

1 BELLSOUTH TELECOMMUNICATIONS, INC.
2 SUPPLEMENTAL REBUTTAL TESTIMONY OF A. J. VARNER
3 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
4 DOCKET NO. 920260-TL
5 October 17, 1996
6
7
8 Q. Please state your name, employer, position and business address.
9
10 A. My name is Alphonso J. Varner. I am employed by BellSouth
11 Telecommunications, Inc. ("BellSouth" or "BST") as Senior Director for
12 Regulatory Policy and Planning for the nine state BellSouth Region.
13 My business address is 675 West Peachtree Street, Atlanta, Georgia.
14
15 Q. Are you the same Alphonso J. Varner who filed direct testimony on
16 behalf of BellSouth on July 31, 1996?
17
18 A. Yes, I am.
19
20 Q. What is the purpose of your testimony?
21
22 A. My testimony rebuts the amended direct testimony filed in this case by
23 Thomas Erwin Allen, Jr. of Intermedia Communications, Inc. on
24 September 11, 1996, and addresses the modified issue concerning the
25 rating of N11 service.

1

2 Q. Palm Beach Newspapers, Inc. and Florida Today have modified their
3 issue on N11 service and are now seeking a reduction of BellSouth's
4 N11 service tariff so that the N11 customers pay a flat charge of \$.01
5 per minute or the current monthly minimum, whichever is greater.
6 Does BellSouth agree with this proposal?

7

8 A. No. This proposal is inappropriate from a cost perspective and from a
9 market perspective. First, BellSouth's costs are associated with
10 switching and transport of N11 calls. Such costs are incurred both per
11 minute and per message. The proposal appears to ignore that there is
12 a per message cost. Second, the market response indicates that
13 BellSouth existing rates are appropriate. The current demand exceeds
14 the quantity of numbers which are available in the major markets,
15 where there is currently a waiting list for N11 codes (there have been
16 approximately 51 applications for the limited N11 codes in Florida since
17 the service was introduced). The price for the service is clearly within
18 the market willingness to pay. Therefore, the current rate levels and
19 structure are appropriate, and the modified N11 proposal should be
20 rejected.

21

22 ~~Q. Have you previously filed rebuttal to Mr. Allen's direct testimony?~~

23

24 ~~A. Yes, I have.~~

25

1 Q: Please state your name, business affiliation, address, and on whose behalf you
2 are testifying?

3 A: My name is Douglas S. Metcalf. I am President of Communications Consultants,
4 Inc., 400 N. New York Avenue, Suite 213, Winter Park, Florida 32790-3159. CCI
5 provides regulatory, tariff and management assistance to clients using or providing services
6 affected by regulation. My responsibilities include the examination of costing
7 methodologies and rate design policy. I have previously testified on behalf of the Florida
8 Ad Hoc Telecommunications Users' Committee (Ad Hoc) in this proceeding.

9
10 Q: What is the Florida Ad Hoc Telecommunications Users' Committee?

11 A: It is an ad hoc group of large users of business telephone services within the state
12 of Florida. The members are major customers of the local exchange companies who are
13 vitally interested in the fairness of any tariff structure or rate changes affecting business
14 services. Further, they are users who are very interested in fostering full and fair
15 competition in the telecommunications marketplace. The current members of Ad Hoc are:

16	Advantis (Sears/IBM)	Great Western Bank
17	Alarm Assn. of Florida	Harris Corporation
18	American Express Co.	Honeywell Protection Svcs.
19	Barnett Technology Corp.	NationsBank of Florida
20	Burdine's	Publix Supermarkets
21	Dean Witter Reynolds	Seimens/Stromberg-Carlson
22	Equifax, Inc.	Southeast Switch (HONOR Group)
23	First Union National Bank	State of Florida - DMS
24	Florida Informanagement Svcs. (FIS)	SunTrust Service Corp.

25

26 Q: What is the purpose of your testimony?

27 A: The purpose of my testimony is to discuss and support the comments in the Joint
28 Proposal for Disposition of \$48 Million which was submitted by Ad Hoc, MCI, AT&T,
29 FIXCA, Sprint, McCaw Communications, and later joined by the Department of Defense.

