

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of

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

DOCKET NO. 030867-TL

PETITION BY SPRINT-FLORIDA,
INCORPORATED TO REDUCE INTRASTATE
SWITCHED NETWORK ACCESS RATES TO
INTERSTATE PARITY IN REVENUE-NEUTRAL
MANNER PURSUANT TO SECTION
364.164(1), FLORIDA STATUTES.

DOCKET NO. 030868-TL

PETITION FOR IMPLEMENTATION OF
SECTION 364.164, FLORIDA STATUTES,
BY REBALANCING RATES IN A
REVENUE-NEUTRAL MANNER THROUGH
DECREASES IN INTRASTATE SWITCHED
ACCESS CHARGES WITH OFFSETTING
RATE ADJUSTMENTS FOR BASIC SERVICES,
BY BELLSOUTH TELECOMMUNICATIONS, INC.

DOCKET NO. 030869-TL

FLOW-THROUGH OF LEC SWITCHED
ACCESS REDUCTIONS BY IXC's,
PURSUANT TO SECTION
364.163(2), FLORIDA STATUTES.

DOCKET NO. 030961-TI

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VOLUME 2

PAGES 49 THROUGH 219

PROCEEDINGS:

HEARING



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FPSC-COMMISSION CLERK

1 BEFORE: CHAIRMAN LILA A. JABER
2 COMMISSIONER J. TERRY DEASON
3 COMMISSIONER BRAULIO L. BAEZ
4 COMMISSIONER RUDOLPH "RUDY" BRADLEY
5 COMMISSIONER CHARLES M. DAVIDSON

6 DATE: Wednesday, December 10, 2003

7 TIME: Commenced at 11:29 a.m.

8 PLACE: Betty Easley Conference Center
9 Room 148
4075 Esplanade Way
Tallahassee, Florida

10 REPORTED BY: LINDA BOLES, RPR
11 Official FPSC Reporter
12 (850) 413-6734

13 APPEARANCES: (As heretofore noted.)
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I N D E X

WITNESSES

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NAME:

PAGE NO.

KENNETH GORDON

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CERTIFICATE OF REPORTER

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 25 for a detailed description of Exhibits 5 through 44

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24 REPORTER'S NOTE: Please see Pages 54A through 54E
25 for a detailed description of Exhibits 5 through 44

DOCKET NO. <u>030867-TL, 030868-TL, 030869-TL, 030691-TL</u>	CASE NAME: <u>Verizon, Sprint, BellSouth Restructuring and IXC Flowthrough</u>
DATE: <u>December 10-12, 2003</u>	PLACE OF HEARING: <u>Tallahassee, Florida</u>

COMMISSIONERS PARTICIPATING: Jaber, Baez, Bradley, Davidson, Deason

PRIOR	#	PARTY/ WITNESS	Proffered By	TITLE	IN REC'D
Stip-1		Verizon	Staff	<ol style="list-style-type: none"> 1. Verizon's responses to Staff's 1st Interrogatories, 1-41 2. Verizon's supplemental responses to Staff's 1st Interrogatories, 25 3. Verizon's responses to Staff's 1st Production of Documents, 1-25 4. Verizon's 1st supplemental responses to Staff's 1st Production of Documents, 3, 5-9 5. Verizon's 2nd supplemental response to Staff's 1st Production of Documents, 2,4 6. Verizon's responses to Staff's 2nd Interrogatories 42-73 7. Verizon's responses to Staff's 2nd Production of Documents, 26-32 8. Verizon's responses to Staff's 3rd Interrogatories, 74-85 9. Verizon's responses to Staff's 3rd Production of Documents, 33 	
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Stip-3		SPRINT	Staff	<ol style="list-style-type: none"> 1. Sprint's responses to Staff's 1st Interrogatories, 1-34 2. Sprint's responses to Staff's 1st Production of Documents, 1-15 3. Sprint's responses to Staff's 2nd Interrogatories, 35-56 4. Sprint's responses to Staff's 2nd Production of Documents, 16-24 5. Sprint's responses to Staff's 3rd Interrogatories, 57-69 6. Sprint's responses to Staff's 3rd Production of Documents, 25-27 	

PRIOR	#	PARTY/ WITNESS	Proffered By	TITLE	IN REC'D
Stip-4		BELLSOUTH	Staff	<ol style="list-style-type: none"> 1. BellSouth's corrected responses to Staff's 3rd set of Interrogatories No. 85 2. BellSouth's responses to Staff's 4th set of Interrogatories Nos. 81-90 3. BellSouth's responses to OPC's 1st set of Interrogatories Nos. 9, 10, 17-22 (inclusive) 4. BellSouth's responses to OPC's 1st Request for Production of Documents Nos. 2, 6, 7, 8-10, 24 5. BellSouth's supplemental responses to OPC's 1st set of Interrogatories, No. 5, and Request for Production of Documents, No. 13 6. BellSouth's responses to OPC's 2nd set of Interrogatories Nos. 30, 32, 33, 34, 37, 38 7. BellSouth's supplemental responses to OPC's 2nd set of Interrogatories Nos. 34 and 38 8. BellSouth's responses to OPC's 4th set of Interrogatories Nos. 51, 52, 53 (including attachment), 55, 57, 58 (including attachments for a, b, & c), 60, at page 57; No. 57, pages 2 and 3 added at page 612 of exhibit 9. BellSouth's responses to OPC's 3rd Request for Production of Documents Nos. 31, 32, 35 (attachments 1-8), 36 10. BellSouth's responses to OPC's 2nd set of Interrogatories Nos. 34 and 38 	
Stip-5		SPRINT	Staff	<ol style="list-style-type: none"> 1. Sprint's responses to Staff's 4th set of Interrogatories Nos. 77-87 2. Sprint's responses to Staff's 5th set of Interrogatories Nos. 88-95 3. Sprint's responses to OPC's 1st Request for Production of Documents, No. 7 4. Sprint's responses to OPC's 1st set of Interrogatories Nos. 13, 14, 15, 24, 25, 26 5. Affidavits to Staff's First Set of Interrogatories 	
Stip-6		OPC	Staff	<ol style="list-style-type: none"> 1. OPC's responses to Staff's 1st set of Interrogatories (excluding No. 1) and 1st Request for Production of Documents 	
Stip-7		VERIZON	Staff	<ol style="list-style-type: none"> 1. Verizon's responses to Staff's 4th set of Interrogatories Nos. 86-98 2. Verizon's responses to Staff's 5th set of Interrogatories Nos. 99-117 3. Verizon's supplemental responses to OPC's 1st set of Interrogatories No. 3 4. Verizon's responses to OPC's 2nd set of Interrogatories No.31 	
Stip-8		BELLSOUTH	Staff	<ol style="list-style-type: none"> 1. BellSouth's responses to Staff's 5th Set of Interrogatories 	
Stip-8A		STAFF	Staff	<ol style="list-style-type: none"> 1. Staff's responses to OPC's 2nd set of Production of Documents, No. 6 2. Staff's responses to OPC's 2nd Set of Interrogatories No. 10(b) 	

