in such manner as to insure the availability of credit at reasonable rates to the people of the state while affording a competitive return to persons extending such credit.

2. (a) For the purpose of effectuating the policy declared in subdivision one of this section, the banking board shall have power prior to September first, nineteen hundred seventy-one by a three-fifths vote of all its members:

(1) from time to time, but not more often than quarterly, to prescribe by regulation a rate of interest not less than five per centum per annum nor more than seven and one-half per centum per annum as the maximum rate of interest to be charged, taken or received, upon a loan or forbearance of any money, goods or things in action, except as otherwise provided by law, and

(2) to adopt such other regulations as it shall deem necessary or proper to implement the provisions of this section.

(b) The rate of interest prescribed by the banking board pursuant to paragraph (a) of this subdivision shall be based on prevailing economic conditions including, in particular, yields on conventional home mortgages throughout the United States and on corporate interest-bearing securities of high quality, and shall include as interest any and all amounts paid or payable, directly or indirectly, by any person, to or for the account of the lender in consideration for making the loan or forbearance as defined by the banking board pursuant to subparagraph two of paragraph (a) of this subdivision.

(c) No rate of interest prescribed by the banking board pursuant to paragraph (a) of this subdivision shall remain in effect after September first, nineteen hundred seventy-one, except that any loan or forbearance made on or before such date at a rate of interest not in excess of the rate of interest authorized by law at the time such loan or forbearance was made shall continue to be enforceable in accordance with its terms and the provisions of section 5–501 of the general obligations law.

3. The banking board shall provide reasonable notice to the public of any change in the rate of interest, of the effective date of each such change, which shall be not less than seven days following the adoption of such change by the banking board, and of any rule or regulation adopted pursuant to paragraph (a) of subdivision two of this section. Such notice shall be provided by publication in the state bulletin, the weekly bulletin of the banking department, and in newspapers of general circulation promptly following the adoption of such change, and by such other means as the banking board shall deem necessary or proper. The banking board shall also make available to the public copies of all regulations adopted pursuant to this section.

Added L.1968, c. 349, § 3, eff. May 15, 1968.

Historical Note

Effective date and expiration of L.1968, c. 349. Section 13 of L.1968, c. 349 provided: "This act [adding this section and amending sections 108, 173, 202, 235–b, 293–a, 380–e, 454, 510–a, 577 and General Obligations Law §§ 5-501, 524.] shall take effect May fifteenth, nineteen hundred sixty-eight and shall apply in accordance with its terms only to a loan or forbearance made on or before September first, nineteen hundred seventy-one, on which date the authority granted to the banking board by this act to prescribe the maximum rate of interest to be charged, taken or received upon a loan or forbearance shall expire."

Cross References

Criminal usury, see Penal Law § 190.40.
Interest and usury generally, see General Obligations Law § 5-501 et seq.
Possession of usurious loan records, see Penal Law § 190.45.

Notes of Decisions

Computation of interest rate 4
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1. Constitutionality

This section giving banking board, for limited period of time, power to adjust maximum and minimum rates of interest within prescribed limits, ... if deemed a delegation of legislative power, was not invalid. Woodhouse, Drake and Carey Limited v. Anderson, 1970, 61 Misc.2d 951, 307 N.Y.S.2d 113.

Action of legislature in conferring power on Banking Board, and regulations of Banking Board pursuant thereto, fixing maximum rates of interest for specified period of time were not unconstitutional as an improper delegation of power. Id.

2. Judgments

Interest payable from time of judgment against defaulting obligor is at legal rate prevailing at time of judgment regardless of whether rate has changed between default and judgment. Jamaica Sav. Bank v. Giacomantonio, 1969, 59 Misc.2d 704, 300 N.Y.S.2d 718.

Rate of interest prescribed by banking board is the "legal rate of interest" as that term is used in CPLR 5004 providing that interest on judgment shall be at the legal rate; rates of interest prescribed by banking board constitute "legal rate" of interest on money judgments. Id.

The legal interest rate of six per cent or such other rate as may be established by the banking board is applicable when the county clerk calculates interest on default judgments. Op.State Compt. 68-690.

3. Mechanics' liens

The legal interest rate of six per cent or such other rate as may be established by the banking board is applicable when the county clerk passes on the sufficiency of cash bonds substituted for mechanics' liens. Op. State Compt. 68-690.

4. Computation of interest rate

Increases in legal rate of interest, as established by bank board pursuant to law, control to fix rate of interest recoverable upon a past-due demand from effective dates of increases in rate. Rachlin & Co. v. Tra-Mar, Inc., 1970, 33 A.D.2d 370, 308 N.Y.S.2d 153.

