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**BEFORE THE PUBLIC SERVICE COMMISSION**  
**REBUTTAL TESTIMONY**  
**OF**  
**BRIAN K. STAIHR**

**I. INTRODUCTION**

**Q. Please state your name, title and business address.**

**A.** My name is Brian K. Staihr. I am employed by Sprint as Senior Regulatory Economist. My business address is 6450 Sprint Parkway, Overland Park, Kansas 66251.

**Q. Are you the same Brian K. Staihr who filed direct testimony in this proceeding on August 27, 2003?**

**A.** Yes I am.

**Q. What is the purpose of your rebuttal testimony?**

**A.** In my rebuttal testimony I address one issue raised in the testimony of Mr. Gregory L. Shafer, testifying on behalf of the Commission staff. I also respond to one issue raised in the testimony of Dr. David Gabel, testifying on behalf of the Office of Public Counsel.

**II. MR. GREGORY L. SHAFER**

**Q. In general, does Sprint agree with the arguments contained in Mr. Shafer's testimony?**

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1     **A.**     Sprint agrees with many of Mr. Shafer's points. For example, on page 9 of his  
2             testimony he states that "the improvement in the cost/price relationship for basic local  
3             exchange service as reflected in the companies petitions will be a signal to competitors  
4             that the potential for profitability is improved" and Sprint agrees with this statement.

5  
6             But Sprint disagrees with Mr. Shafer's suggestion that the adjustments to the price for  
7             basic local service that have been proposed by Sprint should be implemented over a  
8             different timeframe than the adjustments proposed by BellSouth and by Verizon. Mr.  
9             Shafer suggests that Sprint should adjust its prices in four steps, rather than three steps  
10            (a process that has been proposed by all three companies). And he proposes that these  
11            four steps take place over a longer period of time than the period over which  
12            BellSouth and Verizon would make their adjustments.

13  
14     **Q.**     **What reason does Mr. Shafer provide as to why the adjustments proposed by**  
15             **Sprint should take place over a longer period of time?**

16     **A.**     On page 5 of his testimony he claims that this adjustment will "put Sprint's residential  
17             customers more on par with those of BellSouth and Verizon in terms of the amount of  
18             the increase they receive at any one time." It appears that Mr. Shafer is concerned  
19             with the fact that the magnitude of Sprint's adjustments—while extremely small from  
20             the point of view of an average consumer's disposable income—is larger than that of  
21             adjustments made by the other companies.

22  
23     **Q.**     **Is there an obvious reason why the amount of the adjustment proposed by Sprint**  
24             **should be larger?**

25     **A.**     Yes. As Mr. Shafer himself states on page 4 of his testimony, Sprint's intrastate

1 access charges are higher than those of BellSouth. Therefore, re-balancing what is a  
2 relatively higher rate (the access rate) requires a relatively larger adjustment on the  
3 other side (the basic local side).

4  
5 I believe that Mr. Shafer's suggestion is fueled by an understandable, but - in the  
6 context of this legislatively specified process - misplaced concern regarding the  
7 concept of "rate shock" on the part of Sprint's customers, because in his testimony he  
8 follows his description of the suggested revision to Sprint's proposed adjustments with  
9 a discussion of rate shock (Shafer testimony, page 6). While he does not explicitly  
10 state in his testimony that he believes the adjustment proposed by Sprint will cause a  
11 problem stemming from rate shock, he argues that the Legislature had a desire to  
12 "temper rate impacts on consumers." What Mr. Shafer overlooks is that Sprint's  
13 proposal already includes a factor that will "temper rate impacts on customers" in the  
14 sense that Sprint is including an additional customer benefit of approximately \$1.00 to  
15 \$1.25 for customers by including in its proposal a "five free call allowance" on  
16 extended calling services (ECS). This additional customer savings has the effect of  
17 helping to mitigate any perceived differential between Sprint's proposal and  
18 BellSouth's and Verizons' proposals in terms of customer impact.