PRIOR	#	PARTY/ WITNESS	Proffered By	TITLE	IN REC'D
Stip-9		BELLSOUTH	Staff	1. BellSouth's responses to Staff's 6 th set of Interrogatories Nos. 103-104	
Stip-10		STAFF/ OLLILA	Staff	1. FPSC's 2003 Annual Report on Competition Telecom Markets in Florida	
Stip-11		SPRINT	Staff	1. Sprint's responses to Staff's 6 th set of Interrogatories Nos. 96-97 2. Sprint's supplemental responses to OPC's 1 st set of Interrogatories No. 22 3. Sprint's responses to OPC's 2 nd set of Interrogatories No. 34, 37 (cover sheet omitted 37)	
Stip-12		SPRINT	Staff	1. Sprint's supplemental responses to Staff's 1 st set of Interrogatories Nos. 33-34 (cover sheet stated 34-35, in error) 2. Sprint's supplemental responses to Staff's 1 st request for Production of Documents No. 15 3. Sprint's supplemental responses to Staff's 3 rd set of Interrogatories Nos. 69-70 and 73 4. Sprint's responses to Staff's 3 rd request for Production of Documents Nos. 25-27	
Stip-13		KNOLOGY	Staff	1. Knology's responses to Staff's 1 st set of Interrogatories, Nos. 1-9 2. Knology's responses to Staff's 2 nd set of Interrogatories, Nos. 10 through 17	
Stip-14		AT&T	Staff	1. AT&T's responses to Citizen's 2 nd Request for Production of Documents Nos. 2, 3, 4 2. AT&T's responses to Staff's 1 st set of Interrogatories, Nos. 1-21 (22 through 78 omitted) 3. AT&T responses to Staff's 1 st set of Interrogatories, Nos. 79-87 (22 through 78 omitted)	
Stip-15		Verizon	Staff	1. Verizon's responses to Staff's 6 th set of Interrogatories	
Stip-16		MCI	Staff	1. MCI's responses to Staff's 1 st set of Interrogatories, Nos. 1-62 2. MCI's responses to Staff's 2 nd set of Interrogatories, Nos. 63-76	
DEPO-1		BELLSOUTH/ SPRINT/ VERIZON	Staff	1. Deposition of BellSouth/Sprint/Verizon witness Dr. Kenneth Gordon	
DEPO-2		BELLSOUTH	Staff	1. Deposition of BellSouth witness John A. Ruscilli	
DEPO-3		BELLSOUTH	Staff	1. Deposition of BellSouth witness W. Bernard Shell 2. Late Filed Deposition Exhibits	
DEPO-4		BELLSOUTH	Staff	1. Deposition of BellSouth witness E. Stephen Bigelow	
DEPO-5		BELLSOUTH	Staff	1. Deposition of BellSouth witness Jerry Hendrix	
DEPO-6		BELLSOUTH	Staff	1. Deposition of BellSouth witness Dr. Aniruddha Banerjee	

PRIOR	#	PARTY/ WITNESS	Proffered By	TITLE	IN REC'D
DEPO-7		VERIZON	Staff	1. Deposition of Verizon witness Orville D. Fulp 2. Late Filed Deposition Exhibits	
DEPO-8		VERIZON	Staff	1. Deposition of Verizon witness Carl R. Danner	
DEPO-9		SPRINT	Staff	1. Deposition of Sprint witness Kent W. Dickerson	
DEPO-10		SPRINT	Staff	1. Deposition of Sprint witness Dr. Brian K. Staihr	
DEPO-11		SPRINT	Staff	1. Deposition of Sprint witness John M. Felz (See DEPO-17 for Late-file exhibits)	
DEPO-12		KNOLOGY	Staff	1. Deposition of Knology witness Felix L. Boccucci, Jr.	
DEPO-13		AT&T	Staff	1. Deposition of AT&T witness Wayne Fonteix, excluding page 29, line 18, through page 35, line 18; page 9, line 21 through page 10, line 10; page 17, line 23 through page 24 line 8.	
DEPO-14		OPC	Staff	1. Deposition of OPC witness Dr. David J. Gabel	
DEPO-15		OPC	Staff	1. Deposition of OPC witness Bion C. Ostrander	
DEPO-16		AARP	Staff	1. Deposition of AARP witness Dr. Mark N. Cooper	
DEPO-17		SPRINT	Staff	1. Late-filed Deposition Exhibits of Sprint witness John M. Felz	
CONF STIP-1		VERIZON	Staff	1. CONFIDENTIAL DN 08885-03 Verizon's responses to OPC's 1st Request for Production of Documents, Nos. 2, 3, 11, 12, and 31.	
CONF STIP-2		VERIZON	Staff	1. CONFIDENTIAL DN 09366-03 Verizon's responses to OPC's 3rd Request for Production of Documents No. 51.	
CONF STIP-3		VERIZON	Staff	1. CONFIDENTIAL DN 09449-03 Verizon's responses to staff's 1 st set of Interrogatories, Nos. 12, 14, 15, 16, 41 and staff's 1 st Request for Production of Documents, Nos. 24, 25	
CONF STIP-4		VERIZON	Staff	1. CONFIDENTIAL DN 10128-03 Verizon supplemental responses to Staff 1 st Request for Production of Documents, Nos. 3 and 9 (both on CD) and paper copy of 9 printed from CD.	
CONF STIP-5		VERIZON	Staff	1. CONFIDENTIAL DN 10632-03 Verizon's responses to OPC's 1st Request for Production of Documents, Nos. 16, 18, 19.	
CONF STIP-6		VERIZON	Staff	1. CONFIDENTIAL DN 10697-03 Verizon's second supplemental responses to OPC's 1st Request for Production of Documents No. 6.	
CONF STIP-7		VERIZON	Staff	1. CONFIDENTIAL DN 11728-03 Verizon supplemental responses to Staff 1 st Interrogatories, No. 25	

PRIOR	#	PARTY/ WITNESS	Proffered By	TITLE	IN REC'D
CONF STIP-8		VERIZON	Staff	1. CONFIDENTIAL DN 11928-03 Verizon responses to Staff 3rd set of Interrogatories, Nos. 77 and 85	
CONF STIP-9		VERIZON	Staff	1. CONFIDENTIAL 11932-03 Verizon's supplemental responses to OPC's 2nd Request for Production of Documents No. 37 and 40 on diskette and supplemental responses to OPC's 2 nd set of Interrogatories Nos. 29 and 33.	
CONF STIP-10				DELETED	
CONF STIP-11				DELETED	
CONF STIP-12		BELLSOUTH	Staff	1. CONFIDENTIAL DN 11783-03 BellSouth's responses to Staff 3 rd set of Interrogatories, Nos. 56, 57 (57 is attachment only, not interrogatory)	
CONF STIP-13		BELLSOUTH	Staff	1. CONFIDENTIAL DN 12053-03 BellSouth's responses to staff's 4th set of Interrogatories, No. 81 and attachments to Interrogatories Nos. 89, 90	
CONF STIP-14		SPRINT	Staff	1. CONFIDENTIAL DN 09829-03 Sprint's responses to OPC's 1 st Request for Production of Documents, No. 5	
CONF STIP-15		SPRINT	Staff	1. CONFIDENTIAL (DN 10142-03) Sprint responses to Staff 2 nd Request for Production of Documents No. 16 (on CD) and 19, page 1 through 3 of 3	
CONF STIP-16		SPRINT	Staff	1. CONFIDENTIAL (DN 10288-03) Sprint responses to Staff 1 st set of Interrogatories No. 21 (paper) and 1st Request for Production of Documents No. 2, (CD and highlighted portion of paper copies, pgs. 1-33 of 33) 3 (on CD), and 15 (on CD).	
CONF STIP-17		SPRINT	Staff	1. CONFIDENTIAL DN 11531-03 Sprint's responses to OPC's 3 rd set of Interrogatories Nos. 50a and 50b. CLEC market share data.	
CONF STIP-18		SPRINT	Staff	1. CONFIDENTIAL DN 11533-03 Sprint's supplemental response to OPC's 1st Request for Production of Documents, No. 6	
CONF STIP-19		SPRINT	Staff	1. CONFIDENTIAL (DN 12155-03) Sprint supplemental responses to Staff 1 st set of Interrogatories Nos. 33 and 34 and 1st Request for Production of Documents No. 15	
CONF STIP-20		SPRINT	Staff	1. CONFIDENTIAL DN 11885-03 Sprint's response to OPC's 2 nd set of Interrogatories, No. 29	
CONF STIP-21		SPRINT	Staff	1. CONFIDENTIAL (DN 11794-03) Sprint responses to Staff 3rd set of Interrogatories, Nos. 59, 66, 67, with attachments	
CONF STIP-22		BELLSOUTH	Staff	1. CONFIDENTIAL (DN 12258-03) BellSouth late-filed deposition exhibit of Bernard Shell	
CONF STIP-23		SPRINT	Staff	1. CONFIDENTIAL DN 12491-03 Sprint-Florida's answer to Staff's 6 th set of Interrogatories Nos. 96-97	
CONF STIP-24		Knology	Staff	1. CONFIDENTIAL DN 12499 Knology responses to Staff's 2 nd set of Interrogatories 11-17	

P R O C E E D I N G S

(Transcript continues in sequence from Volume 1.)

COMMISSIONER DAVIDSON: Thank you, Madam Chairman.

I would like to start by thanking the parties for attaching the transcript of the prior order. That production will encourage me to speak more frequently in grammatically correct sentences.