After maturity of an obligation, whether occasioned by due date or by default or other act on part of obligor that permits acceleration of maturity, rate of interest is to be computed from date of maturity or date of default resulting in maturity of obligation at rate then prescribed by statute. Dime Sav. Bank of Brooklyn v. Carlomo, 1969, 58 Misc.2d 511, 296 N.Y.S.2d 806.

On and after date on which statutory interest rate was established at 7½ per cent per annum, interest on unpaid principal of note in default should have been computed at that rate. Id.

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§ 15. Deputies, clerks, examiners, special agents and other employees; appointment; compensation; oath of office; bonds; powers of deputies

1. The superintendent may appoint five deputies, and shall employ from time to time such clerks, examiners, special agents and other employees, under such titles as he may assign to them, as he may need to discharge in the proper manner the duties imposed upon him by law. They shall perform such duties as the superintendent shall assign to them. The superintendent shall fix their compensation.

2. Every deputy, within fifteen days after notice of his appointment, shall take and subscribe the constitutional oath of office, and file such oath in the department of state. Every examiner, before entering upon his duties as such examiner, shall take and subscribe such oath and file it in the office of the clerk of the county in which he resides.

3. The superintendent may require from deputies, examiners, agents and other employees such bonds and undertakings as he may deem necessary. Premiums charged by corporations approved by him as surety upon such bonds and undertakings shall be a general expense of the department.

4. If any deputy who, prior to appointment as deputy, has served as examiner for a period of three years or more, is removed by the superintendent from such position as deputy he must be restored to the position of examiner and as such shall be entitled to the same rights and privileges to which he would have been entitled had he continued as examiner and shall receive full credit for his service as deputy and be entitled to receive a salary at least equal to that paid to him as deputy, upon the audit and warrant of the comptroller as provided in section seventeen of this article, if he shall have served as deputy continuously for more than one year or, if he shall have served as deputy for one year or less, at least equal to that paid to him as examiner immediately preceding his appointment as deputy. The superintendent may, in his discretion, appoint as an examiner for a term of not more than six months any person who shall have served in such capacity for at least three years, and shall have left the department voluntarily and in good standing.

5. Any action which the superintendent is required or authorized hereinafter by this chapter to take may be taken by a dep-

Where no action to recover usurious payment had been commenced by intestate prior to her death, action commenced by her administrator more than one year after making of payment was untimely. Blias v. Schwartz, 1960, 22 Misc.2d 129, 201 N.Y.S.2d 223.

An action against a broker for deducting interest in excess of 6 per cent must be brought within one year. Lavers v. Hutton, 1924, 122 Misc. 516, 203 N.Y.S. 23[illegible].

TITLE 6. INTEREST ON CERTAIN DEPOSITS

Section

5-601. Interest on deposits in escrow with mortgage investing institutions.

5-602. Interest on insurance draft deposits in escrow with mortgage investing institutions.

New York Codes, Rules and Regulations

Payment of interest on mortgage escrow accounts, see 3 NYCRR Part 10.

United States Code Annotated

Real estate settlement procedures, see section 2601 et seq. of Title 12, Banks and Banking.

WESTLAW Electronic Research

WESTLAW supplements McKinney's Consolidated Laws of New York and is useful for additional research. Enter a citation in Insta-Cite for display of any parallel citations and case history. Enter a statute citation in a case law database for cases of interest.

Example query for Insta-Cite: IC 403 N.Y.S.2d 123

Example query for New York Constitution: N.Y.Const. Const. Constitution /s 6 VI +3 3

Example queries for statute: "General Obligations" G.O.L. Gen.Obli /s 5-703 /5 2

Also, see the WESTLAW Electronic Research Guide following the Explanation.

§ 5-601. Interest on deposits in escrow with mortgage investing institutions

Any mortgage investing institution which maintains an escrow account pursuant to any agreement executed in connection with a mortgage on any one to six family residence occupied by the owner or on any property owned by a cooperative apartment corporation, as defined in subdivision twelve of section three hundred sixty of the tax law, (as such subdivision was in effect on December thirti-

eth, nineteen hundred sixty), and located in this state shall, for each quarterly period in which such escrow account is established, credit the same with dividends or interest at a rate of not less than two per centum per year based on the average of the sums so paid for the average length of time on deposit or a rate prescribed by the banking board pursuant to section fourteen-b of the banking law and pursuant to the terms and conditions set forth in that section whichever is higher. The banking board shall prescribe by regulation the method or basis of computing any minimum rate of interest required by this section and any such minimum rate shall be a net rate over and above any service charge that may be imposed by any mortgage lending institution for maintaining an escrow account. No mortgage investing institution shall impose a service charge in connection with the maintenance of an escrow account unless provision therefor was expressly made in a loan contract executed prior to the effective date of this section.

(Added L.1974, c. 119, § 2; amended L.1979, c. 32, § 2; L.1987, c. 267, § 2.)

