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August 27, 2003

Ms. Blanca S. Bayo, Director  
Division of the Commission Clerk  
and Administrative Services  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Tallahassee, FL 32399-0850

030867-TL

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Re: Docket No.  
Petition of Verizon Florida Inc. to Reform Its Intrastate Network Access and  
Basic Local Telecommunications Rates in Accordance with Florida Statutes,  
Section 364.164

Dear Ms. Bayo:

An original and 15 copies of the following documents are enclosed for filing:

- 08002-03 1. Verizon Florida Inc.'s Petition to Reform Its Intrastate Network Access and  
Basic Local Telecommunications Rates in Accordance with Florida Statutes,  
Section 364.164;
- 2. Direct Testimonies of Dr. Carl R. Danner, Orville D. Fulp, Dr. Kenneth Gordon  
and Evan T. Leo; 08003-03 08004-03 08005-03  
08006-03
- 08007-03 3. Request for Confidential Classification and Motion for Protective Order.

Service has been made as indicated on the Certificate of Service. If there are any  
questions regarding this matter, please contact me at 813-483-1256.

Sincerely,

Richard Chapkis  
RC:tas  
Enclosures

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**CERTIFICATE OF SERVICE**

I HEREBY CERTIFY that copies of the foregoing were sent via U.S. mail on August 27, 2003 to the parties on the attached list.

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition of Verizon Florida Inc. to Reform )  
Its Intrastate Network Access and Basic Local )  
Telecommunications Rates in Accordance with )  
Florida Statutes, Section 364.164 )  
\_\_\_\_\_ )

Docket No. 030867-JL  
Filed: August 27, 2003

PETITION OF VERIZON FLORIDA INC.  
TO REFORM ITS INTRASTATE NETWORK ACCESS AND  
BASIC LOCAL TELECOMMUNICATIONS RATES IN  
ACCORDANCE WITH FLORIDA STATUTES, SECTION 364.164

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Pursuant to Florida Statutes, Section 364.164,<sup>1</sup> Verizon Florida Inc. (Verizon) submits this petition to reform its intrastate network access and basic local telecommunications rates.

## **I. INTRODUCTION AND BACKGROUND**

In the recently enacted Tele-Competition Innovation and Infrastructure Enhancement Act of 2003 (Act), the Legislature and the Governor expressly found that the competitive provision of local exchange telecommunications services “is in the public interest and will provide customers with freedom of choice, encourage the introduction of new telecommunications service, encourage technological innovation, and encourage investment in telecommunications infrastructure.”<sup>2</sup> In furtherance of these goals, the Act authorizes Verizon to petition the Commission to offset, over a period of two to four years, a reduction in intrastate access revenues with an increase in basic local service revenues.<sup>3</sup>

In conformance with the Act, Verizon seeks over two years to bring its intrastate access rates to parity with its interstate access rates and to offset that decrease with a corresponding increase in its basic local service rates. Verizon’s rate rebalancing plan will remove support for its basic local services and produce prices that are more closely aligned with the costs of providing service.

Rebalancing retail rates in this fashion will promote competition by enhancing the ability of competitors to enter and serve the basic local exchange market. Enhanced competition will benefit consumers by forcing all competitors to operate more efficiently and

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<sup>1</sup> Hereinafter, all statutory references are to the Florida Statutes.

<sup>2</sup> Section 364.01(3).

<sup>3</sup> Section 364.164.

lower their prices wherever possible. It will also benefit residential consumers in particular by making them a more attractive target for efficient competitors that have every incentive to meet their demands with new and innovative products and services.

In addition, the establishment of more accurate retail rates will benefit subscribers by allowing them to make more intrastate long distance calls at lower prices. This will be especially beneficial for an expanded base of Lifeline customers, who will benefit from decreased intrastate long distance prices but will not have to pay increased basic local rates.

Because Verizon's rate rebalancing plan advances the public interest by spurring competition and creating a more attractive local exchange market for residential consumers – consistent with the requirements of the Act – Verizon's plan should be adopted in its entirety.