I recall very well that hearing, and my decision was based upon the entire changes to the statute, but specifically Section 364.164(1). That section sets forth four factors that the Commission shall consider in determining whether to grant the petition. The operative language for me reads, "In reaching its decision, the Commission shall consider whether granting the petition will," and then the section enumerates the four factors. The language does not provide, "In reaching its decision, the Commission shall only consider these four factors." It mandates four factors, but in my view doesn't prevent us from looking at possibly other factors.

That said, with regard to the language in the order, I would agree with the statement that consideration of the impact on the toll market is not required for the Commission's determination of the petitions. I would suggest striking "full and complete" because we may determine we want to look at that very full and complete determination, but the Legislature didn't say we must look at that factor. And I think

1 footnote -- the last sentence of that footnote emphasizes that
2 point. Staff notes in the draft or in the order, "In reaching
3 this conclusion, we do not find that we are precluded from such
4 consideration, rather we conclude only that we are not required
5 to do so." I agree with that sentence. The statement, "The
6 relevant market for use in making the final determination on
7 the petitions is the local exchange market," I don't know that
8 that's a necessary sentence and I would propose just striking
9 that. But, but that was my intent. I think the testimony --
10 the transcript sets forth what we indicated might very well be
11 important for us to consider and what might be an important
12 aspect of the petitioners' burden of proof. I stand by those
13 prior statements.

14 If we can tweak the order, I think I'm fine with the
15 gist of what staff was trying to get at in terms of what we're
16 required to do by statute and what we've indicated that we may
17 also do beyond those minimum requirements.

18 CHAIRMAN JABER: Sounds good. Mr. Mann, then we come
19 back to the original question posed to you all. What would you
20 recommend be deleted from the order?

21 MR. MANN: I think Commissioner Davidson has shed
22 some good light on that little crisis for me at any rate. The
23 most important thing is that first sentence of that paragraph
24 beneath subsection (a): "As such, the relevant market for use
25 in making the final determination is the local exchange

1 market." But I would still suggest that from the paragraph
2 above subsection (a), which begins, "As plainly stated by the
3 Legislature through the citing of subsection (a)," I think that
4 that section itself, that whole section of language itself
5 misleads the parties in, in whether or not there has been
6 established a definition of residential benefits.

7 CHAIRMAN JABER: Okay. Commissioners, let me just
8 state for the record, because it's been pointed out that in the
9 order that's being discussed was a 4/1 vote, but what has not
10 been pointed out that was very critical to how I approached
11 this motion is that you may recall this order was primarily
12 designed to address a motion to dismiss that was filed by AARP
13 using the argument that the IXCs were indispensable parties,
14 and my dissent was limited to that.

15 And the other thing I found useful for me in
16 approaching this motion was not just reading this order and
17 this transcript, but you may recall at that agenda we had
18 back-to-back items with similar issues. Item 4A dealt with the
19 motion to dismiss as it relates to the indispensable party
20 argument. The next item, you may recall, is when we got into a
21 little bit more discussion regarding why we needed this
22 information, and recognizing that there was some discretion, we
23 wanted to leave on the table opportunities we wanted to take
24 advantage of throughout this hearing. And how we end up
25 applying it, I think we all took extra care in preserving the

1 opportunity to discuss that at the conclusion of the hearing.
2 I say all of that because if it's the Commissioners' pleasure
3 today to modify this order in some form or fashion as suggested
4 by Commissioner Davidson or by Public Counsel, I'm going to
5 support that, and I don't find that to be inconsistent with the
6 original vote on the motion to dismiss. Because I do believe
7 when you consider both items at that agenda, there was
8 consensus that this was information that we needed and we
9 wanted to preserve for the hearing.

10 So if you don't have any other questions, if someone
11 would like to make a motion, we'll entertain a motion.

12 Mr. Twomey, we're ready to have a motion.

13 MR. TWOMEY: May I ask for clarification after you
14 vote then, Madam Chair?

15 CHAIRMAN JABER: Yeah, after we vote.

16 Commissioners, is there a motion? Questions? I
17 should haven't precluded questions. Commissioner Baez.

18 COMMISSIONER BAEZ: Well, I guess I'm having a little
19 trouble following what the -- the question was put out, what
20 would you suggest in terms of changes, and I guess it's three
21 or four people that, that produced suggestions, including
22 Commissioner Davidson.

23 And I guess I'm looking at AARP's motion, Page 11,
24 where I guess all the relevant language is found on one page,
25 and there's some language there that's underlined, and I know

1 that that's most of the language in question. The language
2 that starts, "As plainly stated," I guess my -- I'll let you
3 know where I am on it. I'm having trouble seeing -- I'm having
4 trouble seeing this as anything more than a, than a statement
5 of what is plainly found in the statute. I don't -- I'm having
6 trouble having this language rise to the level of a finding.

7 I will say that the next paragraph down after
8 subsection (a) where the language starts, "As such the relevant
9 market," I think that does rise to the level of a finding. Now
10 whether, whether that is something that -- certainly that's
11 something that I would have contemplated, as I had stated back
12 in November when we were discussing this, that I would have
13 contemplated being a finding as a result of a complete hearing,
14 that that should be a determination. So that particular
15 language, I think, kind of gives me a little bit of heartburn.

16 And lastly, I'm, I'm a little -- I don't remember,
17 and if someone can, can point me to the transcripts, which I
18 think we've all received copies of, where the discussion of the
19 clarity or where the determination of how clear exactly the
20 statute was, because I do remember there was some conversation
21 as to what discretion we had and that we were not making any
22 determinations on what discretions were. So I'm not, I'm not
23 sure how the statement that 364.164 appears clear and need not
24 look further, the Commission need not look further to divine
25 the Legislature's intent, I mean, I don't remember that

1 discussion in particular. Perhaps it was implied by our vote,
2 but I just -- I'm not comfortable with that finding necessarily
3 as well.

4 CHAIRMAN JABER: It may have been as simple as it was
5 in the original staff recommendation and it's one of those cut
6 and paste things. I don't --

7 COMMISSIONER DAVIDSON: Maybe -- I share that
8 concern. I don't recall that. If anything, I recall a bit of
9 a concern that we actually look at clearly what the intent was,
10 and we discussed different views, so it may have just been
11 lifted.

12 COMMISSIONER BAEZ: There, there may, there may have
13 been some discussion briefly. I guess I'm not -- I'm having
14 trouble -- I know that the central topic of our discussion was,
15 among other things, what Commissioner Deason's question was as
16 to what -- whether we were making a determination that we did
17 or didn't have discretion under the statute, and certainly what
18 the definition of benefit of the residential consumer would be
19 interpreted as. And I think generally the order left that
20 open. Certainly I know I voted on that basis, that that
21 particular question was one that, that benefited -- that needed
22 to benefit from the full hearing before we actually got to
23 answer it.

24 In terms -- what the implications of that decision
25 are to the question of whether, whether the statute is clear or

1 not, I, I guess I don't know. But I don't remember any
2 direct --

3 CHAIRMAN JABER: And I wanted, and I think you all
4 agreed, and I wanted to preserve the opportunity to look at the
5 allocations of flow-throughs between residential and consumer.
6 And -- I mean, residential and commercial. And there was --
7 again, it's like you have to read those two items, the
8 transcript of both of those items in harmony. And in
9 hindsight, maybe the order should have been one order, but
10 hindsight is a wonderful thing.

11 COMMISSIONER BAEZ: No. I'm -- again, I point those,
12 I point those up -- maybe they mean different things to
13 different people. I, too, am comfortable with the gist of the
14 order. Perhaps what we need is clarification. And I think we
15 did have enough discussion, and I think, again, at the risk of
16 repeating myself, you know, there was a lot of discussion as to
17 what, what discretion would be there for the Commission at the
18 end. And anything -- it's my belief, and I'm not -- I'll wait
19 to hear what you all think, but at the end of the day it's my
20 belief that if that was the central, if that was at the center
21 of our decision somehow, then anything that speaks to the
22 plainness of the statute, anything that speaks to, you know,
23 forecloses what, what our ultimate discretion is to define or
24 decide what, what benefit of the rate, benefit of the
25 residential consumer means to us necessarily constrains us.

