BELLSOUTH TELECOMMUNICATIONS, INC.

REBUTTAL TESTIMONY OF JERRY D. HENDRIX

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 920260-TL

SEPTEMBER 16, 1996

Q. PLEASE STATE YOUR NAME, EMPLOYER, POSITION AND BUSINESS ADDRESS.

A. My name is Jerry D. Hendrix. I am employed by BellSouth Telecommunications, Inc. ("BellSouth") as Director - Pricing and Regulatory Interconnection Services Marketing in the Interconnection Customer Business Unit. My business address is 675 West Peachtree Street, Atlanta, Georgia 30375.

Q. ARE YOUR THE SAME JERRY D. HENDRIX WHO FILED DIRECT TESTIMONY ON BEHALF OF BELLSOUTH ON JULY 31, 1996?

A. Yes, I am.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS DOCKET?

A. The purpose of my testimony is to rebut direct testimony filed in this case by: Joseph Gillan on behalf of the Florida Interexchange Carriers Association;

Michael Guedel on behalf of AT&T Communications; Don J. Wood on behalf of MCI; Daniel Vanderpool on behalf of Sprint; and Jill Butler on behalf of Florida Cable Telecommunications Association, Inc.

Q. ON PAGE 4, LINES 15-20 OF JOSEPH GILLAN'S TESTIMONY, MR. GILLAN STATES THAT A REDUCTION IN THE CARRIER COMMON LINE CHARGE (CCLC) IS APPROPRIATE "BECAUSE IT IS THIS ELEMENT THAT IS MOST RESPONSIBLE FOR INTRASTATE RATES EXCEEDING INTERSTATE RATES. THE COMMISSION SHOULD THEN USE A PORTION OF THE DISCRETIONARY, UNSPECIFIED REDUCTION TO ELIMINATE THE RESIDUAL INTERCONNECTION CHARGE OR RIC." DO YOU HAVE ANY COMMENTS?

A. Yes. BellSouth agrees that the CCLC should be reduced, but BellSouth disagrees that the RIC should be eliminated. In 1994 BellSouth filed its first switched access reduction in compliance with the Stipulation and Agreement. At that time, BellSouth also indicated what the rate levels would be for the next two years and proposed them to the Florida Public Service Commission Staff. The switched access reductions filed in the past two years have been approved by this Commission as filed. BellSouth believes it is appropriate to use the remaining $40 million in 1996 to reduce the CCLCas we indicated in 1994.

BellSouth is also in agreement that a portion of the $48 million should be used to further reduce switched access rates. In fact, consistent with Mr. Gillan, BellSouth has filed an additional $16.4 million switched access reduction of which $12 million or 75% of the reduction is used to reduce the Interconnection (RIC) rate element.

However, as usual, the Interexchange Carriers (IXCs) have gone to the extreme in their request for switched access reductions. The IXCs are requesting that $35 million of the $48 million be applied to eliminate the RIC. BellSouth believes the IXCs requested switched access reductions are excessive. BellSouth's pending $48 million reduction provides a benefit to a variety of our customers not just the IXCs. It is BellSouth's position that the reductions targeted in this docket should benefit as many of the ratepayers in Florida as possible. It is not appropriate to target $35 million or 73% of the rate reduction to one class of customer who has seen tremendous benefits to the tune of $145 million since 1994. BellSouth has attempted to consider many types of customers in its rate reduction proposal, including an additional $16.4 million in switched access charge reductions for the IXCs.

Q. MR. GUEDEL ON PAGE 7, MR. GILLAN ON PAGE 18, MR. VANDERPOOL ON PAGE 3 AND MR. WOOD ON PAGE 5 ALL STATE THAT THE RIC HAS NO COST BASIS. DOES BELLSOUTH AGREE THAT THERE IS NO COST BASIS FOR THE INTERCONNECTION RATE ELEMENT?