## **II. AN OVERVIEW OF VERIZON'S RATE REBALANCING PLAN**

As Verizon witness Fulp explains, Verizon's rate rebalancing plan will restructure its intrastate network access and basic local telecommunication services rates in accordance with the Act. More specifically, Verizon's rate rebalancing plan will reduce the Company's intrastate total average revenue per minute (APRM) composite rate from \$.0485047 to \$.0112453 over two years,<sup>4</sup> which will result in an intrastate revenue decrease of \$76.8 million.<sup>5</sup> This rate reduction will bring Verizon's intrastate access APRM composite rate to parity with its interstate access APRM composite rate.<sup>6</sup>

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<sup>4</sup> Direct Testimony of Orville D. Fulp On Behalf Of Verizon Florida Inc. (Fulp Direct Testimony), filed concurrently herewith, at 7:18-19.

<sup>5</sup> Id. at 8:2.

<sup>6</sup> Id. at 7:20-22.



To bring its intrastate access rate to parity with its interstate access rate, Verizon will eliminate or significantly reduce four intrastate access rate elements. Specifically, the Company will: (1) eliminate the interconnection charge; (2) eliminate the information surcharge; (3) eliminate the originating carrier common line charge (CCL); and (4) decrease the terminating CCL from \$.0246950 to \$.0023635.<sup>7</sup>

To offset the intrastate access rate reductions and achieve revenue neutrality, Verizon will increase its basic local residential revenues by approximately \$71.4 million and its basic local business revenues by approximately \$5.4 million – a total increase in basic local service revenues of approximately \$76.8 million.<sup>8</sup>

On the consumer side, Verizon will raise the basic monthly recurring charges in each of its five rate groups by \$4.61.<sup>9</sup> These increases will take place over two years in increments of \$2.25 the first year and \$2.36 the second year.<sup>10</sup> Verizon will also raise the residence non-recurring network establishment charge from \$20.00 to \$25.00, and the non-recurring central office connection charge from \$35.00 to \$40.00.<sup>11</sup> Both of these increases will take place in the first year.<sup>12</sup>

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<sup>7</sup> Id. at 13:4.

<sup>8</sup> Id. at 14:23-15:1.

<sup>9</sup> Residential rates currently range from \$10.12 in Rate Group 1 (the least dense rate group) to \$12.10 in Rate Group 5 (the most dense rate group). Id. at 15:3-4.

<sup>10</sup> Id. at 15:4-6.

<sup>11</sup> Id. at 15:6-9.

<sup>12</sup> Id. at 15:8-9.

In accordance with Section 364.10(3)(c), the foregoing rate increases will not be imposed on Lifeline customers.<sup>13</sup> Verizon will also implement new qualification standards for lifeline service that should substantially increase the number of customers eligible for its benefits.

On the business side, Verizon will raise the basic monthly recurring charges in each of its five rate groups to \$32.00.<sup>14</sup> The rate increase up to \$32.00 in Rate Group 5 (the most dense rate group) will take place in the first year, and the rate increases in the other four rate groups will take place over two years.<sup>15</sup> Verizon will also raise the business non-recurring network access establishment charge from \$33.90 to \$34.00.<sup>16</sup>

Upon approval of Verizon's rate rebalancing plan, the Company will file tariffs setting forth the first year's proposed rates and the Commission will have 45 days to approve those tariffs. The rates in the first year tariffs will be the same as those in the illustrative tariffs submitted with this filing.<sup>17</sup> The second-year rates will necessarily be somewhat different than those in the illustrative tariffs. Because the revenue neutral rate adjustments must take place once each year and must be made using the most recent 12 months demand units, the rate increases made after the first year will have to be updated to account for the

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<sup>13</sup> Id. at 16:5-18.

<sup>14</sup> Single-line business rates currently range from \$24.47 in Rate Group 1 (the least dense rate group) to \$30.35 in Rate Group 5 (the most dense rate group). Id. at 15:11-12.

<sup>15</sup> Id. at 15:11-16.

<sup>16</sup> Id. at 15:16.