1 And I'm not interested in doing that for this purpose for the
2 very reason that we did go for hours and hours talking to
3 Mr. Hatch and his clients and Ms. McNulty and their clients
4 about what the importance of having, you know, the information
5 on the IXCs, without making that the exclusive criteria for a
6 determination, but how important having that information was
7 ultimately to our determination. So I can't see -- I guess I'm
8 seeing a conflict between the statements that the statutes
9 appear clear and what we have somehow decided to maintain our
10 discretion available for the end of the hearing.

11 CHAIRMAN JABER: Since, since -- hang on,
12 Commissioner Bradley. Since we're not entertaining a motion,
13 which I thought we were, let me go ahead and get Mr. Twomey's
14 comments so that we don't have to revisit those after we're all
15 done.

16 COMMISSIONER BAEZ: I'm sorry, Madam Chair. I didn't
17 mean to take you out of the --

18 CHAIRMAN JABER: You're fine. You're fine. It's
19 Mr. Twomey.

20 MR. TWOMEY: Yes, ma'am, just very briefly. I think
21 it may be instructive to remember that the basis of the AARP's
22 motion to dismiss was the theory that the presence of the IXCs,
23 the long distance companies was critical, and how they would
24 flow through the reductions in in-state tolls to residential
25 customers was, was critical. And AARP -- and what you all did,

1 I take it, was the Chair said, that's fine, because they're not
2 here, the Chair said she would, she would vote to dismiss on
3 that basis in part.

4 I took the rest of the Commissioners to say, we view
5 that as something that we want to look at, retain the right to
6 look at, but it doesn't rise to, the absence doesn't rise to
7 the level of granting a motion to dismiss. And I think
8 Commissioner Deason in particular and Commissioner Baez and
9 Commissioner Davidson as well were saying, you know, they've
10 repeatedly said it's the burden for the, it's the burden for
11 the local companies, because the IXCs weren't in at that point.
12 You hadn't gone to Issue 5. So Commissioner Deason, his
13 comment repeatedly was it's the burden of the local companies,
14 it's the burden of the local companies, but they should have a
15 chance to meet it in the hearing. And I think Commissioner
16 Baez had that concern as well as Commissioner Davidson. And I
17 think yours was inherent, Madam Chair, in that, and
18 Commissioner Bradley didn't speak to it.

19 But my concern is, is that all you needed to do then
20 was is say the motion to dismiss is denied because we think the
21 issue is, one, burden of proof on the companies to be
22 considered at hearing. The rest of this is gratuitous to your
23 discussion in my view, and I'm particularly concerned I'm glad
24 that Commissioner Baez picked up on this, at Page 11 of the
25 AARP's motion, any of the language that talks about how plain

1 the statute is is gratuitous to, to your decision on the motion
2 to dismiss. But particularly important, I think, is that you
3 understand that if you, if you -- previously today you've
4 allowed official recognition of the, of the floor debates in
5 the Florida House and the Florida Senate. And if, if you
6 retain this language that, that starts -- the language of
7 Section 364.164, Florida Statutes, appears clear, "Thus under
8 principles of statutory interpretation, the Commission need not
9 look further to divine the Legislature's intent," then you buy
10 into the local companies' and the IXCs' position that you can't
11 look at what financial benefits go to the residential
12 customers. And I'm afraid effectively if you leave that
13 language in, you may inadvertently be ruling on the Attorney
14 General's motion, which addresses questions of, of benefit to
15 consumers.

16 So I think in particular any language that says that
17 you've ruled on the plainness and the clarity of the statute
18 was something that you did not discuss. You decided the motion
19 to dismiss based on the burden of proof, and I think that's all
20 you need to say. And so I would again urge your caution on, on
21 retaining any language that would, would, would answer the
22 question -- the Attorney General's motion even before he has a
23 chance to argue it, and would urge you to just say that the
24 motion to dismiss is, is denied for AARP and strike the
25 language that I've suggested. Thank you.

1 CHAIRMAN JABER: Okay. Commissioner Deason,
2 Commissioner Bradley and then Commissioner Davidson.

3 COMMISSIONER DEASON: Madam Chairman, I was prepared
4 to make a motion, so I'll defer to other Commissioners if there
5 are more questions or concerns.

6 CHAIRMAN JABER: Commissioner Bradley, you had
7 questions.

8 COMMISSIONER BRADLEY: Well, I think Mr. Twomey
9 probably just answered my question. Well, I'll ask it anyhow.
10 In the four corners of the statute, I'm going to deal
11 with C and D, it says, "Require intrastate switched network
12 access rate reductions to parity over a period of not less than
13 two years or more than four years, be revenue neutral as
14 defined in subsection (7) within the revenue category defined
15 in subsection (2)." My question is, wouldn't that statutory
16 language encompass your, your language?

17 MR. TWOMEY: I'm not sure, Commissioner Bradley. I'm
18 not sure. The, the -- you know, again, our concern is, is that
19 while we, while we would have loved to have seen a motion to
20 dismiss granted, we understand that the majority of you didn't
21 want to do that and so we accept that. And, and our concern
22 with the order is that it, that it, as evidenced by your
23 discussions in the transcript of that agenda conference, go
24 well beyond what you discussed in deciding to deny the motion
25 to dismiss. So, again, we're concerned, we're concerned that

1 if you decide that it's, if you decide that the statute is so
2 clear that reliance on legislative history and other
3 indications of intent can't be relied upon, then granting our
4 official recognition gives us no advantage.

5 Did that address your, your question at all?

6 CHAIRMAN JABER: Commissioner Davidson, you had a
7 question, or are you ready for Commissioner Deason's motion?

8 COMMISSIONER DAVIDSON: Well, I have a motion as
9 well, so however you --

10 COMMISSIONER DEASON: I will defer to Commissioner
11 Davidson.

12 COMMISSIONER DAVIDSON: I think he'll beat me on
13 that.

14 CHAIRMAN JABER: Commissioner Davidson, motion.

15 COMMISSIONER DAVIDSON: And the motion is based upon
16 the language appearing at Pages 2 and 3 of AARP's motion.

17 CHAIRMAN JABER: Pages 2 and 3.

18 COMMISSIONER DAVIDSON: The order 1331 contains the
19 following language at Pages 11 and 12. That's the version I
20 used for a markup, and here are the changes.

21 The first sentence -- proposed changes. The first
22 sentence would remain the same.

23 The second sentence, "Contrary to AARP's assertions,
24 none of the four," insert the word "mandatory," "criteria set
25 forth for our consideration in addressing the petitions,"

1 strike "necessitates" and insert the word "mandates."

2 In the underlined section, go down to the third line
3 of the underlined section, "for our consideration does not
4 mandate that the Commission," strike the word "to," "consider
5 how the ILECs' proposals will affect." Parenthetical A remains
6 the same.

7 CHAIRMAN JABER: I'm sorry, Commissioner Davidson.
8 So you would strike -- and then you would strike, "as plainly
9 stated by the Legislature," that would be stricken?

10 COMMISSIONER DAVIDSON: Yes. Yes.

11 CHAIRMAN JABER: Okay.

12 COMMISSIONER DAVIDSON: Strike "as plainly stated by
13 the Legislature." I apologize. And then just go to the first
14 factor set forth in Section 364(1), "for our consideration does
15 not mandate that the Commission consider."

16 CHAIRMAN JABER: Okay.

17 COMMISSIONER DAVIDSON: To the next full text
18 paragraph, strike that first sentence, "as such the relevant
19 market."

20 Continuing over to the next page, strike the words
21 "full and complete."

22 Then I would move up into the text the footnote
23 sentence, which is not here, but the footnote sentence reads,
24 "In reaching this conclusion, we do not find that we are
25 precluded from such consideration, rather we conclude only that

1 we are not required to do so."

2 The last change would be strike the underlined
3 sentence beginning with the language of Section 364.164 all the
4 way down to the case cite.

5 And I think we can move the, the -- we never -- we,
6 "We acknowledge AARP's contention that the Legislature consider
7 the impacts on customer toll bills," we could move that up into
8 the prior paragraph.

9 The overall reasoning behind those changes is, as I
10 tried to articulate at our last conference on this proceeding,
11 the Legislature set forth four factors. They mandated we look
12 at four factors. The Legislature did not mandate that we
13 consider the impact on toll customers. We have determined that
14 we need that information, it's relevant to our consideration,
15 we need to look at the overall statutory scheme. So -- and I'm
16 fine with any, obviously fine with any changes to that
17 proposal, but I think it's important to reflect, in my view,
18 what was mandated versus what we have nonetheless indicated we
19 may look at.