Historical Note

1987 Amendment. L.1987, c. 267, § 2, eff. July 20, 1987, inserted parenthetical reference to section 360, subd. 12 of the Tax Law as was in effect on Dec. 30, 1960.

1979 Amendment. L.1979, c. 32, § 2, eff. Mar. 30, 1979, in sentence beginning "Any mortgage" inserted "or on any property owned by a cooperative apartment corporation as defined in subdivision twelve of section three hundred sixty of the tax law".

Effective Date. Section effective July 1, 1974, pursuant to L.1974, c. 119, § 7.

Library References

American Digest System

Deposits; rights and liabilities of parties, see Deposits and Escrows ⚷4.

Encyclopedia

Depositaries; rights and liabilities of parties, see C.J.S. Depositaries § 5.

Notes of Decisions

1. Agreement of parties

Issue whether corporate mortgagor was entitled to interest received by institutional mortgagee on payments made to an account of real estate taxes on mortgaged premises depended, not upon categorical concepts suggested by such labels as "trust," "agency," "escrow," "debtor-creditor," but upon rights and obligations parties intended to create as manifested by words they used in their written agreement, with parol evidence admissible to clarify ambiguities, if any under recognized canons of construction. Surrey Strathmore Corp. v. Dollar Sav. Bank of New York, 1975, 36 N.Y.2d 173, 366 N.Y.S.2d 107, 325 N.E.2d 527.

§ 5-602. Interest on insurance draft deposits in escrow with mortgage investing institutions

Any mortgage investing institution which maintains an escrow account pursuant to any agreement executed in connection with a

or labor, in order to determine whether or not there has been usury. Root v. Pinney (1860) 11 Wis. 84.

29. Sale of goods

If there be a sale of goods at an unfair price, made as a condition of the loan, the court will determine the fair value of the goods in order to determine whether there has been usury. Root v. Pinney (1860) 11 Wis. 84.

30. Sale of promissory notes

Sale of interest-bearing note at discount will not be deemed usurious unless its transfer, viewed in light of all surrounding facts and circumstances, is found to be cloak or cover for what is in reality usurious loan. Val Zimmermann Corp. v. Leffingwell, (1982) 318 N.W.2d 781, 107 Wis.2d 86.

Contingent nature of indorser's liability to indorsee precluded mere fact that unmatured, interest-bearing note was indorsed and transferred from establishing that there was understanding between parties that amount due on the note was repayable absolutely by indorser, and thus contract of indorsement, by which the note was transferred for less than its face value, was sale of the note, with recourse, and was not loan subject to usury statutes. Id.

Payee, by indorsing promissory note "with recourse," expressly intended and provided that, upon default and notice of dishonor, he would repay note according to its tenor at time of his indorsement, and thus indorsement and transfer of the note for amount less than balance due at time of transfer was not sale without recourse or conditional sale such as would limit indorser's liability to his transferee to adjusted purchase price. Id.

31. Reservation of property use

Where plaintiff, by the agreement in each transaction, reserved the equal undivided one-third of the land for the use of his money advanced to secure the same together with the right to the repayment of the full amount so advanced within a year, and, if not then paid, the repayment of the amount, with interest at 8 per cent. thereafter, such reservation, so far as it exceeded the rate of interest allowed by law, was illegal. Scheiber v. LeClaire (1886) 29 N.W. 570, 66 Wis. 579.

32. Partnerships

Where an agreement was made that a party was to receive, as his share of a business, $250 every six months, in consideration of $2,000 advanced to the concern, without any reference to the fact whether the business produced any profit or not, and also that if there was danger that the party would lose the $2,000, he might immediately enter a judgment, and collect the amount upon execution, such an agreement does not constitute a partnership between the parties thereto, but it is a usurious transaction. Cooper v. Tappan (1859) 9 Wis. 361.

33. Third-party payments

The rule that usury laws being for the protection of the borrower, the lender may receive an excess over the legal interest voluntarily paid by a third person, applied in a case where one agreed to pay $2,500 cash for a farm if he could borrow the money, but the lender asking $30 in excess of the legal rate, and the borrower refusing to pay it, the owner agreed to pay the lender the $30, and the borrower paid the owner $2,470, and gave the lender a note and mortgage for $2,500. McArthur v. Schenck (1873) 31 Wis. 673, 11 Am.Rep. 643.

34. Admissibility of evidence

Although real estate installment sales contracts did not on their face appear to provide a usurious rate of interest, parol evidence was admissible to show that usurious interest was actually charged. First Nat. Bank of Wisconsin Rapids v. Dickinson (App.1981) 308 N.W.2d 910, 103 Wis.2d 428.

35. Injunction

Retailer's one and one-half percent monthly charge on declining unpaid balance of its revolving charge account, in violation of usury statute, constituted a "public nuisance" which would be enjoined at instance of the state. State v. J. C. Penney Co. (1970) 179 N.W.2d 641, 48 Wis.2d 125.