<sup>17</sup> Id. at Exhibit ODF-4.

difference between the current units and the actual updated units, which will become available only at the end of the first year.<sup>18</sup>

**III. VERIZON'S RATE REBALANCING PLAN MEETS THE CRITERIA THE COMMISSION MUST CONSIDER IN REACHING ITS DECISION ON THIS PETITION**

Section 364.164 establishes four criteria that the Commission must consider in reaching its decision on this Petition. Under Section 364.164, the Commission shall consider whether Verizon's rate rebalancing plan will:

1. remove current support for basic local telecommunications services that prevents the creation of a more attractive competitive local exchange market for the benefit of residential consumers (Section 364.16(1)(a));
2. induce enhanced market entry (Section 364.16(1)(b));
3. require intrastate switched network access rate reductions to parity over a period of not less than two years nor more than four years (Section 364.16(1)(c)); and
4. be revenue neutral, as that term is defined in the statute (Section 364.16(1)(d)).

As discussed below, Verizon's plan meets the foregoing criteria.

**A. The Rate Rebalancing Plan Removes Current Support For Basic Local Telecommunications Services (Section 364.16(1)(a))**

Verizon's plan removes current support for basic local telecommunications services. According to Verizon witness Dr. Carl R. Danner, a supported service is one that (1) is priced below its incremental cost or (2) even if it covers its incremental cost, does not make

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<sup>18</sup> Fulp Direct Testimony at 18:2-7.

an appropriate contribution towards joint and common costs.<sup>19</sup> As Verizon witness Mr. Orville D. Fulp demonstrates, Verizon's basic local residential services receive support because they are priced below incremental cost, and thus do not make any contribution to joint and common costs.<sup>20</sup> Verizon's rate rebalancing plan removes support from its basic local services, as Mr. Fulp explains, by increasing the price of these services.<sup>21</sup>

**1. Verizon Properly Estimated The Incremental Cost Of Provisioning Basic Local Services Using Commission-Approved UNE Rates**

Verizon relied on Commission-approved unbundled network element (UNE) rates to estimate the incremental cost of provisioning basic local service.<sup>22</sup> It was proper to rely on UNE rates for this purpose because they conservatively estimate the total service long-run incremental costs (TSLRICs) of provisioning basic local services.<sup>23</sup> First, these rates exclude retailing costs (e.g. marketing and advertising) and retail directory listing costs that Verizon actually incurs to provision these services, thus understating the estimated TSLRIC.<sup>24</sup> Second, they do not include features.<sup>25</sup> Third, they reflect other TELRIC

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<sup>19</sup> Direct Testimony of Carl R. Danner On Behalf Of Verizon Florida Inc. (Danner Direct Testimony), filed concurrently herewith, at 4:6-10. Verizon cannot profitably sustain its services merely by covering only its incremental cost. Id. at 4 (ft note 2).

<sup>20</sup> Fulp Direct Testimony at 24:1-16.

<sup>21</sup> Fulp Direct Testimony at 18:23-25.

<sup>22</sup> Id. at 19:5-11.

<sup>23</sup> In other words, if Verizon were to have used TSLRIC costs in lieu of UNE-P rates, its cost estimate would have been significantly higher resulting in a showing that less contribution is made toward the incremental and joint and common costs of providing basic local services.

<sup>24</sup> Fulp Direct Testimony at 20:9-14.

<sup>25</sup> Id. at 20:16.

assumptions that understate the true TSLRIC of provisioning basic local services.<sup>26</sup> Fourth, notwithstanding Verizon's previously-stated concerns about the accuracy of these UNE rates, they are suitable for establishing a lower bound for these costs without any further need for review.

## **2. Verizon Properly Estimated The Incremental Cost Of Provisioning Basic Local Services At The Rate Group Level**

Verizon estimated the TSLRICs of provisioning basic local services utilizing Commission-ordered UNE rates at the rate group level, as opposed to the exchange or total company level.<sup>27</sup> It is proper to estimate the cost at the rate group level because current and proposed prices are set at that level.<sup>28</sup> Due to cost variations, establishing prices at the exchange level would create a more complicated rate structure and cause consumers in the higher-cost exchanges to pay higher basic local rates than those established in the rate rebalancing plan. For example, a customer in Indian Lake, a Zone 3 exchange, would pay significantly more than the conservative \$35.75 estimated UNE-P rate if prices were calculated at the exchange level. Based on Verizon's filed UNE cost in docket number 990649B-TP, Indian Lake's cost is 75% higher than the average Zone 3 cost. Therefore,

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<sup>26</sup> Id. at 20:9-14. In fact, Verizon has appealed the UNE rates to the Florida Supreme Court precisely because they understate Verizon's cost to render service. Thus, these rates are conservative and set a value that is below the true cost of provisioning basic local service. Id. at 20:1-7.