A. No. In the Federal Communications Commission's (FCC's) Transport Rate Structure and Pricing, Report and Order, CC Docket No. 91-213, released

October 16, 1992, the FCC apparently recognized that the RIC recovers common transport costs and tandem switching costs that are not recovered by the transport and tandem switching rates. The RIC was established because the rate paid by users of tandem switching and transport were intentionally set so low as to not recover the full cost of these elements.

Q. MR. GILLAN, MR. GUEDEL, MR. WOOD AND MR. VANDERPOOL ALL ARGUE THAT SWITCHED ACCESS CHARGES SHOULD BE REDUCED CLOSER TO COST IN ORDER TO, AS MR. VANDERPOOL STATES ON PAGE 3 OF HIS TESTIMONY, "SEND CORRECT ECONOMIC SIGNALS TO POTENTIAL COMPETITORS". SHOULD THE COMMISSION REQUIRE BELLSOUTH TO REDUCE ITS SWITCHED ACCESS RATES TO "COST-BASED" LEVELS AS ADVOCATED BY THESE WITNESSES?

A. No. BellSouth should not be required to reduce switched access rates to the "cost-based" levels that are being advocated by these witnesses. BellSouth has already reduced switched access rates by nearly 76% since 1984. In today's value, this amounts to over $590 million annually.

In addition, since 1994 alone, BellSouth has reduced switched access rates by more than $145 million. The Florida Statute requires BellSouth to reduce switched access rates by 5% each year until 1994 interstate parity is reached. With the Stipulated $40 million reduction, plus the $16.4 million additional switched access reduction, BellSouth will meet this requirement in 1996. As

BellSouth has come to expect, the IXCs are continuing to insist on further reductions; nonetheless, it is inappropriate.

Q. BEGINNING ON PAGE 8 LINE 25 AND CONTINUING ON PAGE 9, LINES 1-7 OF MIKE GUEDEL'S TESTIMONY, HE STATES THAT "HIGH ACCESS CHARGES CAN DISTORT THE ECONOMICS OF COMPETITIVE LOCAL ENTRY - PERHAPS ENCOURAGING POTENTIAL ENTRANTS TO BUILD FACILITIES WHERE OTHER FORMS OF ENTRY SUCH AS RESALE MAY MAKE BETTER ECONOMIC SENSE. IN EITHER CASE, THE END USER RECEIVES LESS THAN THE DESIRED RESULTS OF COMPETITION". IN ADDITION, MR. GILLAN ON PAGE 9 LINES 22 - 23 STATES "THE FULL UTILIZATION OF THESE NETWORKS IS ARTIFICIALLY RETARDED BY THE HIGH PRICES THAT LOCAL TELEPHONE COMPANIES IMPOSE ON LONG DISTANCE CALLING." MR. WOOD ECHOES ON PAGE 4 OF HIS TESTIMONY THAT "IF ACCESS RATES REMAIN EXCESSIVELY HIGH, RETAIL TOLL PRICES WILL LIKEWISE REMAIN HIGH EVEN IF THE MARKETPLACE FOR RETAIL TOLL SERVICES IS EFFECTIVELY COMPETITIVE." WILL YOU PLEASE COMMENT?

A. BellSouth has reduced intrastate switched access rates by nearly 76% since 1984; however, the majority of consumers in Florida have not directly benefited from these intrastate switched access reductions. In other words, the IXCs have not been reducing long distance rates correspondingly. My analysis shows that on average, there have been increases in the IXC's basic toll rates (MTS) from 1991 to the present. During this same period, switched access rates declined by approximately 57%. See JDH-3.

In fact, as discussed in a previous North Carolina hearing, BellSouth's level of access charges has had little to do with retail toll prices assessed by IXCs. The North Carolina Utilities Commission acknowledged this fact in their recent Price Regulation Order in Docket No. P-55, Sub 1013 in which the Commission directed the IXCs to flow through switched access reductions to their MTS customers. The Commission stated that:

> those reductions should be flowed through in a way such that as many of the IXCs' customers as practicably possible would receive some direct benefit therefrom. The Commission believes that the foregoing can best be accomplished by directing the IXCs to flow through these reductions to their basic residential and business subscribers through decreased intrastate basic message telephone service (MTS) rates on a dollar-for-dollar basis.