20 CHAIRMAN JABER: Can I -- let me, for the record and
21 also for the benefit of the Commissioners, let me read you what
22 I think you said. And would you follow with me and correct
23 this as we go along?

24 What you had proposed that the order be corrected to
25 reflect is this: "In reaching this conclusion, we refer to the

1 language of Section 364.164, Florida Statutes. Contrary to
2 AARP's assertions, none of the four mandatory criteria set
3 forth for our consideration in addressing the petitions
4 mandates participation by the IXC's. The first factor set forth
5 in Section 364.164(1), Florida Statutes, does not mandate that
6 the Commission consider how the ILECs' proposals will affect
7 the toll market for the benefit of residential consumers.
8 Instead, the plain language states that the consideration
9 should be given to whether granting the petitions will, A,"
10 and, of course, A stays the same. "Thus, we find that for
11 purposes of Section 364.164, Florida Statutes, consideration of
12 the impact on the toll market and resulting impact on toll
13 customers is not required for the Commission's determination of
14 the petitions." You would insert the footnote here from the
15 order. And then you would move up to the prior paragraph, the
16 sentence that said, "We nevertheless acknowledge AARP's
17 contention." Recognize, of course, you've struck the sentence
18 that starts the language of Section 364.

19 COMMISSIONER DAVIDSON: Yes, Madam Chair, that's
20 correct.

21 CHAIRMAN JABER: Okay. Everything else stays the
22 same.

23 COMMISSIONER DAVIDSON: Yes.

24 CHAIRMAN JABER: Commissioner Bradley? Commissioner
25 Deason? I need -- that's the motion.

1 COMMISSIONER DAVIDSON: Yes.

2 CHAIRMAN JABER: That would be the motion. And is
3 there a second?

4 COMMISSIONER DEASON: Second.

5 CHAIRMAN JABER: And a second. All those in favor,
6 say aye.

7 (Unanimous affirmative vote.)

8 CHAIRMAN JABER: That resolves AARP's motion for
9 reconsideration of that order.

10 MR. SHREVE: Madam Chairman, could I get some
11 clarification? I thought I knew where Commissioner Davidson
12 was going with that, but I'm not sure that my reading comes out
13 the same.

14 Are you in that motion that just passed saying that
15 you are not mandated to consider the benefit of residential
16 consumers?

17 CHAIRMAN JABER: Mr. Shreve, let me interrupt you for
18 just a minute and, just to close up the record. There was a
19 motion, and I need to say for the record that it carried
20 unanimously.

21 Now you've got -- you're seeking -- you want
22 clarification on the motion; is that correct, Mr. Shreve?

23 MR. SHREVE: Please. Because to me the motion that
24 was just carried would not require you or not mandate you to
25 consider the benefit of residential consumers.

1 COMMISSIONER DEASON: That's not what was voted for.

2 CHAIRMAN JABER: No, that's not what was said.

3 COMMISSIONER DEASON: And maybe it needs to be
4 clarified.

5 CHAIRMAN JABER: Yeah. Let's let Commissioner
6 Davidson speak for himself. He -- a couple of times he made
7 clear what the intent was, so we'll let him speak for himself,
8 and then we'll all weigh in. Commissioner Davidson.

9 COMMISSIONER DAVIDSON: Thank you, Chairman.

10 I thought I explained this clearly a moment ago, but,
11 as the Chairman indicated when she read the revised order, the
12 order makes clear that the mandatory factors set forth in
13 364.164(1) do not mandate that we consider how the proposals
14 will affect the toll market for the benefit of residential
15 customers. That comes straight from the language of the
16 statute.

17 The order then goes on to make clear that despite
18 that we may not be mandated by those factors, we nonetheless
19 are not precluded from such consideration, should we choose to
20 do so.

21 CHAIRMAN JABER: Commissioner Davidson, that may be
22 the sentence we'd want to add in because that --

23 COMMISSIONER DAVIDSON: That was the footnote that
24 was added in.

25 The footnote reads, "In reaching this conclusion, we

1 do not find that we are precluded from such consideration.
2 Rather, we conclude only that we are not required to do so."

3 COMMISSIONER DEASON: May I make a clarification for,
4 for at least my vote?

5 Nothing in my vote would indicate that somehow we are
6 not mandated to or that we are mandated -- let me start over
7 again.

8 Nothing in my vote would indicate that somehow we can
9 ignore benefit of residential consumers. We have to consider
10 that.

11 What this states is that we are not mandated to
12 consider that within the confines of the toll market. We have
13 the discretion to consider benefits in terms of the toll
14 market; it's not mandated that we do such. But we are mandated
15 to consider benefits for residential consumers. How we define
16 those benefits and what they are and the magnitude of those,
17 that's within our discretion. That's what my vote was.

18 CHAIRMAN JABER: Yeah. Commissioner Deason, that is
19 the spirit of the motion. That was the spirit of my
20 understanding.

21 COMMISSIONER BRADLEY: Exactly.

22 CHAIRMAN JABER: That was the spirit of the vote.

23 And, Commissioners --

24 COMMISSIONER BRADLEY: That's my intent, also.

25 CHAIRMAN JABER: Thank you, Commissioner Bradley.

1 Okay. Commissioners, I think with that clarification
2 on the record, we have resolved this motion and we can go on to
3 the next one. And the next one would be the Attorney General's
4 motion for summary final order.

5 MR. SHREVE: Thank you, Madam Chairman, and I will be
6 relatively brief. I think most of the discussion has already
7 gone forward.

8 CHAIRMAN JABER: Mr. Shreve, it actually may not be
9 working. Let's have you talk into it. Let's make sure it's
10 working. Talk right into it.

11 MR. SHREVE: How is that?

12 CHAIRMAN JABER: Better.

13 MR. SHREVE: Thank you.

14 What I would like to go to is the statute, and I
15 think you've just made that decision that the Commission must,
16 is mandated to consider the benefit of residential consumers,
17 and we think that's what the statute says and the intent of the
18 statute is.

19 Earlier, in your earlier discussion in the AARP's
20 motion, at that point there had been, there had not been the
21 testimony filed showing what the breakdown was as far as the
22 benefits that would supposedly flow to the residential
23 consumers. Now there is. And by the very testimony that has
24 been filed, it shows that there is no overall benefit to the
25 residential consumers. We think that's necessary and mandated

1 and the essence of the law and exactly what was intended by the
2 Legislature.

3 I think the Commissioners in their discussions have
4 hit on this and have hit on it accurately. We feel that there
5 is an undisputed material fact that no benefit, or that there
6 is no overall benefit to the residential customers in the
7 testimony they've filed at this time, and all the testimony and
8 evidence is in. If you take it as it stands right now by the
9 companies, they've made our case to show that there is no
10 overall benefit to the residential companies -- to residential
11 customers. Anything new coming in during the hearings would
12 really be prohibited and would keep the customers or the
13 opposition to the petitions from having due process.

14 The -- essentially that's it. Mr. Beck has prepared,
15 I think, some very good documents to pass out, which are
16 precluded from discussion at this time because they're
17 confidential. We know what the increases in the rates are, we
18 now know what has been proposed by the companies and what those
19 decreases are, and we just do not feel that the company has
20 carried the burden. On the other hand, we think they've
21 actually shown that we have -- are entitled to a motion for
22 summary order at this time based on the evidence that they have
23 filed.

24 We'd like to, if possible, reserve time for rebuttal,
25 and turn it over to Mr. Beck at this point.

1 CHAIRMAN JABER: Okay. Mr. Beck.

2 MR. BECK: Thank you, Madam Chairman. Commissioners,
3 we now have the evidence from the interexchange carriers and we
4 have the evidence from the local companies, and the evidence is
5 clear, it's unequivocal and it's susceptible of only one
6 interpretation, and that is residential customers will not
7 benefit if you grant these petitions. Instead, they'll be
8 harmed.

9 What I've handed you is excerpts from the testimony
10 presented by the companies, and there's, it's testimony -- it's
11 evidence that the companies' claim are confidential. And in
12 the package I've given you there's excerpts from the evidence
13 presented by four separate companies: AT&T, MCI, Sprint Long
14 Distance and the Verizon local company. And so you have four
15 separate claims from four separate companies, but we needed to
16 present this to you so you can see what the evidence overall
17 has been presented on the benefits to the customers.

