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US Sprint

November 16, 1992

VIA HAND DELIVERY

Mr. Steven C. Tribble, Director
Division of Records and Reporting
Florida Public Service Commission
101 East Gaines Street
Fletcher Building
Tallahassee, Florida 32399-0870

Re: Docket No. 920260-TL - Comprehensive Review of the Revenue Requirements and Rate Stabilization Plan of Southern Bell Telephone and Telegraph Company

Dear Mr. Tribble:

Enclosed for filing with the Commission are an original and fifteen (15) copies of Sprint Communications Company Limited Partnership's Testimony along with a * 5-1/4" diskette in the above-referenced matter. Please return a filed-stamped copy in the enclosed return self-addressed envelope.

Thank you.

Very truly yours,

Chanthina R. Bryant

Chanthina R. Bryant
Attorney, State Regulatory

CRB:lj

cc: Parties of Record

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DIRECT TESTIMONY OF EMERIC KAPKA
ON BEHALF OF
SPRINT COMMUNICATIONS COMPANY LIMITED PARTNERSHIP

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Emeric Kapka. My business address is 7171 West 95th Street, Overland Park, Kansas, 66212.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT ARE YOUR RESPONSIBILITIES?

A. I am the Manager-Regulatory Access Planning at Sprint Communications Company Limited Partnership ("Sprint"). I am responsible for developing Sprint's position on access and related issues in federal and state regulatory forums.

Q. PLEASE SUMMARIZE YOUR PROFESSIONAL AND EDUCATIONAL BACKGROUND?

A. Prior to joining Sprint in December, 1991, I was General Manager - Pricing & Planning at United Telephone of Ohio where I was responsible for pricing and revenue attainment for all regulated services. From 1986 until acceptance of the position at United of Ohio in 1988, I was Toll Rates & Tariffs Manager for United Telephone - Southeast Group where my responsibilities included developing and tariffing toll products for United Southeast Group's three state region of Tennessee, Virginia and South Carolina.

From 1984 to 1986, I was Staff Economist and later, Manager - Industry Analysis for United Telecommunications Corporate Staff where my major responsibilities were to assist in development of state and federal regulatory positions. I began my career in regulation with the Indiana Public Service Commission in 1983 as a financial analyst; my responsibilities included testifying on a number of financial issues before the Commission, including determination of appropriate cost of capital in rate proceedings as well as more economic oriented issues, such as a cost/benefit analysis of local measured service pricing options for Indiana Local Exchange Companies ("LECs"). Prior to joining the Indiana Commission Staff, I was an economic analyst for the Indiana Department of Commerce.

I received a MA degree in Economics, with a concentration in Business, from Cleveland State University in 1982. I also hold a BA degree in Economics from the same university, awarded in 1980.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. Sprint believes that Southern Bell's access rates, especially for switched services, continue to be priced to include large contributions which are borne by access customers without reference to cost causation. This condition is addressed but not sufficiently corrected in the proposed Price Regulation Plan ("PRP"), which, if adopted, envisions a slight reduction in access rates. However, the proposed distribution of the $47.5 million customer credit does not even address access services. Sprint, therefore, urges the Commission to correct for this omission by requiring that a portion of the $47.5 million Southern Bell revenue reduction be targeted to access rates. Further, Sprint recommends that the Commission require that access rates be reduced under the framework of the Southern Bell proposed Price Regulation Plan, should the Commission adopt it. Sprint's comments address the overall rationale for encouraging reductions in access rates as well as recommending specific actions that Southern Bell should take to help foster a more competitive long distance marketplace.

