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February 7, 1996

IN REPLY REFER TO:

Tallahassee



BY HAND DELIVERY

Ms. Blanca S. Bayo, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Resolution of Petition to Establish Non
Discriminatory Rates, Terms, and Conditions
for Resale Involving Local Exchange Companies
and Alternative Local Exchange Companies
pursuant to Section 364.161, Florida Statutes
Docket No. 950984-TP

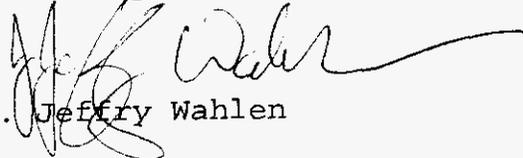
Dear Ms. Bayo:

Enclosed for filing in the above-styled docket are the original and fifteen (15) copies of Sprint-United/Centel's Direct Testimony of F. Ben Poag.

Please acknowledge receipt and filing of the above by stamping the duplicate copy of this letter and returning the same to this writer.

Thank you for your assistance in this matter.

Sincerely,

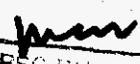

J. Jeffrey Wahlen

JChase

JJW/csu
5/10/96

Enclosures
cc: All parties of record

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FPSC-BUREAU OF RECORDS

DOCUMENT NUMBER-DATE

01449 FEB-7 96

FPSC-RECORDS/REPORTING

UNITED TELEPHONE COMPANY
OF FLORIDA
CENTRAL TELEPHONE COMPANY
OF FLORIDA
DOCKET NO. 950984-TP
FILED: February 7, 1996

1 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

2 DIRECT TESTIMONY

3 OF

4 F. BEN POAG

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

A. My name is F. Ben Poag. I am employed as Director-Tariff and Regulatory Management for United Telephone Company of Florida ("United"). My business mailing address is Post Office Box 165000, Altamonte Springs, Florida 32716-5000. I am responsible for state regulatory matters for United and its affiliate, Central Telephone Company of Florida ("Centel"). Collectively, United and Centel will be referred to as "Sprint-United/Centel" or the "Companies."

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address Sprint-United/Centel's positions on the issues in this docket.

Q. Have Sprint-United/Centel and MFS reached any agreement on unbundling issues?

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FPSC-RECORDS/REPORTING

1 A. No. While the companies have been negotiating the
2 unbundling issues as required by the statute, they have
3 not been able to reach an agreement. Nevertheless,
4 Sprint-United/Centel are continuing to negotiate with MFS
5 and hope to reach an agreement on the issues between
6 them.

7

8 Q. What elements should be made available by Sprint-
9 United/Centel to MFS on an unbundled basis?

10

11 A. At this time, Sprint-United/Centel proposes that the
12 unbundled elements of its special access tariff represent
13 the elements that would be provided to MFS on an
14 unbundled basis. This will allow the Companies to
15 provide the same unbundled services on a
16 nondiscriminatory basis to ALECs, IXCs, AAVs, and
17 cellular providers at the same rates, terms and
18 conditions.

19

20 Q. What are the appropriate financial arrangements for each
21 of the unbundled elements?

22

23 A. The provision of unbundled services should be priced
24 consistent with the Companies' special access tariffs.
25 This will provide the services on a nondiscriminatory

1 basis to ALECs, IXCs, AAVs, and cellular providers at the
2 same rates, terms and conditions.

3

4 Q. How were the prices for special access developed?

5

6 A. These prices were developed based on the underlying
7 incremental cost, and include a contribution to shared
8 and overhead costs.

9

10 Q. Why not establish separate prices for these services for
11 ALECs at incremental cost?

12

13 A. Several reasons. First, these services are cross elastic
14 with other services, e.g., toll and switched access
15 services, which provide substantial contribution. A
16 price reduction for these services could have substantial
17 negative impacts on the financial integrity of the
18 Companies.

19

20 Second, it would be inappropriate and discriminatory to
21 offer these services to ALECs at prices that are
22 different from the prices AAVs, IXCs, and cellular
23 providers pay for these same services. If ALECs are able
24 to obtain these services at lower prices than IXCs, the
25 ALECs could use the additional margin to undercut an

1 IXC's' prices to win the customers and then resell the
2 same or a different IXC's toll services. This would be
3 a significant advantage to the ALEC since the ALEC could
4 use these same facilities to provide both local and toll
5 services.