138.051. Residential mortgage loans

(1) In this section:

(a) "Contract rate" means the initial rate contracted to be paid on the principal of a loan from time to time.

(b) "Loan" means a loan, other than a loan made by a federally chartered or state-chartered savings and loan association, secured by a first lien real estate mortgage on, or an equivalent security interest in, a one- to 4-family

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dwelling which the borrower uses as his or her principal place of residence and which is:

1. Made on or after April 6, 1980 and prior to November 1, 1981;

2. Refinanced, renewed, extended or modified on or after April 6, 1980 and prior to November 1, 1981; or

3. Made within 2 years after November 1, 1981, pursuant to a loan commitment made on or after April 6, 1980 and prior to November 1, 1981.

(2) A loan may be prepaid by the borrower at any time in whole or in part without premium or penalty. Upon prepayment of a loan in full by cash, renewal or refinancing, the borrower is entitled to a refund of unearned interest charged determined as follows:

(a) On a loan which is repayable in substantially equal, successive instalments at approximately equal intervals of time and the face amount of which includes predetermined interest charges, the amount of such refund shall be as great a proportion of the total interest charged as the sum of the balances scheduled to be outstanding during the full instalment periods commencing with the instalment date nearest the date of prepayment bears to the sum of the balances scheduled to be outstanding for all instalment periods of the loan.

(b) On any other loan, the amount of the refund shall not be less than the difference between the interest charged and interest, at the rate contracted for, computed upon the unpaid principal balance of the loan from time to time outstanding prior to prepayment in full.

(3) For purposes of computing a refund under sub. (2), interest does not include:

(a) Identifiable and separately itemized charges for services incident to the loan if they are bona fide and paid to 3rd parties unrelated to the lender;

(b) Fees, discounts or other sums actually imposed by government national mortgage association, federal national mortgage association, federal home loan mortgage corporation or any other governmentally sponsored or private secondary mortgage market purchaser of a loan from the original lender; and

(c) A loan administration fee charged by a lender, not to exceed 2% of the principal amount of any construction loan and one percent of the principal amount of any other loan.

(4) For the purpose of calculating the rate of interest on a loan scheduled to be paid in instalments under sub. (2), the parties may agree that any instalment paid within 30 days prior to or after the scheduled due date will be considered to have been paid on the due date.

(5) A bank, credit union or mutual savings bank which originates a loan and which requires an escrow to assure the payment of taxes or insurance shall pay interest on the outstanding principal balance of the escrow of not less than 5.25% per year. This subsection applies to any refinancing, renewal, extension or modification of the loan on or after November 1, 1981.

(6) Delinquency charges on a loan shall not exceed an amount determined by application of the contract rate to the unpaid amount, including interest accrued and unpaid, until paid or maturity of the obligation, whether by acceleration or otherwise, whichever first occurs. Interest imposed after maturity may not exceed the contract rate applied to the amount due on the date of maturity.

(7) This section does not apply to a loan insured, or committed to be insured, or secured by mortgage or trust deed insured by the U.S. secretary of housing and urban development, insured, guaranteed or committed to be insured or guaranteed under 38 USC 1801 to 1827 or insured or committed to be insured under 7 USC 1921 to 1995.

(8) The contract rate is not subject to rate limitations imposed under this chapter or s. 218.01 or 422.201.

Historical Note

Source:
L.1979, c. 168, § 3, eff. April 6, 1980.
L.1981, c. 45, §§ 5, 6, eff. Nov. 1, 1981.
Laws 1979, c. 168, § 20 provides:

"This act is not the adoption of a law limiting the amount or rate of interest under P.L. 96-161 or a successor thereto."

Cross References

Effect of usury and penalties, see § 138.06.
Precomputed loan law, see § 138.09.
Primary mortgage loan program not subject to this section, see § 45.79.

Law Review Commentaries

A description of the modification of Wisconsin's Usury Laws. James L. Brown and Robert A. Patrick. 65 Marquette L.Rev. 309 (1982).

Library References

Mortgages ⇐122.
WESTLAW Topic No. 266.
C.J.S. Mortgages § 179.

138.052. Residential mortgage loans

(1) In this section:

(a) "Contract rate" means the rate contracted to be paid from time to time on the principal of a loan.

(b) "Loan" means a loan secured by a first lien real estate mortgage on, or an equivalent security interest in, a one- to 4-family dwelling which the borrower uses as his or her principal place of residence and which is made, refinanced, renewed, extended or modified on or after November 1, 1981, but does not include a mobile home transaction as defined in s. 138.056(1)(c).

(c) "Loan administration" means a lender's processing of a loan and includes review, underwriting and evaluation of the loan application, document processing and preparation and administration of the loan closing, but does not include appraisals, inspections, surveys, credit reports or other activities