18 This is the evidence in the case, Commissioners. The
19 incumbent local exchange companies would impose the vast
20 majority of the local increase on the residential customers:
21 For Verizon, 93 percent of the increase goes on residential
22 customers; for BellSouth, it's 87 percent; for Sprint, it's
23 86 percent. This is translated into local increases that, that
24 are up to a \$1.58 for the first installment by Verizon, \$1.25
25 for BellSouth and \$2.95 for Sprint in the first of the three

1 increases.

2 What I'd like to do is ask you to compare what
3 customers may get back according to the testimony and the
4 evidence that we have from the companies, the testimony of
5 AT&T, MCI and Sprint, as well as the evidence by Verizon that
6 we've handed you.

7 The first piece of evidence is an excerpt from the
8 testimony of AT&T witness Richard Guepe, and I've handed you
9 Page 9 of his testimony that AT&T claims is confidential. What
10 you can see at Page, or Line 5 from this excerpt from AT&T is
11 the total amount of access reductions that AT&T believes they
12 will experience should the petitions be granted.

13 Then if you go down to Lines 16 through 19, you'll
14 see how AT&T proposes that they will pass through that
15 reduction. And, in fact, you can make a -- if you want to see
16 a portion of the access reduction that AT&T will pass through
17 to residential versus business customers, you can do that by
18 making a fraction. The numerator of the fraction is on Line 18
19 where they show the amount that would be passed on to
20 residential customers, and the denominator is from Line 5. I
21 can't say the percent because it would be revealing what
22 they've claimed is confidential. But you can see the portion
23 or the percentage of the access reduction that will flow
24 through to residential customers under AT&T's proposal, that
25 fraction is the number on Line 18 divided by the number on Line

1 5.

2 Compare that fraction to what we know the incumbents
3 are going to raise local rates. That's 93 percent for Verizon,
4 87 percent for BellSouth and 86 for Sprint. I would also ask
5 you to consider what local customers are going to get back if
6 you subscribe to AT&T, and that's described on Lines 16 through
7 17.

8 But even more important or at least as important as
9 seeing what customers will get back is what's not listed there.
10 And I wish I could describe it a little better to you, but it's
11 the best I've got with, you know, trying to handle confidential
12 information. But what you see on Lines 16 and 17, that's it.
13 That's what residential customers are going to get back. And
14 what's not listed there I think should be plainly obvious to
15 you. But that's the total, what customers are going to get
16 back. And you compare that to the \$2.95 that Verizon customers
17 will pay on this first installment, \$1.58 for Verizon -- I'm
18 sorry. \$2.95 for Sprint, \$1.58 for Verizon and \$1.25 for
19 BellSouth.

20 And AT&T, of course, is the market leader. Let's
21 look at the next one, which is the MCI witness testimony. And
22 what I've handed you is for reference is, is Pages 5 and 6.

23 COMMISSIONER DEASON: I'm sorry, Mr. Beck, before you
24 leave the AT&T.

25 MR. BECK: Yes.

1 COMMISSIONER DEASON: And here again I'm going to
2 endeavor not to divulge anything that's been classified
3 confidential, but when you refer to Lines 16 through 19, that
4 is the sum total of all benefit for residential customers being
5 proposed?

6 MR. BECK: Yes. Right. And you would compare that
7 to the total amount that AT&T will experience, which is listed
8 on Line 5. So that would be your, that would be your
9 proportion; the number that appears on Page, on Line 18 divided
10 by the number that is listed on Line 5.

11 Now as you in your head, you think of that
12 proportion, but I'm not going to say what it is, but you can
13 calculate it and I think get a very rough idea. I would ask
14 you then to return to MCI, and what I've handed you is Pages
15 5 and 6 from the testimony of MCI witness Dunbar, and you can
16 see the split. I mean, it's on Line 1 of Page 6. Look at the
17 split between residential and business because they list it
18 there. Again, comparing it to the 93 percent for Verizon,
19 87 percent for BellSouth and 86 percent that Sprint gets, and
20 you'll see what portion the residential customers will get back
21 from MCI.

22 Now MCI doesn't state precisely in this section
23 where, where the decreases or what exactly they will do to pass
24 on that percentage that you see there. But elsewhere in public
25 testimony AT&T, or MCI tells you that they will, they will

1 reduce their in-state connection fee by at least a third in
2 each of the three years. That's publicly stated in the
3 testimony by MCI.

4 CHAIRMAN JABER: Mr. Beck.

5 MR. BECK: Yes.

6 CHAIRMAN JABER: One of the customers this morning, I
7 think it was Mrs. Day, pointed to the part of the statute that
8 talked about, you know, the single-line businesses and how much
9 is flowed through to them. She referred to them as the mom and
10 pop operations.

11 MR. BECK: Yes.

12 CHAIRMAN JABER: Again, without revealing any of
13 those numbers, where -- are those included in the business
14 percentage or are they included in --

15 MR. BECK: That would be my, my take on it,
16 Commissioner. I don't, I don't know where it says specifically
17 what the single-line business would get from the testimony or
18 from the evidence that MCI has presented to you.

19 CHAIRMAN JABER: On its face this doesn't address
20 that?

21 MR. BECK: That's correct. What you have is a
22 breakdown between residential and business. I mean, that's the
23 cutoff. So I assume that means single-line businesses in the
24 business section there, and the residential is -- now what I
25 want to try to make you do is, and it's difficult to do this,

1 but if you look at the percentage that AT&T gives back to
2 residential versus business, compare that in your head to the
3 percentage you see from MCI and think about the, you know, how
4 they compare to each other.

5 Now from AT&T, they've told you exactly what that
6 proportion, what they're going to do with it. MCI doesn't tell
7 you, but they have said elsewhere about the in-state connection
8 fee, that they're committed to reducing at least a third of
9 that each year. If you put that all together, I think you can
10 conclude precisely what MCI is going to do by comparing the
11 different data and the information they've given. I can't
12 state it, but I think it's -- you could -- the conclusion you
13 would draw is pretty clear.

14 COMMISSIONER DEASON: Mr. Beck, I'm going to ask you
15 a question. If you can answer it, fine. I don't think it's
16 revealing anything confidential. But even if there's any
17 question about it, don't answer the question.

18 The percentage that is shown on Page 6, Line 1, for
19 residential --

20 MR. BECK: Yes.

21 COMMISSIONER DEASON: -- is it your understanding
22 that that percentage is achieved by reduction in in-state
23 connection fees and nothing else, or is that confidential
24 information? If it is, don't even answer the question.

25 MR. BECK: I think you have to draw the conclusion

1 from what I've said. I'm not willing to state that.

2 COMMISSIONER DEASON: All right. Thank you.

3 CHAIRMAN JABER: Do you know that though?

4 MR. BECK: No. You have to draw the conclusion. You
5 look at the percentages, residential versus business for MCI,
6 compare that to AT&T. You know what AT&T did, you know what
7 MCI is committed to. There's a conclusion that can be reached
8 from that, I believe.

9 CHAIRMAN JABER: I guess my point goes back to my
10 previous question. On its face these two pages don't tell us
11 that.

12 MR. BECK: You have to draw that conclusion. I'm
13 simply trying to give you the facts that I know them and the
14 conclusions that I would draw from them. I'm hoping you're
15 drawing the same conclusion. But, right, what you have before
16 you are the percentages from MCI and AT&T; you know what both
17 those percentages are that the residents will get back.

18 The next piece of evidence I'd ask you to consider is
19 Sprint, you know, just going down looking at the major carriers
20 in Florida. And what I've handed you is the excerpt from the
21 testimony from Sprint witness Kapka, Page 9. And on Page 9,
22 the confidential information again is the, the proportion of
23 the decrease that Sprint plans to give back to their
24 residential customers. Compare that to the increases where you
25 know what the proportions are from the evidence presented by

1 the incumbents, you know, in the ballpark of 90 percent, and
2 you can see how much the Sprint customers will be getting back.

3 I think what this evidence so far, and I'm about to
4 get to the Verizon local company evidence that you have,
5 reflects a massive transfer of wealth from residential
6 customers to business customers that will occur if you approve
7 the petitions by the incumbent companies. They won't get back
8 the rate increases that vary from \$1.25 to \$2.95 in the first
9 year.