6

7 Q. Why not reduce the prices to IXCs, AAVs and cellular
8 carriers?

9

10 A. Prices for these services contain contributions to shared
11 and overhead costs as do the prices for switched access
12 charges. Prices for these and other services have
13 traditionally been set to keep basic service rates lower
14 than would otherwise be the case. Not only would the
15 Companies lose the existing contributions to costs from
16 these services but you would see migration to these
17 services from other services as the prices were
18 decreased. This migration, or substitution of services,
19 would result in the loss of the contribution from the
20 substitute services. In the short run there would be a
21 significant financial impact to the Companies, however,
22 over time these would be costs that would need to be
23 recovered from end users of basic and vertical services.
24 It is inappropriate to transfer recovery of these costs
25 to only the ILEC's end users.

1 Q. Are there other reasons that the prices for unbundled
2 network elements should not be priced at long run
3 incremental cost?

4
5 A. Yes. First, it is generally accepted that incremental
6 costing methods are not used for price setting but are
7 rather a price floor which is used to test for cross-
8 subsidization. Second, firms have other costs in
9 addition to the incremental cost of products and services
10 which must be recovered if the firm is to maintain
11 profitability. These other costs can generally be
12 categorized as shared or joint costs and overhead costs.
13 An example of shared cost would be a software program
14 which provides two features, for example, call waiting
15 and three-way calling. By the definition of an
16 incremental cost study, the shared software cost would
17 not be included in the incremental cost of either of the
18 individual features. However, unless you had that
19 software in place you could not provide the service and
20 unless you could recover the software cost with revenues
21 from one or both features, it would not be a financially
22 prudent decision to offer the services.

23
24 In addition to shared costs, there are also overhead
25 costs. From a facilities perspective, the SS7 network

1 would be a good example of an overhead cost. It is a
2 network manager that makes all the other pieces work more
3 efficiently. These, and many more real costs, do not get
4 included in the economic definition of an incremental
5 cost study. However, they are necessary to efficiently
6 and effectively provide the requested services, and they
7 do need to be recovered for the firm to be profitable.

8

9 Q. Does having some of an ILEC's shared and overhead costs
10 included in its prices for unbundled elements shield
11 these costs from market pressure?

12

13 A. Absolutely not. ILECs have significant pressures to
14 reduce costs and increase productivity to compete
15 effectively in the marketplace. The idea that these
16 cost-cutting activities will be divided between
17 competitive and non-competitive services is totally
18 illogical.

19

20 Q. Do historical pricing policies impact this issue as well?

21

22 A. Yes. Based on all the evidence I have seen, and
23 logically, the new entrants will be entering markets
24 where there is a significant revenue/cost margin for the
25 packages of services for which new entrants will be

1 competing with the LECs. These revenue/cost margins
2 result from the social pricing of LECs' services under
3 rate base, rate of return regulation. Under rate base,
4 rate of return regulation, a LEC's basic service rates
5 were developed based on a residual revenue requirement
6 basis; cost of individual services was not a factor.
7 Basic service prices were kept low with the shortfall of
8 revenues being made up from other services, e.g., toll,
9 access and other discretionary services.

10

11 The net result of these prior pricing decisions is that
12 revenues from Sprint-United/Centel's high density low
13 cost exchanges provide contribution to its high cost low
14 density exchanges. In the historical monopoly
15 environment, such pricing could be maintained. However,
16 with local competition, these embedded revenue/cost
17 mismatches, and Sprint-United/Centel's US/COLR
18 obligations, new entrants already have significant market
19 opportunities. Therefore, shifting additional shared and
20 overhead costs to the LECs to attempt recovery in an
21 environment where existing revenue/cost distortions
22 already favor new entrants is inappropriate because it
23 will exacerbate these revenue/cost distortions.

24

25 Q. Please summarize your concerns regarding an incremental

1 cost approach to pricing unbundled elements.