<sup>27</sup> Id. at 21:7-17.

<sup>28</sup> Id.

Indian Lake's exchange level estimated UNE-P cost would be \$62.56 (ordered rate of \$35.75 x 1.75).<sup>29</sup>

**B. Verizon's Rate Rebalancing Plan (1) Facilitates The Creation Of A More Attractive Local Exchange Market For The Benefit Of Residential Consumers And (2) Induces Enhanced Market Entry (Section 364.164(1)(a)– (b))**

By removing current support for basic local residential services, Verizon's rate rebalancing plan (1) facilitates the creation of a more attractive local exchange market for the benefit of residential consumers and (2) induces enhanced market entry.

The existing below cost rates for basic local residential services, which were developed in a less competitive era, are inconsistent with the development of competition and the maximization of social welfare. After all, these prices reflect a past policy objective – namely, the use of implicit support for basic local rates to promote universal service – that is inconsistent with current public policy and market realities.<sup>30</sup> As a result, the existing below cost rates inhibit market entry, distort competition and harm consumers.

Below cost basic local residential rates inhibit market entry and distort competition because they create false price signals that exclude providers that would enter the market if prices were set at efficient levels. Distorted price signals exclude efficient providers from the market because economically rational firms will only enter the market if they can produce services at a lower price than the incumbent local exchange carrier (ILEC), and still remain profitable.<sup>31</sup>

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<sup>29</sup> Id.

<sup>30</sup> 47 USC Section 253(a).

<sup>31</sup> Danner Direct Testimony at 14:20-21 and 7:14-17. Because Florida residential basic local prices are lower than those in many other states, and in fact lower than the national average, the problem facing potential new entrants as a result of these low rates is likely to be even more severe and

Below cost basic local residential rates also harm consumers for several reasons. First, consumers must in effect pay a “tax” (i.e., higher prices) on intrastate long distance services to support basic local services.<sup>32</sup> Second, paying artificially high rates for intrastate long distance services inappropriately discourages consumers from making long distance calls.<sup>33</sup> Third, by reducing the incentive for providers to enter and compete in the local exchange market, below cost basic local residential rates diminish customer choice by impeding new entrants from offering alternative products and services.<sup>34</sup>

Removing current support for basic local rates, as Verizon intends, will enhance market entry. Competitors will be able to offer services at a price equal to or lower than that offered by Verizon, thereby making the local exchange market more attractive to potential competitors.<sup>35</sup> In addition, it will stimulate demand for intrastate long distance services. This will promote market entry by increasing the size of the market opportunity for competitors.<sup>36</sup> Moreover, it will signal investors that the Governor, Legislature and this Commission are serious about promoting competition and removing impediments to its success. This will inspire confidence in the local telecommunications market and attract

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pronounced in Florida than in other states. Therefore, it is important that Florida policymakers tackle this problem sooner rather than later. Direct testimony of Dr. Kenneth Gordon on behalf of Verizon Florida Inc., BellSouth Telecommunications, Inc., and Sprint-Florida Inc. (Gordon Direct Testimony), filed concurrently herewith, at 10:16-11:11.

<sup>32</sup> Danner Direct Testimony at 5:16-6:4; Gordon Direct Testimony at 12:22-13:5.

<sup>33</sup> Danner Direct Testimony at 5:16-6:4; Gordon Direct Testimony at 12:22-13:5.

<sup>34</sup> Danner Direct Testimony at 12:6-12.

<sup>35</sup> Danner Direct Testimony at 7:14-19; Gordon Direct Testimony at 23:21-24:17.