1 I will also comment on the proposal which has been made by BellSouth. These proposals
2 were made to achieve the \$48 million (\$48M) rate reduction for 1996 which was agreed to
3 and required by the Stipulation and Agreement dated January 5, 1994, and the Implementa-
4 tion Agreement dated January 12, 1994 in settlement of SBT's 1994 rate case.

5
6 **Q. What are the basic principles that should guide the Commission during their**
7 **deliberations in this refund proceeding?**

8 **A.** The Commission's task in this proceeding is twofold: First, the Commission should
9 target the refund to the parties who have paid the most in excessive contribution and rates
10 over the years. Second, the Commission should effectuate this refund in a manner that
11 enhances competition, on a going forward basis, as directed by the Legislature in the
12 telecommunications legislation which was passed in the 1995 session. Ad Hoc believes
13 that, of the proposals currently before the Commission in this proceeding, only the Joint
14 Proposal filed by Ad Hoc and others reflects these two factors.

15
16 **Q. Please explain the differences in the Joint Proposal and BST's proposed**
17 **reductions with respect to their impact on business users?**

18 **A.** First, the Commission will note that BST's proposed reduction in PBX and DID
19 rates exceeds \$15M, while Ad Hoc's proposal would decrease business user rates by only
20 \$11M. However, BST's reduction, although it is greater than that proposed by Ad Hoc and
21 other parties to the Joint Proposal, is not an equitable reduction for BST's current business
22 customers.

23
24 **Q. Please describe the factors which lead you to conclude that business users are**
25 **better off foregoing the higher total PBX refund that BST has proposed.**

1 A. BST's proposal suffers from two serious flaws. The rate reductions filed May 31,
2 1996 will skew competition in business services in favor of BST (and to the ultimate
3 detriment of other BST ratepayers), and the proposed rate reduction inequitably favors new
4 business customers whose payments did not contribute to the overearnings being refunded.

5

6 **Q. Please address your concern that the BST proposal will unfairly skew**
7 **competition for business users in favor of BST.**

8 A. BST's proposal unfairly seeks to "lock in" business users during a time that historic
9 competitive opportunities will otherwise be available to these customers. Specifically, BST
10 has tied its proposed business customer refund to the acceptance of long term customer
11 contracts. In previous rate proceedings, Ad Hoc has testified, BST has agreed, and the
12 Commission's staff has concluded in its recommendations, that PBX trunk rates across-the-
13 board are priced significantly over cost. Yet BST's proposal unfairly holds hostage refunds,
14 which are rightfully due to these customers, to a scheme that would now deny these
15 customers the fruits of local competition.

16

17 **Q. Please explain your concern that BST's proposal will lessen competition and**
18 **thereby, will hurt all current telecommunications customers within Florida.**

19 A. This proposal stifles competition, since it proposes to lower rates for subscribers
20 of new DID services and long term PBX contracts. Lowering (in fact, virtually eliminating)
21 nonrecurring charges for new subscribers has the impact of making BST's services
22 significantly more attractive to new and expanding businesses within Florida. These are not
23 the users who paid the overearnings in the past, but they *are* one of the larger potential
24 markets for the new competitive telecommunications suppliers seeking a foothold in the
25 business market with their offerings. BST's proposal would allow it to use its ill gained

1 earnings to leverage itself against would-be competitors in the local market. Since business
2 users are usually the initial target market of competitors, and have facilitated nascent
3 competitors in other market sectors to gain a foothold, BST's proposal will have the longer
4 term effect of lessening competition for all users, including residential users.

5
6 **Q. Please address your point that the proposed rate reduction inequitably favors**
7 **new business customers whose payments did not contribute to the overearnings**
8 **and the consequent refund.**

9 A. As I mentioned earlier, it is Florida's current business customers who have paid the
10 high business and access rates in existence today. Their rates are the rates that should be
11 lowered. However, BST's proposed rate structure targets new customers by
12 eliminating/reducing non-recurring charges associated with ordering new or additional
13 ESSX, Multiserve, and DID services. This particular reduction badly misaligns costs and
14 benefits -- a result which is just the opposite of that historically urged by BST's frequent
15 reliance on principles of 'cost causation.' This proposal is simply inequitable.