AT&T, MCI and Worldcom, Inc. filed a Joint Motion with the North Carolina Utilities Commission requesting the Commission to reconsider and amend the Price Regulation Order to allow IXCs to flow through access charge reductions to <u>all</u> of their switched access customers. The Commission denied the IXCs' request to spread the access charge reduction among many services and reaffirmed the original May 2, 1996 Order in Docket No. P-55, Sub 1013. The

North Carolina Commission will even monitor flow through because end users were not seeing total benefit of access reductions.

Q. WHAT CONCLUSION CAN BE DRAWN ABOUT THE FLOW THROUGH OF SWITCHED ACCESS REDUCTIONS FROM PREVIOUS EXPERIENCES?

A. Unless the Florida Commission orders the IXCs to flow through the switched access reductions to their basic MTS toll rates, there are no guarantees that reduced switched access rates will result in benefits for the majority of consumers in Florida. As we have seen in the past, if not so ordered, the IXCs will target flow through reductions to their high volume markets and not to the basic MTS ratepayers. Section 364.163 of the Florida Statutes requires that "any telecommunications company whose intrastate switched access rate is reduced ... shall decrease its customer long distance rates by the amount necessary to return the benefits of such reduction to its customers." Even though the Florida Statutes require the IXCs to flow through switched access reductions, there is no guarantee that reduced switched access rates would result in benefits for end users in the form of lower basic toll rates.

Q. MR. GUEDEL STATES ON PAGE 8 THAT "ACCESS CHARGES IN EXCESS OF INCREMENTAL COST PROVIDE THE INCUMBENT MONOPOLIST WITH THE OPPORTUNITY TO EXACT A CONTRIBUTION...FROM ANY POTENTIAL COMPETITOR THAT WOULD "DARE" TO ATTEMPT TO COMPETE WITH AN

INCUMBENT'S RETAIL SERVICES." DO YOU AGREE WITH HIS ASSESSMENT?

A. No, Mr. Guedel's statement is ludicrous. There is already significant competition in the intraLATA toll market, and the lack of "cost-based" access rates has not prevented competitors from entering the market. This Commission has approved numerous IXC tariffs for services with intraLATA capability, such as AT&T's Software Defined Network, MegaCom, MegaCom 800, 800 Readyline, and similar services for MCI and Sprint. These services have made significant inroads into the intraLATA business toll market.

IXCs are also competing for intraLATA calls through the use of 10XXX, 500, 700, 800, and 900 access services. IXCs are using these services effectively to take any lucrative high volume customers from BellSouth. These same IXC competitors are now targeting the small to medium business markets and high volume residential users.

Furthermore, on February 13, 1995, the Florida Public Service Commission in Docket No. 930330-TP ordered the implementation of intraLATA presubscription by the end of 1997. BellSouth's tariff was approved on May 1, 1996 and BellSouth is moving forward to implement 1+ intraLATA presubscription. In fact, the IXCs such as AT&T are actively seeking customers in BellSouth to subscribe to AT&T as their only toll provider.

Finally, BellSouth's competitive intraLATA toll rates must cover the cost that an IXC would incur in providing a similar service. These rates satisfy the requirements of the imputation standard addressed in the Florida Statute which provide competitors an advantage in competing with our retail services.

Q. MR. GILLAN ON PAGE 11, LINES 1-2 OF HIS TESTIMONY STATES THAT "MOST ELEMENTS OF SWITCHED ACCESS SERVICE-- PARTICULARLY TERMINATING ACCESS- ARE INVULNERABLE TO COMPETITIVE PRESSURES." PLEASE EXPLAIN WHY HIS ASSESSMENT IS WRONG.

A. There are competitive pressures in the switched access market, many of which have been fueled by the FCC. In the past few years, the FCC has issued several orders restructuring local transport and allowing expanded interconnection or collocation for the purpose of reducing regulatory and economic barriers to competitive entry into the access transport services market. This Commission approved BellSouth's restructure of local transport with switched transport zone pricing on January 1, 1996 and collocation on February 6, 1996. Those changes in switched access have encouraged new competitors, i.e. Alternate Access Providers (AAVs), to enter the already competitive access markets.