<sup>36</sup> Danner Direct Testimony at 10:8-12; Gordon Direct Testimony at 23:21-24:17.

investment.<sup>37</sup> As ILEC witness Dr. Gordon summarizes, “[b]y better aligning residential basic local prices with cost, competitors will have increased incentives to target a broader mix of residential consumers, which is the intent of the Florida legislature.”<sup>38</sup>

That accurate prices induce market entry and foster competition is supported by more than just economic theory. Empirical studies show that Verizon’s plan – by setting residential rates at more economically efficient levels – will make the residential local exchange marketplace more attractive to potential entrants. In fact, Dr. Gordon cites three empirical studies that confirm this fact.<sup>39</sup>

Adopting prices that more accurately reflect costs will also benefit residential consumers. According to Dr. Gordon, “telephone consumers are better off as a result of moving prices more in line with costs, and will likely increase their purchases of those services whose price has come down.”<sup>40</sup> It is relatively straightforward to demonstrate the increased consumer welfare created by these increased purchases. As Dr. Danner explains:

This point can be demonstrated by a consumer surplus analysis, or by the common-sense observation that a customer who freely elects to make more calls would do so only if he or she is made better off as a result.<sup>41</sup>

More accurate prices will also place increased pressure on all market entrants to operate efficiently. This in turn will place downward pressure on rates and promote the efficient use

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<sup>37</sup> Danner Direct Testimony at 13:2-9.

<sup>38</sup> Gordon Direct Testimony at 4:3-5.

<sup>39</sup> Id. at 27:12-28:17.

<sup>40</sup> Id. at 4:17-19.

<sup>41</sup> Danner Direct Testimony at 12:1-4 (footnotes omitted).



of telecommunications resources in Florida's economy.<sup>42</sup> Finally, more accurate prices will encourage innovation, affording consumers increased freedom of choice in today's dynamic telecommunications marketplace.<sup>43</sup>

Verizon's rate rebalancing plan will be of particular benefit to Florida's low income consumers. This is because Lifeline customers will be able to enjoy the benefits of rate rebalancing, including reduced prices for intrastate long distance services, without experiencing an increase in their basic local service rates.<sup>44</sup>

In sum, Verizon's rate rebalancing plan is in the public interest because it will encourage investment in the telecommunications infrastructure by new and existing competitors and it will provide significant benefits to subscribers.

**1. Even Though Verizon's Rate Rebalancing Plan is Revenue Neutral, It Provides An Effective Incentive For Entry**

Under Verizon's rate rebalancing plan, basic local rates will increase but Verizon's total rebalanced revenues will not. Nevertheless, Verizon's rate rebalancing plan provides an effective incentive for competitors to enter the local exchange market.

Competitors are free to compete in the basic local market, the long distance market, markets for specialized offerings, or all of the above. Certain competitors may choose to compete only in the basic local exchange market, or, even if they intend to compete in all markets, may view the price of local basic service as the most important price signal. The price of local service has historically been substantially more stable than the price of, for

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<sup>42</sup> Danner Direct Testimony at 12:10-12.

<sup>43</sup> Danner Direct Testimony at 12:6-12; Gordon Direct Testimony at 5:25-6:2.

<sup>44</sup> Danner Direct Testimony at 10:22-11:4; Gordon Direct Testimony at 13:7-15.

example, long distance. These competitors will react to an increase in the stand-alone price of basic local residential service.<sup>45</sup>

Moreover, Verizon's rate rebalancing plan will stimulate market entry because it will increase the number of compensatory customers in the market. Under Verizon's existing rate structure, high volume long distance users currently subsidize low volume long distance users. This means that total bills of the high volume users are artificially high and the total bills of the low volume users are artificially low.<sup>46</sup> Therefore, the number of compensatory customers is smaller than it would be under an efficient rate structure.

As Dr. Danner explains, this has implications for the entry decisions made by competitive providers. All competitors (facilities-based providers in particular) must base entry decisions on the number of potential customers they may attract, and those customers' likely spending on their services. Because Verizon's existing rate structure artificially decreases the number of potentially compensatory customers, it reduces the number of competitive targets. Reducing the pool of competitive targets increases the risk of investing in the market, and thus makes entry less attractive to competitors.<sup>47</sup>

Verizon's rate rebalancing plan will increase the number of compensatory customers, and thus the number of competitive targets for new entrants. This will reduce the risk of investing in the local exchange market, and encourage investment in Florida's telecommunications infrastructure.<sup>48</sup>

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<sup>45</sup> Danner Direct Testimony at 8:12-9:2.