2

3 A. ILECs are already disadvantaged in the marketplace by the
4 fact that their rates have historically been set based on
5 the social objective to maintain low local service rates.
6 This social objective has resulted in the prices of other
7 LEC services; e.g., access and toll, being priced higher
8 than would otherwise be the case. The result is that new
9 entrants already have many opportunities to undercut
10 LECs' prices without shifting additional shared and
11 overhead costs to the LECs' end users as a result of
12 underpricing unbundled elements.

13

14 Q. Should the sum of the prices of the parts of an unbundled
15 service be equal to the price for the same package of
16 services on a bundled basis?

17

18 A. No, there are additional operational requirements and
19 costs associated with offering the unbundled services.
20 It may be as simple as additional transaction costs, but
21 could be much more complicated. For example, if the
22 Companies can do end-to-end testing of a bundled service
23 remotely, but must dispatch to test an unbundled service,
24 not only are there the increased costs of the dispatch,
25 but there will be different operational requirements in

1 terms of test procedures and testing and maintenance
2 coordination with the unbundled services subscriber.
3 Obviously, these additional requirements will increase
4 the costs, and those costs should be visited on the ALECs
5 that cause those costs to be incurred. For these
6 reasons, it would not be unreasonable to expect that the
7 sum of the price of unbundled elements would exceed the
8 price of the bundled service itself.

9

10 Q. Can you provide an example?

11

12 A. Yes. A good example is where the loop is actually
13 unbundled from the switch (such as a basic service
14 business line) and where the actual loop element
15 terminates into the central office via a high capacity
16 service. In that situation, in order to provide the loop
17 to the ALEC it has to be removed or separated from the
18 high capacity service. This requires special design and
19 the use of separate facilities and/or the use of
20 additional multiplexing (demux) equipment to isolate the
21 requested loop for connection to the ALEC's facilities.

22

23 Q. What are the appropriate technical arrangements for the
24 provision of the unbundled elements?

25

1 A. The technical arrangements contained in the Companies'
2 special access tariff provide a good point of beginning.
3 For example, voice grade local loops are already
4 available today from the Companies' special access
5 tariff. Alterative Access Vendors ("AAVs") order these
6 local channels today, and ALECs can do the same.
7 Additionally, any interoffice transport facilities needed
8 to connect to an ALEC are also available from the special
9 access tariffs.

10

11 Sprint-United/Centel are in the process of considering
12 whether other elements should be offered, the technical
13 arrangements for the provision of those elements and
14 whether its special access tariff should be revised
15 accordingly.

16

17 Q. What additional unbundled services, other than the
18 special access services, do the Companies propose to
19 offer?

20

21 A. The Companies propose to provide unbundled ports which
22 provide the capability to originate and/or terminate
23 local, long distance, directory assistance, operator, and
24 911 type calls. The ports, when connected to end users
25 via a loop, will effectively provide a residence or

1 business dial tone service.

2

3 Q. What arrangement, if any, are necessary to address other
4 operational issues?

5

6 A. It is not necessary for the Commission to address
7 detailed operational issues at this time. Sprint-
8 United/Centel are willing to work in good faith with MFS
9 and other ALECs to address their operational concerns.
10 Since it will be difficult to predict the areas in which
11 the Commission will be called upon to arbitrate
12 operational disagreements between Sprint-United/Centel
13 and ALECs, it is premature to decide detailed operational
14 issues at this time. Rather, detailed operational issues
15 are best left to the parties, with resolution by the
16 Commission on a case-by-case basis when disagreements
17 occur.

18

19 Q. Does this conclude your direct testimony?

20

21 A. Yes, it does.

22

23

24

25 utd\950984.tst

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by U. S. Mail or hand delivery (*) or overnight express (**) this 7th day of February, 1996, to the following:

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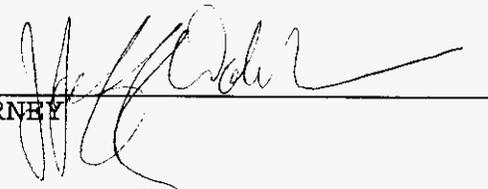
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