Q. WHAT IS SPRINT'S INTEREST IN THIS PROCEEDING?

A. Sprint is a facilities-based interexchange carrier

("IXC") and a major purchaser of Southern Bell provided access services in Florida. During 1992, for example, Sprint will pay Southern Bell approximately $70 million in access charges, of which some 40 percent is jurisdictionally intrastate. Southern Bell currently provides more than 99 percent of Sprint's access connections in its franchised territory. Sprint believes that the long-term viability of IXCs will depend, to some extent, on reducing the huge cost of switched access. Sprint also believes that Southern Bell's long-term viability will depend to some extent, on its ability to reduce its access rates. As the smallest of the major three long distance carriers in an extremely competitive industry, Sprint is concerned about any potential attempt by Southern Bell, faced with competition, to shift its revenue needs away from its largest access customers to smaller access customers through access rate restructuring.

Q. ARE ACCESS RATES CURRENTLY PRICED ABOVE COST?

A. Yes. Access rates are significantly greater than the underlying economic costs associated with providing access services. This mismatch of access rates and costs is evidenced by the fact that interexchange carriers ("IXCs"), such as Sprint, pay dramatically different prices for access services that have the same underlying economic costs.

Q. CAN YOU PROVIDE SOME EXAMPLES OF THIS PRICE-COST MISMATCH?

A. Yes. Sprint pays Southern Bell in Florida approximately 5.76¢ per minute on each end of an intrastate switched access call, but pays approximately 2.84¢ per minute for an equivalent interstate call. Fundamentally, there is no difference in the economic costs associated with providing interstate or intrastate access services, but yet, the per minute price of intrastate switched access services is more than double the interstate price.

While interstate switched access charges are priced well below intrastate levels, Sprint believes that interstate switched access charges are also set well above the underlying economic costs of providing the service. Consider, for example, LEC provided local transport service, which is one of the elements of switched access charges intended to cover the costs of transmitting calls between a LEC end-office and an IXC's point of presence ("POP"). The table accompanying my testimony shows Southern Bell's interstate rates for three types of transport service, local transport via switched access, special access transport for DS-1 service and special access transport for DS-3 service.

The final number represents Sprint's estimate of the long run incremental cost ("LRIC") of providing transport services using DS-3 facilities (the row labeled "Dark Fiber Transport w/Electronics").

Sprint believes that Southern Bell provides transport service, whether for switched or special access type services at DS-3 levels in most instances. So the underlying cost of providing transport service, expressed on a per minute of use basis, is somewhere between the Sprint estimated LRIC level of .023 cents and the BellSouth DS-3 implied per minute rate of .09157 cents. Compare this rate to Southern Bell's current intrastate average transport rate per minute of 1.23 cents. This differential leads Sprint to conclude that Southern Bell switched access prices, in this example, local transport service, are generally priced far above the underlying economic costs of providing access services.

Many individual LEC access rate elements are priced above cost such as the level of the Carrier Common Line charge ("CCLC"). It is not clear why LEC access elements, such as local transport, are priced so much higher than the underlying economic cost of the service.

Q. HOW WOULD CONSUMERS BENEFIT FROM LOWER ACCESS PRICES?

A. High access costs inflate long-distance prices. For example, Sprint pays Southern Bell approximately 5.76 cents per minute on each end of an instate long-distance call, compared to 2.84 cents per minute for interstate long-distance calls originating or terminating in Florida. This means that a 3 minute call from Tallahassee to Orlando, for example, "costs" Sprint more than 34 cents in access compared to approximately half of that for an equivalent 3-minute call from Tallahassee to Atlanta, for example. Not surprisingly, given that access is such a significant portion of Sprint's costs, Sprint's retail price for a 3 minute call from Tallahassee to Orlando is approximately 14 percent higher than what a comparable out-of-state Tallahassee to Atlanta call would cost a customer. If LEC access services, especially switched access services, were priced closer to cost, competitive forces in the long-distance market would require downward pressure on toll prices. This would, in turn, be a benefit to customers.

Q. WHY SHOULD SOUTHERN BELL INCLUDE REDUCTIONS IN ACCESS CHARGES WITHIN ITS $47.5 MILLION CUSTOMER CREDIT IN EFFECT FOR 1993?