AAVs, like IXCs, are targeting high volume customers, densely populated areas, and metropolitan business districts. Because revenues are highly concentrated in these areas, they are ideal areas for AAVs to target with facilities and services to high volume customers and IXCs. As of 1996 there are at least 32 AAVs in numerous locations throughout the state, which have either constructed fiber networks in major cities or have expressed an interest in building networks. AAVs are displacing switched access (both originating and terminating) and special access services. Mr. Gillan's assessment is not well thought through.

Q. ON PAGE 18 OF MR. GILLAN'S TESTIMONY AND ON PAGE 10 OF MR. GUEDEL'S TESTIMONY, BOTH WITNESSES STATE THAT THE COMMISSION SHOULD NOT APPROVE BELLSOUTH'S ZONE PRICING PROPOSAL WITHOUT COST-JUSTIFICATION. WHY IS BELLSOUTH'S ZONE PRICING PROPOSAL APPROPRIATE AS FILED?

A. On January 1, 1996, the Zone Pricing for Switched Transport tariff became effective in Florida. This filing was made in compliance with the Florida Public Service Commission Order No. PSC-94-0277-PCO-TL in Docket No. 921074-TP. BellSouth has not performed cost studies related to zone pricing of the switched access rate elements. However, there may indeed be cost differences in providing switched access between the urban and rural areas.

Rather than providing cost based zone pricing reductions, BellSouth has zone priced switched access based on market pressures. This is consistent with the actions taken by BellSouth's competitors in the marketplace. The bottom line is simply that BellSouth chose to price its services to reflect market conditions in the various zones. It makes good business sense to lower BellSouth's switched access rates in its most competitive areas. BellSouth's competitors, however, do not want zone pricing because it makes it more difficult for them to "cream skim"/"cherry pick" BellSouth's most valuable customers.

Q. MR. GILLAN STATES ON PAGE 18 THAT "BELLSOUTH WILL BE INCREASING, NOT REDUCING, ITS SWITCHED ACCESS PRICES...AFTER THIS PROCEEDING." WHAT IS BELLSOUTH'S RESPONSE TO THIS ALLEGATION?

A. Mr. Gillan has no basis to conclude that BellSouth will increase switched access rates after this proceeding. I am unaware of any plans to raise switched access rates at this time. Section 364.163 of the Florida Statutes mandates that BellSouth's intrastate switched access rates must be decreased by at least 5% annually until December 31, 1994 interstate parity is reached. In addition, switched access rates in Florida are capped at the rates in effect on July 1, 1995 and are to remain capped until January 1, 1999.

Q. JILL NICKEL BUTLER OF THE FLORIDA CABLE TELECOMMUNICATIONS ASSOCIATION (FCTA) ARGUES THAT "A PORTION OF THE $48 MILLION IN RATE REDUCTIONS SHOULD BE UTILIZED TO ELIMINATE THE NON-RECURRING CHARGES FOR THE INTERCONNECTION TRUNKS THAT ALTERNATIVE LOCAL EXCHANGE TELECOMMUNICATIONS COMPANIES (ALECS) ORDER FROM BELLSOUTH AND NON-RECURRING CHARGES FOR DEDICATED, SWITCHED CIRCUITS ALECS ORDER OUT OF THE

BELLSOUTH ACCESS TARIFF." DOES BELLSOUTH SUPPORT ELIMINATING THESE NON-RECURRING CHARGES?

A. No. As stated in my direct testimony, the cost of installing interconnection trunks is appropriately recovered through non-recurring charges. The elimination of non-recurring charges would simply line the pockets of new vendors. End Users most likely would never see any benefit from the elimination of such charges. The nonrecurring charges that BellSouth has proposed to reduce in this docket are those charges that are paid by our end user customers, not competing carriers. Furthermore, this is not the appropriate docket to handle this particular issue.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.