19

20 **Q. Does Mr. Shafer provide any evidence, analysis, data, or studies to suggest that**  
21 **Sprint's proposed adjustments will have a different impact on customers than**  
22 **BellSouth's proposed adjustments or Verizon's proposed adjustments?**

23 **A. No.**

24

25

1   **Q.**    **Does Mr. Shafer make any reference to any other known example of problems**  
2            **stemming from “rate shock” to use as a benchmark against which to measure**  
3            **Sprint’s proposed adjustment?**

4   **A.**    No.

5  
6   **Q.**    **Are his concerns regarding the possibility of problems stemming from “rate**  
7            **shock” valid?**

8   **A.**    Not really. As discussed in my direct testimony and the testimony of Sprint witness  
9            John Felz, Sprint has engaged in rate rebalancing in other states and it is our  
10           experience that horror stories regarding the effects of “rate shock” are massively  
11           exaggerated. We simply have not seen negative effects of re-balancing rates; we have  
12           not seen large numbers of customers opting to discontinue service; we have not seen  
13           material volumes of complaints filed with state commissions; and we have not seen  
14           any evidence to suggest that any customer’s overall quality of life was negatively  
15           affected by rate rebalancing.

16  
17           Also, it is useful to clarify exactly what we mean by “rate shock.” The fact that a  
18           consumer might be faced with a price adjustment that he or she finds disagreeable  
19           does not constitute “rate shock.” Obviously all consumers would be happy to never  
20           see price increases on the goods and services they buy. And obviously all consumers  
21           would love to pay prices that are below cost—as in the case of basic local telephone  
22           service in Sprint’s Florida serving territory—for everything they buy. But price  
23           adjustments occur throughout any market economy, and prices tend toward cost in a  
24           market economy, and the fact that many local service customers have grown  
25           accustomed to reaping the benefits of cross-subsidization for years is no reason to

1 attempt to maintain an inefficient, unsustainable pricing mechanism any longer than  
2 necessary.

3

4 Finally, when examined in the context of personal income per capita for the state of  
5 Florida, the magnitude of the difference between Sprint's proposed adjustment and  
6 Verizon's (or BellSouth's) proposed adjustment is simply too miniscule to suggest  
7 that Sprint's adjustment would have some effect on consumers that the other firms'  
8 adjustments would not have. Using data contained in the direct testimony of Sprint  
9 witness John Felz, I find that the difference between Sprint's proposed adjustment and  
10 Verizon's proposed adjustment amounts to a difference of 6/100ths of one percent of  
11 monthly personal income per capita in Florida. Mr. Shafer offers no explanation or  
12 analysis as to why he believes such a miniscule difference makes Sprint's proposed  
13 adjustment problematic (in his view).

14

15 **Q. Aside from the fact that Mr. Shafer's concerns are not justified, are there**  
16 **additional reasons to reject his proposed change to Sprint's timeline?**

17 **A.** Yes, there are two additional reasons.

18

19 First, as discussed in the direct testimony of Dr. Ken Gordon, one of the key  
20 advantages of all three companies acting together is that IXCs will be able to  
21 aggregate and coordinate their access cost reductions (Gordon Direct page 16). By  
22 placing Sprint on a different timeline than BellSouth and Verizon, the Commission  
23 forces the IXCs to adjust the implementation of the reductions unnecessarily.

24

25 But more importantly, also as discussed in Dr. Gordon's testimony, it is important to

1           avoid unnecessary marketplace distortions that could affect the purchase decisions of  
2           end-users (Gordon Direct page 15). Mr. Shafer, in suggesting that Sprint extend its  
3           timeframe beyond that of BellSouth and Verizon, introduces exactly such a distortion.  
4           The result of Mr. Shafer's suggestion would be that Sprint could be perceived as  
5           continuing to raise rates long after the other incumbent companies have stopped  
6           raising theirs. As Dr. Gordon discusses, the result would be that regulatory  
7           scheduling, rather than the relative costs and benefits, could become the driving force  
8           behind customer purchase decisions to opt for one provider or another.