A. Two factors should influence the decision on how to distribute the $47.5 million customer credit. First, the source or existence of any credit should be recognized by reducing rates associated with those services achieving higher than average demand growth because, absent this growth, there would be no credits to disburse. Second, Southern Bell should be required to reduce rates for those services which are currently priced above LRIC. And as a corollary to this second point, the credit distribution among services priced higher than LRIC should be roughly proportional to the difference between current prices and LRIC. This "crediting rule" should govern all rate reduction circumstances.

According to information provided by Southern Bell, there is only one service priced below LRIC, and that is basic residential service. Therefore, all other services should be considered for rate reductions associated with the credit.

In order to determine this distribution, Southern Bell should be required to categorize services into logical groupings and determine the appropriate price and LRIC associated with each service. Based on the price/cost relationship, Southern Bell can then determine the appropriate services to be targeted for price reductions.

We can illustrate how this process might work with the following example: Assume Southern Bell provides only two services that meet the price compared to LRIC test, intraLATA toll and switched access service. Assume further that the LRIC associated with intraLATA toll service is 5 cents per minute while the average revenue for intraLATA toll service is 10 cents per minute. Assume that the LRIC associated with switched access service is 2 cents per minute and the average revenue is 6 cents per minute. Now, if both toll service and switched access service demand levels outpace the average revenue growth rate for Southern Bell services, the crediting rule we propose suggests that switched access service prices must be reduced to 4 cents per minute (two times LRIC - the current intraLATA toll price/LRIC ratio), before intraLATA toll prices are reduced. If intraLATA toll demand growth was lower than average, then all of the credit allowance would be used to reduce switched access prices, in this example.

As indicated earlier, Sprint believes switched access prices are priced much higher than the relevant cost of providing switched access service. Southern Bell has also indicated that it anticipates access demand growth of 16 percent in 1992 which appears to be greater than the average demand growth enjoyed by Southern Bell. Access revenues should, therefore, be targeted for a portion of the credit.

Q. DO YOU AGREE WITH SOUTHERN BELL'S PROPOSED REDUCTIONS OF SWITCHED ACCESS RATES AS PART OF ITS PRICE REGULATION PLAN PROPOSAL?

A. First of all, Sprint agrees with the idea of reductions in switched access rates. As I indicated earlier, these service rates are priced far above the underlying cost of providing switched access service; these higher than cost prices have damaging consequences for consumers, as I have outlined. As I understand the Southern Bell proposal, average originating and terminating switched access revenue per minute would decline from 4.610 cents and 7.03 cents respectively, to 4.403 cents and 6.758 cents, respectively. This rate reduction is achieved by lowering the local transport element, for both originating and terminating switched access from 1.60 cents to 1.328 cents.

While Sprint supports the idea of reductions in higher than cost services such as switched access, we believe that Southern Bell could have achieved an equivalent revenue reduction in a far more efficient way.

Q. WHAT SORT OF ACCESS RATE REDUCTIONS WOULD SPRINT PROPOSE?

A. Given the fact that switched access rates are priced much higher than LRIC today, Sprint believes that the time-of-day aspect of the Southern Bell switched access rate structure is particularly onerous and should be targeted for immediate correction. Sprint believes that time of day discounts should be eliminated from the switched access tariff. Revenue generated by removal of the discounts should be applied to lowering the originating CCLC from its excessively high level of 2.62 cents.

Q. WHY SHOULD TIME OF DAY SWITCHED ACCESS RATES BE ELIMINATED?

A. The Florida Public Service Commission ordered switched access discounts to encourage access customers to utilize the LEC access network during off-peak periods. While in theory such pricing makes economic sense if demand can be shifted to off-peak periods thereby conserving capital and reducing overall costs, the practical effect of the Florida experience has been a shifting of access expense among IXCs based on their time of day switched access demand, with little, if any, decrease in LEC capital outlays attributable to demand shifts.