<sup>46</sup> Id. at 9:4-9:12.

<sup>47</sup> Id. at 9:14-10:3.

<sup>48</sup> Id.

## 2. Intra- and Intermodal Carriers Are Poised To Enter The Local Exchange Market As Soon As Prices Are Reformed

Verizon's report on local competition in its Florida territory, which is attached as Exhibit ETL-1 to the testimony of Verizon witness Leo, demonstrates that facilities-based competition in Verizon's Florida footprint is far more robust for business customers than for residential customers. It shows, for example, that competitors in Verizon's region serve approximately 10 business lines for every one residential line, and facilities-based carriers serve more than one-hundred business lines for every residential line.<sup>49</sup>

The report also demonstrates that the paucity of residential competition in Verizon's Florida service territory cannot be attributed to an absence of viable potential entrants. To the contrary, it demonstrates that facilities-based intra- and intermodal carriers have the necessary facilities in place to compete vigorously for residential customers as soon as the Commission reduces or eliminates the current support system and rebalances retail rates.<sup>50</sup>

Competitors have deployed extensive facilities (including numerous circuit and packet switches, and numerous competitive local fiber networks) in geographic locations that include virtually all of Verizon's residential customers in the state.<sup>51</sup>

Moreover, cable operators are well situated to expand their competitive offerings to include business and residential telephone services delivered over a fiber optic

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<sup>49</sup> Direct Testimony of Evan T. Leo On Behalf of Verizon Florida Inc. (Leo Direct Testimony), filed concurrently herewith, Exhibit ETL-1 at 2. See also Gordon Direct Testimony at 10:16-11:11 (In Florida, the percentage of lines provided to residential and small business customers by CLECs is low when compared to other states).

<sup>50</sup> See generally Leo Direct Testimony, Exhibit ELT-1.

<sup>51</sup> Leo Direct Testimony, Exhibit ELT-1 at 6-7; Danner Direct Testimony at 14:15-18.

infrastructure.<sup>52</sup> Indeed, Bright House Networks, the principal cable television provider in Verizon's service area, has completed much of the work necessary and has the experience to begin offering cable telephony services in response to pricing reform.<sup>53</sup>

In addition, Verizon has shown that its plan will promote increased competition by wireless providers.<sup>54</sup> As Dr. Danner testifies:

Wireless services already compete extensively with wireline services, and pricing reform will increase the attractiveness of wireless as a substitute for wireline services. Increased competition from wireless providers will benefit a large number of Floridians because: (1) wireless phones are close substitutes for wireline phones; (2) wireless phones are prevalent in this state; and (3) a growing number of customers are abandoning their wireline phone service for a wireless phone, and an even larger share of traffic minutes are migrating to wireless networks.<sup>55</sup>

Verizon's plan will also promote increased competition among other providers making use of alternative technologies.<sup>56</sup> Vonage, which employs Internet Protocol (IP) technology, to offer a full range of telecommunications services, including basic local service, is a good example. It offers a flat-rate local service plan for \$25.99 per month that includes a large local calling area, 500 minutes of long distance, vertical services, and deeply discounted long distance and international calling rates.<sup>57</sup> Pricing reform will provide a strong incentive for Vonage to focus on the Florida market because Vonage's competitive rate will become much closer to Verizon's after rates are reformed.

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<sup>52</sup> Danner Direct Testimony at 16:19-18:4; Leo Direct Testimony, Exhibit ELT-1 at 9-14.

<sup>53</sup> Danner Direct Testimony at 17:1-13.

<sup>54</sup> Danner Direct Testimony at 20:19-21:3; Leo Direct Testimony, Exhibit ELT-1 at 14-17.

<sup>55</sup> Danner Direct Testimony at 21:22-22:4 (footnotes omitted).

<sup>56</sup> See generally Leo Direct Testimony, Exhibit ELT-1; Danner Direct Testimony at 20:16-21:4.

<sup>57</sup> Danner Direct Testimony at 20:16-21:4.