10 We also have some evidence that we received from
11 Verizon, and the first thing I'd ask you to look at -- there's
12 two documents from Verizon we've put in there. The first are
13 Pages, Bate stamped 5 through 9. We've noticed our intent to
14 use this testimony or this document in the proceeding.

15 If you'll look at this document, you'll see that it's
16 dated August 8th, 2003. That date precedes the company's
17 submissions in this case. So, in other words, Verizon had this
18 information when they filed their first petition, which was
19 dismissed and then refiled, but this is information Verizon had
20 but was not filed in the case. We got it through discovery
21 after Commissioner Bradley had some rulings in our favor on
22 this and we obtained this from Verizon. I took a deposition of
23 Verizon on this document.

24 Let me briefly -- this is an analysis that Verizon
25 did on the impact that they thought that would occur on the

1 customers' bills that excluded bundled packages on it, but it
2 looked at the total bills that customers pay and it divided it
3 by rate group and so forth. It had an assumption in there. I
4 don't think this is accurate. The evidence will show you in
5 the case that this -- I believe that this is not accurate
6 information, given what we know about flow-throughs from the
7 companies. But Verizon -- but this is evidence that Verizon
8 has, and I'm about to show you some other testimony that was
9 submitted that follows up on this.

10 Verizon concluded, based on the assumptions they
11 made, and again this is what they thought. If you turn to Page
12 Bate stamp 8, second to the last page, and you'll see some,
13 you'll see a column, and this is when Verizon had two changes
14 in the prices they were going to charge customers. And what
15 they said is the total impact on customers' total bill, long
16 distance and local for the first year, would be the number that
17 you see on the row "Total" and on the column that changed
18 dollars per unit year one rates. And then you'll see another
19 number for year two rates. And if you add those two numbers,
20 the one under the -- one -- the bottom number under year one
21 rates plus year two rates, that was their conclusion that that
22 would be the impact on customers' bills from granting their
23 petition back when they had two changes over a one-year period.

24 You'll also see on Page 9 --

25 COMMISSIONER DEASON: Mr. Beck, before you leave Page

1 8.

2 MR. BECK: Yes.

3 COMMISSIONER DEASON: The amount at the bottom of
4 column for year one and then the amount at the bottom for
5 column labeled year two, you add those two numbers together,
6 you get the cumulative effect, and that number is, is net of
7 any toll benefits; is that correct?

8 MR. BECK: Yes, that's my, my understanding. And
9 Verizon assumed in this presentation that, that all of the
10 access reductions would be flowed through on a permanent basis
11 to customers. And so those numbers are net. That's the total
12 impact of everything, both the local increases and what the
13 long distance reductions that they thought would occur. And
14 this was filed -- this was prepared back in August before any
15 of the other information that we have was available. But
16 that's what they saw.

17 COMMISSIONER DEASON: But how could they make such a
18 calculation if they didn't know what percentage the IXCs were
19 going to utilize in, in allocating between residential and
20 business?

21 MR. BECK: They didn't know. They made an assumption
22 and they assumed --

23 COMMISSIONER DEASON: Oh, it was an assumption.

24 MR. BECK: Right. I do want to preface this, I think
25 this number is wrong, given what we know today. But this is

1 the evidence that Verizon had. This is evidence they had
2 before they filed, this is what they thought would be the
3 impact on total customers' bills, and it's evidence that
4 you'll -- and I'm about to address -- they've tried to update
5 this. I'm going to mention that in a minute about how they
6 think there's some updated numbers to this.

7 You'll see on the last page, Bate stamp 9, that they
8 took that total number, remember columns one and two, that
9 appears on Page 9, and they broke it down by demographic, by
10 age strata.

11 What they have said in public rebuttal testimony is
12 that the impact on the elderly will be slightly more than
13 average, and I'm going to show you the updated data. But this
14 is the data we had back from August, and this is the data that
15 Verizon had. And if you look at the different age groups, take
16 a look at the age groups of the elderly and look at the impact
17 on their total bills and compare it to others.

18 Now, their witness Danner has filed rebuttal
19 testimony. I think it's -- I'm not sure -- it's rebuttal, too,
20 other than the deposition I took of him, but there's some
21 rebuttal testimony of Carl Danner, and that's the last item in
22 your package. And there's three pages from his rebuttal
23 testimony: Page 2, Page 42 and Page 43. Now, Verizon says
24 they have updated the information that I just showed you. And,
25 again, this is without the benefit of seeing what the

1 interexchange carriers have done, but this is evidence in the
2 case and this is what Verizon is presenting to you.

3 And, again, they have shown at the bottom of Page
4 42 and the top of 43, they've shown you what they think is the
5 impact on total bills and they've broken it down by the same
6 age criteria. In the public testimony they say that this
7 reflects that the elderly will pay slightly more than the
8 average. I think their idea of slightly is a little different
9 than mine, but there's the numbers. You know, you can read it
10 and determine for yourself whether you think that's an accurate
11 description they've given in their testimony.

12 CHAIRMAN JABER: What is -- Mr. Beck, what is
13 confidential on Page 42? All of it?

14 MR. BECK: The -- it's numbers.

15 CHAIRMAN JABER: At the bottom?

16 MR. BECK: Right. I think the age strata is public
17 as far as what the, what age criteria are, but any of the
18 numbers next to them, the Florida lines and the net change,
19 those are both confidential.

20 CHAIRMAN JABER: Okay.

21 MR. BECK: So there's been various evidence presented
22 now. We know from the large interexchange carriers, you can
23 see what they plan to do. We have some evidence that Verizon
24 had that they didn't file in the case, but they've ultimately
25 had to file it in rebuttal after we had taken their deposition.

1 There may be some difference about the exact magnitude of the
2 impact on local customers, but one thing there isn't any
3 difference in, and that is that customers are going to pay
4 more. There's no dispute, it's not susceptible of any other
5 interpretation, the data, other than customers are going to pay
6 more. Residential customers, I'm sorry, residential customers
7 are going to pay more if you approve the petitions granted by
8 the companies.

9 The companies have submitted nothing showing that
10 their speculative and tangible benefits offset the demonstrated
11 harm that these petitions will cause residential customers.
12 Again, it's the companies' burden to show with evidence that
13 their speculative benefits exceed the demonstrated harm which
14 is the evidence that will be before you in this case. They
15 haven't done it. They've had a chance to make that case and
16 they haven't proven it, and the evidence is clear what's going
17 to -- the impact on residential customers. There's no dispute
18 that residential bills are going up.

19 Based on that, we ask you to grant the motion filed
20 by the Attorney General. We join in them, we agree with them,
21 and think the evidence unequivocally shows there will be no
22 benefit for residential customers; that, in fact, they'll be
23 harmed, if you approve these petitions. Thank you.

24 CHAIRMAN JABER: Thank you, Mr. Beck.

25 Let's see. AARP, you joined in the motion. Do you

1 have additional argument?

2 MR. TWOMEY: Yes, ma'am, but, and very briefly, but
3 just a couple of comments.

4 Madam Chair, Commissioners, you'll recall that the
5 AARP has taken the -- has expressed the fear from the very
6 first of the now 14 public hearings the Commission has
7 graciously undertaken in these dockets, the AARP has expressed
8 the fear consistently that notwithstanding its view that the
9 statute, especially as expressed by the legislators, required
10 residential customers to benefit financially by the reductions
11 in in-state toll calls. The AARP expressed to you the concern
12 that the statute could legally allow the IXCs, who are not
13 parties, to give as much as 99 percent of the flow-throughs to
14 their big business customers, while giving only 1 percent to
15 the residential. We complained about that and we complained
16 about that, and the Commission, in my view in any event, began
17 to take notice that this was a concern, that we only had part
18 of the equation, we had one-half of the equation. We knew what
19 the detriments were to the residential customers in particular
20 in the form of very specific rate increases being requested
21 here. We had no knowledge whatsoever of what benefits, if any,
22 were going to be passed back to the residential consumers in
23 the form of in-state toll reductions.