16
17 **Q. Could you please respond to Mr. Varner's contention that this contract**
18 **proposal responds to customer requests for "rate stabilization" (Page 9.1)?**

19 A. As the Commission knows, Ad Hoc is the principal advocate of business customers
20 appearing before the Commission in telecommunications matters. Ad Hoc and its members
21 have never communicated a desire to BST for this particular rate structure, and Mr. Varner
22 has not discussed it with Ad Hoc or its members. Accordingly, the Commission should not
23 be misled into believing that there is a large nucleus of business users advocating this
24 particular BST rate structure based upon a desire for this form of "rate stabilization."

25

1 Q. How does lowering PBX trunks \$11M on an across-the-board basis, as
2 suggested in the Joint Proposal, increase competition and customer choice?

3 A. PBX trunk service competes with ESSX, yet it is priced significantly above its
4 relative costs. ESSX, however, is not forced to recover revenues so substantially above its
5 costs. This unfair pricing differential hinders fair competition between PBX service and
6 ESSX service, and accordingly denies the full benefits of competition to the customer.

7 For example, two particular elements of PBX service, PBX trunks and Direct
8 Inward Dial (DID), are items which have functionally equivalent features as compared to
9 ESSX. Yet the rates are significantly higher for PBX, even though similar facilities are
10 used and the costs of the elements are essentially the same. Disparities like these make
11 PBX uncompetitive with ESSX, thereby hurting competition in the marketplace.

12

13 Q. Does ESSX service *cost* less to provide than PBX service?

14 A. No. As I stated in last year's \$25M refund proceeding, if the cost of the service
15 is based on the cost of the facilities used to provide it — the most logical way to view the
16 cost of a service — ESSX should be priced significantly higher than PBX service, because
17 ESSX uses more plant and facilities to operate than does PBX. Accordingly, if the aim of
18 the Commission is to foster competition for BST's services, it must take these cost
19 considerations into account.

20

21 Q. How did this ESSX/PBX pricing disparity occur?

22 A. Basically because PBX rates were initially set long ago based on an index of its
23 perceived "value of service" relative to a B-1 line. ESSX, a newer offering, came along
24 later and was priced based on the additional "incremental cost" of providing that service.
25 If the Commission were to direct that PBX service be "incrementally costed" and priced to

1 produce relatively the same percent of contribution as ESSX, PBX vendors would have an
2 opportunity to compete in the large user market, and customers would have an opportunity
3 to purchase their customer provided equipment (CPE) based on the features of the
4 equipment rather than the nonsensical cost of the telephone lines that connect it.

5

6 **Q. Summarize your reasons why the some of \$48M should be applied first to**
7 **repricing PBX trunks and DID to levels of contribution equivalent to ESSX**
8 **service?**

9 A. First, because the resultant "leveling of the playing field" would meet the
10 Legislature's obvious intent to foster competition on a local basis along with the attendant
11 customer benefits. Second, it would more correctly align service prices with their costs,
12 and would avoid an otherwise inequitable distribution of the refund.

13

14 **Q. Why should access rates be lowered beyond the levels agreed to in the original**
15 **stipulation agreement?**

16 A. Interstate access charges have decreased further since the original target was set
17 during the 1994 settlement discussions. Applying some of the refund to that category would
18 assure that Florida's access charges would remain closer to the interstate average.

19

20 **Q. Would large users be a big beneficiary of that alternative?**

21 A. Large users would benefit less in general than other users. This is because the
22 largest users have purchased dedicated access circuits directly to their IXCs, and often avoid
23 the originating or terminating access charge for calls to their facilities connected by those
24 means. The biggest beneficiaries would be the residential and small/medium business users
25 who ultimately pay the excessive access rates within their toll service charges.

1 Q: What is your recommendation to the Commission in this case?

2 A: As the Legislature intended, the Commission can take a major step toward
3 proactively fostering the development of fair and effective competition by using the
4 available funds for some purpose that encourages direct competition between BST and
5 existing or emerging players in the telecommunications marketplace. I believe this can best
6 be done by lowering the cost of all BST PBX trunks to an amount which provides the same
7 level of contribution for those loop/path facilities as for BST's proprietary ESSX product.
8 DID service is similarly overpriced and should also be adjusted. Lowering intrastate access
9 charges to, or even beyond, interstate access levels is also appropriate. I specifically
10 recommend that the Commission not accept BST's suggestions, as they would allow the
11 Company to leverage itself for future competition by the use of an anticompetitive rate
12 structure.

13

14 Q: Does this conclude your testimony?

15 A: Yes, it does.