Significantly, the mere potential for pricing reform is encouraging competitors to enter and compete in Florida. Less than a month after the Act was signed into law, Knology, a provider of broadband and voice telephony services, announced that it had agreed to purchase Verizon's broadband cable assets in Pinellas County. In its press release regarding the transaction, Knology made clear the potential for future pricing reform influenced its decision to expand:

The Tele-Competition Act recently enacted in Florida positively influenced [Knology's] decision to expand operations in the state. This Act, as written by the Florida Legislature and supported by Governor Bush, laid the foundation for companies like Knology to enter the Florida market, and offer competitive services and products to consumers.<sup>58</sup>

Knology's senior director of marketing made a similar comment, stating "the deal was facilitated by the state law approved by the Legislature this year that raised local phone rates as a way to stimulate telephone competition."<sup>59</sup>

Given that (1) there is a large disparity in the level of competition for business and residential customers in Verizon's service area, (2) there are existing facilities that are being underutilized due to existing irrational prices, and (3) both intra- and intermodal competitors are well positioned to make inroads into the basic local residential exchange market, it is clear that Verizon's rate rebalancing plan will enhance competitive opportunities to serve residential customers.

**C. Verizon's Rate Rebalancing Plan Requires Intrastate Switched Network Access Rate Reductions To Parity Over Two Years**

Verizon's rate rebalancing plan requires the Company to reduce its intrastate access composite rate from \$.0485047 to \$.0112453 over two-years.<sup>60</sup> As required by the statute,

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<sup>58</sup> Danner Direct Testimony at 14:4-10; Gordon Direct Testimony at 27:2-7.

this reduction will bring the Company's intrastate access composite rate to parity with its interstate access composite rate in the timeframe afforded by the Section 364.164(1)(c). Among other rate elements, Verizon's interstate composite access rate of \$.0112453 includes the presubscribed interexchange carrier charge (PICC).<sup>61</sup> The PICC is appropriately included in the interstate access rate for two reasons. First, there are traffic-sensitive and non-traffic-sensitive costs associated with provisioning interstate access, and the PICC captures the non-traffic sensitive costs.<sup>62</sup> Second, including the PICC in Verizon's interstate access rate is consistent with the plain language of Section 364.164(6). That section defines the term "intrastate switched network access rate" to include common line charges, but does not define the term "interstate switched network access rate." Because the statute includes common line charges in Verizon's intrastate access rate, the analogous PICC federal common line charge should be included in Verizon's calculation of the interstate rate.<sup>63</sup>

**D. Verizon's Rate Rebalancing Plan Is Revenue Neutral**

Verizon's proposal moves revenues on a dollar-for-dollar basis from switched access charges to basic local residential and business rates.<sup>64</sup> Verizon's proposal thus complies with the statute's requirements for revenue-neutrality.

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<sup>59</sup> Danner Direct Testimony at 14:12-15; Gordon Direct Testimony at 26:16-27:7.

<sup>60</sup> Fulp Direct Testimony at 7:18-19.

<sup>61</sup> Id. at 10:20-11:4.

<sup>62</sup> Id. at 11:11-14.

<sup>63</sup> Id. at 11:16-12:4.

<sup>64</sup> Id. at 25:23-26:3.

#### IV. RETAIL RATE REBALANCING IN OTHER STATES HAS BEEN GOOD FOR COMPETITION AND CONSUMERS

Other states that have implemented rate rebalancing include California, Massachusetts, and Maine.<sup>65</sup> Pricing reform in these states has improved the competitive landscape, benefited consumers and proceeded without notable difficulties for consumers.<sup>66</sup>

In California, the Public Utilities Commission pricing reform order in 1994<sup>67</sup> raised basic rates for Pacific Bell and GTE customers in exchange for reductions in access charges and toll prices. The basic rate increase for GTE was from \$9.75 per month to \$17.25 per month. As is in the instant case, prices for in-state toll and access charges were also cut sharply to promote competition and to encourage economic efficiency. Following the implementation of these rate changes in California, there was no impact on universal service, and no widespread expressions of concern from customers.<sup>68</sup>

In Massachusetts, residential fixed monthly charges were increased significantly, with offsetting decreases in business, toll, and carrier access prices. Over a four year period (1990 to 1994), the price for basic residential measured-rate dial-tone service increased by \$6.91 (net of the subscriber line charge). Over the same time period, the price of residential flat-rate service also experienced comparable increases. Flat rate residential prices had ranged from \$9.95 in rural areas to \$12.38 in urban areas, and these prices were increased to \$16.85 statewide. According to the Massachusetts Commission, these

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<sup>65</sup> See generally, Danner Direct Testimony at 25:22-27:5; Gordon Direct Testimony at 38:20-43:5.