Q. WHY DO YOU ASSERT THAT THERE HAVE BEEN LITTLE CAPITAL SAVINGS ATTRIBUTABLE TO DEMAND SHIFTS CAUSED BY TIME OF DAY SWITCHED ACCESS DISCOUNTS?

A. The vast majority of LEC switched access costs are not attributable to actual access demand, and certainly not attributable to demand at any hour of the day. For example, costs recovered through the CCLC, the largest single component of switched access charges, do not vary by time of day. Costs recovered through the CCLC are incurred to provide a circuit connecting an end user location to a LEC central office. Shifts in temporary demand will in no way reduce capital needs or other costs recovered through the CCLC.

Additionally, LEC access rates are designed to recover much more than the capital costs associated with providing access services. Access rates are set to recover the total revenue requirement. As Sprint has shown regarding the local transport element, the differential between the access rate and the underlying LRIC-type cost may be upward of 300 percent. While Sprint is not disputing that "contribution levels" of this magnitude may be appropriate in the short run, Sprint is suggesting that recovering this via time of day access rates under the guise of "peak-load pricing" is inappropriate because time of day access pricing does not (and cannot) accomplish its intended effect: reduction of overall costs.

Q. WHAT IS THE IMPACT OF TIME OF DAY ACCESS RATE PRICING ON SPRINT RELATIVE TO OTHER ACCESS CUSTOMERS?

A. The recovery of non time-of-day sensitive costs and/or "contribution" via time-of-day access rates harms Sprint because it results in an effective shifting of Southern Bell's access expense from the largest IXC to other IXCs, such as Sprint.

Q. HOW SHOULD SOUTHERN BELL REVISE SWITCHED ACCESS RATES?

A. Sprint recommends that the discounts associated with switched access rates be eliminated and the resulting revenue increase be targeted to reductions in the originating CCLC.

Q. WOULD YOU PLEASE SUMMARIZE YOUR TESTIMONY?

A. Yes. Sprint is a major customer of Southern Bell provided access. Currently, Southern Bell charges for access are priced far above cost. Sprint would like to see those charges reduced so that rates more accurately reflect the underlying costs. In turn, competitive pressures in the long-distance marketplace would create downward pressure on intrastate toll prices. Sprint believes that the best way to achieve more cost-based access prices is to target the $47.5 million customer credit to reductions in access rates. If the Commission adopts the Southern Bell proposed Price Regulation Plan, Sprint recommends that Southern Bell be required to target rate reductions to those services generating higher than average revenue growth and to those services priced higher than LRIC. Sprint also recommends that the Commission abolish time of day access discounts which serve no useful economic function and only result in a shifting of Southern Bell's access expense from AT&T to Sprint.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

Direct Testimony of Emeric Kapka
Florida Public Service Commission
Docket No. 920260-TL
Attachment

BellSouth's Monthly Recurring Charges for Various Transport Services per Equivalent DS-1 Transport (1 Mile) Expressed on a Per Minute of Use Basis

Service	Charge
Switched Access	$0.644
DS-1 Service	$0.1277
DS-3 Service	$0.0916
Dark Fiber Transport w/ Electronics	$0.023

1. DS-1 and DS-3 costs includes the tariff charge for 1 DS-1 or DS-3 channel term and 1 mile of channel mileage.
2. DS-3 cost also includes the tariff charge for 3:1 mux.
3. Assumed capacity per DS-1 is 216,000 minutes.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the within and foregoing TESTIMONY in FPSC Docket No. 920260-TL; "COMPREHENSIVE REVIEW OF THE REVENUE REQUIREMENTS AND RATE STABILIZATION PLAN OF SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY" upon the following parties of record by depositing same in the United States Mail, first class, postage prepaid.

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This 16th day of November, 1992.

SPRINT COMMUNICATIONS COMPANY
LIMITED PARTNERSHIP

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