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10   **III. DR. DAVID GABEL**

11  
12   **Q. In his testimony Dr. Gabel suggests that the Companies' petitions should not be**  
13   **approved because they "have not made a showing that BLTS (basic local**  
14   **telephone service) is supported and therefore there is no record to support the**  
15   **proposed rebalancing." In your experience has Dr. Gabel taken this position**  
16   **before?**

17   **A.** Yes. In fact, Dr. Gabel has espoused this position for years. More than a decade ago  
18   Dr. Gabel's position was that the loop is not a direct cost of basic service but rather is  
19   a common cost to be allocated across multiple services such as basic service and toll.<sup>1</sup>  
20   The result of such a claim, of course, is that only a portion of loop costs would be  
21   attributed to the provision of local service, therefore one could claim that the prices  
22   charged for local service (purportedly) already covered the cost, and that local service  
23   is not supported.

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<sup>1</sup> See "Pricing of Telecommunications Services" by David Gable and Mark Kennet, *Review of Industrial Organization*, 1993.

1 Many other economists working in telecommunications today disagree with Dr.  
2 Gabel's point of view on that subject. Because this issue has been argued extensively  
3 for many years, and because innumerable pages of testimony have been filed on this  
4 issue with the Florida Commission, the FCC, and undoubtedly every other state  
5 commission or board across the country, in the name of efficiency I will not repeat all  
6 of arguments here. Instead, I include below a quote from Dr. Alfred Kahn, testifying  
7 on this subject before the Pennsylvania Public Utility Commission:

8 "The arguments proffered by these witnesses [that the loop is a shared cost] are  
9 the most persistent weeds in the regulatory garden. Other mainstream economists and  
10 I have dealt with and debunked these claims for years—and I suppose this will remain  
11 our task for as long as parties to proceeding such as this insist on conflating the  
12 politics of setting prices with the economics of determining costs."<sup>2</sup>

13  
14 **Q. Is Dr. Gabel making the same argument—that the loop is a shared cost—in his**  
15 **testimony in this proceeding?**

16 A. It is a variation on that theme. In this proceeding Dr. Gabel does not argue for  
17 allocating loop costs to services such as toll. Rather, he suggests that there are other  
18 services that fall within the category of basic local telephone service and certain costs  
19 associated with the loop should be considered shared costs among these services when  
20 calculating TSLRIC (Gabel page 29.) Sprint witness Kent Dickerson responds to Dr.  
21 Gabel's arguments in his rebuttal testimony and explains that, using Dr. Gabel's own  
22 approach to TSLRIC (as put forth in a 1996 white paper) it is still a fact that basic  
23 local service is supported.

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<sup>2</sup> Rebuttal testimony of Dr. Alfred Kahn before the Pennsylvania Public Utility Commission, Docket No. I-940035, February 15, 1996.

- 1   **Q.    Is Dr. Gabel's contention—that basic local service is not supported—consistent**  
2       **with the FCC's views on the subject?**
- 3   **A.**   Not at all. As Mr. Dickerson correctly points out, when the FCC calculates the cost of  
4       basic local service for purposes of universal service support it includes the cost of the  
5       entire loop in its cost calculation (Dickerson page 10). And the FCC has explicitly  
6       stated that access charges contain implicit subsidies that have permitted carriers to  
7       charge below-cost prices, particularly in high-cost areas (CALLS Order paragraph 24).  
8       Of course, as I indicated in my direct testimony (and as Dr. Gabel cites) the loops  
9       accounts for the majority of the costs of basic local service in high-cost areas. So the  
10      cost of the loop is the thing that, in essence, determines that a high-cost area is in fact  
11      a high-cost area. And according to the FCC, access charges are the things that have  
12      kept prices below cost in those areas. So clearly, according to the FCC, basic local  
13      service is being supported and access charges are the thing doing the supporting.  
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- 15   **Q.    Does this conclude your testimony?**
- 16   **A.**    Yes, it does.  
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