<sup>66</sup> Id.

<sup>67</sup> CPUC decision 94-09-065, September 15, 1994.

<sup>68</sup> Danner Direct Testimony at 26:14-17.

increases had virtually no impact on residential telephone subscriber penetration.<sup>69</sup> Moreover, according to ILEC witness Gordon, the price rebalancing helped to lessen opportunities for uneconomic bypass and thus promoted the development of an efficient competitive process.<sup>70</sup>

More recently, the Massachusetts Commission authorized a one-time increase of \$2.44 to its residential dial-tone line charge. In commenting on the decision, the Commission found that “with the \$2.44 increase in the dial-tone line charge, competitive local exchange carriers (CLECs) can profitably enter and serve the residential telephone market in Massachusetts.”<sup>71</sup> The Commission also found that the \$2.44 increase will not harm the state’s universal service goals, based on its experience with rate rebalancing in the early 1990s and experiences with comparable increases in several other states and at the federal level.<sup>72</sup>

Maine, similar to Massachusetts and California, has engaged in rate rebalancing, with no noticeable impact on telephone subscribership levels. In 1997, the Maine Legislature directed the Maine Commission to establish intrastate access rates that are less than or equal to interstate access rates established by the FCC by May 30, 1999.<sup>73</sup> This required Bell Atlantic to lower its interstate access rates from \$.26 to \$.07 per minute.

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<sup>69</sup> See Re Verizon New England, Inc. dba Verizon Massachusetts D.T.E. 01-31-Phase II, Public Utilities Reports, 223 PUR4th at 397.

<sup>70</sup> Gordon Direct Testimony at 39:2-41:20.

<sup>71</sup> See Re Verizon New England, Inc. dba Verizon Massachusetts D.T.E. 01-31-Phase II, Public Utilities Reports, 223 PUR4th at 361.

<sup>72</sup> Gordon Direct Testimony at 41:12-20.

<sup>73</sup> M.R.S.A. 35-A, §7101-B.



Ultimately, the Commission issued an Order that approved a stipulation between Bell Atlantic and a group of interveners, including the Commission's Advocacy Staff and the Public Advocate. That stipulation allowed Bell Atlantic to increase its basic local exchange rates by a total of \$3.50, with steps of \$1.50 in 1998 and \$2.00 in 1999. This was followed by another increase of \$1.78 in 2001. Notwithstanding these rate increases, Maine still has the highest telephone penetration rate in the country.<sup>74</sup> In addition, consumers have been able to enjoy reduced toll rates.<sup>75</sup>

There are other examples showing that pricing reform does not undermine universal service. As set forth in Dr. Danner's testimony, the Consumer Federation of America and the U.S. Public Interest Research Group predicted that 6 million subscribers would give up their phone service during the mid-1980s due to Federal telephone pricing reform (that is similar to the reform Verizon proposes for Florida). This claim proved to be erroneous: subscribers actually increased by 4.1 million during this period, in part due to the reform's beneficial impacts on universal service.<sup>76</sup>

Accordingly, based on the rate rebalancing experiences in other jurisdictions, Verizon's rate rebalancing plan will benefit consumers and promote competition.

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<sup>74</sup> MPUC Annual Report 2002 at 43.

<sup>75</sup> Gordon Direct Testimony at 41:23-42:19.

<sup>76</sup> Danner Direct Testimony at 26:19-27:5.

**V. CONCLUSION**

In light of the foregoing, the Commission should grant Verizon's petition to reform its intrastate network access and basic local telecommunications rates.

Respectfully submitted on August 27, 2003

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