24 Now, I think, I think the, the information that
25 Mr. Beck has passed out to you, which I've seen, and I don't

1 have it in front of me now, so there's no danger, I think, of
2 me disclosing anything, I think you could average those numbers
3 and express them as an average and you would in no fashion
4 impinge on the companies' claims of competitive advantage.
5 What you would do is you'd embarrass them. You would embarrass
6 them exceedingly by disclosing the fact that if you were to go
7 through some kind of a concept of asking, is this number as big
8 as an elephant or how does it compare to a bread box and that
9 kind of thing, I think AARP believes that you'd have to find
10 that it's, that it's embarrassingly small. It's smaller than a
11 bread box; it's crumbs.

12 The IXCs who were essentially dragged into these
13 cases against their will, reluctantly so, at the last minute
14 reluctantly supplied this information claiming competitive
15 advantage or fear at every turn, in some cases only supplying
16 discovery to the Office of Public Counsel at a few minutes to
17 5:00 yesterday evening, have shown their hands, they've been
18 forced to show their hand on how they propose to return the
19 in-state toll reductions to their various classes of customers.
20 I believe that those numbers that are before you now,
21 Commissioners, confirm to the greatest degree the fear that
22 AARP has expressed to you from the outset.

23 There is, as Public Counsel has said, Mr. Shreve has
24 said on behalf of Attorney General, there is no way with the
25 evidence presented in this case, and it's all prefiled, nothing

1 else more can come in from the companies, there is no way that
2 a reasonable person could conclude that the residential
3 customers of this state, of these three companies, especially
4 the elderly, if Verizon's information that Mr. Beck has just
5 shown you is indicative, especially the elderly, who are my
6 clients primarily, can in any fashion benefit in a manner that
7 is meaningful.

8 Consequently, AARP believes that you have sufficient
9 evidence before you so that you can rule. You can grant the
10 Attorney General's motion and decide that there is, based on
11 the pleadings, the evidence before you, all the evidence that
12 can come before you, that there is no way that residential
13 customers of this state can benefit in a fashion as suggested
14 by the Legislature, as demonstrated by the Florida-based
15 transcripts of which you have before you and are now willing to
16 consider. Consequently, we would urge you to grant the
17 Attorney General of the State of Florida's motion and have
18 these people come back again, if they want, at a later time,
19 have all of them file their information, IXCs on the same date,
20 and restart the 90-day clock, if they wish. Thank you.

21 CHAIRMAN JABER: Thank you, Mr. Twomey.

22 Ms. White, I heard you say that the chief justice had
23 already addressed your arguments for the motion for summary
24 final order.

25 MS. WHITE: Yes, ma'am.

1 CHAIRMAN JABER: Mr. Chapkis, you've reserved your
2 opportunity to do that. And Sprint, what about you? He was
3 speaking on your behalf. I'm sorry.

4 MR. FONS: Yes.

5 CHAIRMAN JABER: Verizon, go ahead.

6 MR. CHAPKIS: Thank you, Chairman Jaber.

7 The Attorney General's motion for final summary order
8 should be denied because it fails to demonstrate that there are
9 no material issues of fact. Contrary to the Attorney General's
10 suggestions and the suggestions of the other petitioners here
11 who have joined, Verizon has submitted extensive testimony
12 demonstrating that its rate rebalancing plan satisfies the
13 criteria set forth in the statute.

14 Before I delve into the evidence that's been
15 presented by Verizon, it's important to understand the legal
16 standard governing the Attorney General's motion. The Attorney
17 General is moving for a final summary order. Because the final
18 summary order would bring a sudden and a drastic conclusion to
19 this case foreclosing Verizon from its right to a hearing on
20 the merits, the Attorney General's motion bears a heavy burden.
21 He must demonstrate the absence of a genuine issue of fact.
22 He's got to make the showing conclusively, and the Commission
23 must draw every possible inference in favor of the ILECs.

24 If the record reflects the existence of a material
25 issue of fact, the possibility of an issue or even the

1 slightest doubt that such an issue might exist, the Commission
2 cannot render a final summary order. Indeed, even if the facts
3 are undisputed, a single issue regarding the interpretation of
4 the facts precludes the Commission from rendering a final
5 summary order.

6 In this case the Attorney General and the other
7 petitioners have failed to demonstrate, much less conclusively
8 demonstrate that there are no issues of material fact. To the
9 contrary, Verizon has shown that its plan will remove basic
10 support for local services that stands in the way of increased
11 local competition that will benefit residential customers.

12 First, Verizon has demonstrated that its basic local
13 rates are supported. We've introduced the Commission-ordered
14 UNE rates to demonstrate that fact.

15 Second, Verizon has introduced evidence showing that
16 competitors focus much more heavily on business customers in
17 this state than they do on residential customers. Indeed,
18 Verizon has submitted a report showing that in its territory
19 there are 100 business customers served by competitive
20 facilities for every one residential customer. That clearly
21 shows that competition is not working for residential customers
22 here in the same manner that it's working for business
23 customers.

24 Third, Verizon has shown that reforming its local
25 rates will promote competition for those residential customers.

1 We've shown that reforming rates will make it easier for other
2 providers to offer services at competitive rates, thus making
3 the local exchange market more attractive to those competitors.
4 We've shown that a number of competitors are well positioned to
5 enter the market in response to the proposed rate reform, and
6 we've shown that AT&T and Knology have already entered the
7 market in anticipation of rate reform.

8 Finally, Verizon has demonstrated that the increase
9 in local competition resulting from the plan will provide clear
10 economic benefits to residential consumers. Verizon's
11 testimony shows that enhanced market entry will benefit
12 residential customers by encouraging competitors to offer the
13 best prices and the newest and most innovative products. It
14 also shows that enhanced market entry will place increased
15 pressure on Verizon to cut costs and to be efficient. It also
16 shows that reducing intrastate access rates will increase
17 consumer welfare by allowing residential customers to make more
18 long distance calls at lower prices. It also shows that
19 pricing reform will promote demand for broadband Internet
20 connections in Florida. These are very real benefits that will
21 flow to residential customers as the result of pricing reform.

22 In light of everything that I've just said, the
23 Attorney General's contention that there are no issues of
24 material fact is utterly incorrect. Verizon has submitted
25 substantial evidence demonstrating that its plan passes muster.

1 The Attorney General argues that there's a perceived
2 lack of evidence regarding how the IXCs will flow through the
3 evidence access reductions to the ratepayers, and this
4 contention is also erroneous.

5 The IXCs have submitted evidence demonstrating that
6 they will flow-through the access reductions for the benefit of
7 residential and business customers. For example, and one that
8 I didn't hear Mr. Beck emphasize, Verizon Long Distance has
9 submitted testimony stating that it plans to flow-through the
10 benefits realized from access reductions to both its business
11 and its residential customers based on the relative proportion
12 of the access minutes associated with these class of customers.

13 Now, Verizon has half of the long distance lines in
14 its territory, and that means that the substantial majority of
15 the reductions received by Verizon Long Distance will be flowed
16 through to residential customers.

17 The Attorney General and the other petitioners also
18 argue that Verizon's petition should not proceed further
19 because the evidence shows that there will be a net increase in
20 the average customer's bill. That claim lacks merit. For
21 residential customers, Verizon has shown that the average bill
22 impact over two years will net out to about \$1 a month. That's
23 50 cents per month per year for two years. Now given that the
24 average phone bill is over \$40 and the average cell phone bill
25 is also over \$40, the average increase in each customer's bill

1 will be 1 or 2 percent of what customers spend on those
2 services. The benefits of competition which this Commission
3 has sought to promote since divestiture and since the dawn of
4 the Telecommunications Act of 1996 will definitely outweigh
5 that cost.

6 Accordingly, the Commission should afford Verizon its
7 right to a hearing on the merits of its petition. What we
8 heard from the Attorney General and the other petitioners were
9 arguments of the facts. They were trying to tell you that
10 these facts do not warrant granting the, our petition. We
11 frankly disagree, and that's what the hearing is for. Thank
12 you.

13 CHAIRMAN JABER: Thank you, Mr. Chapkis.

14 AT&T.

15 MR. EARLY: Thank you, Madam Chairman, Commissioners.
16 My name is Gary Early with Messer, Caparello & Self.

17 I think what's been overlooked to some degree here is
18 that we're here on a very simple issue. This -- the
19 consideration of this motion is not the time in this proceeding
20 to weigh evidence or resolve evidentiary disputes. Public
21 Counsel and the Attorney General have given you excerpts of
22 testimony that they believe support their position, and they
23 want you to focus on those to the exclusion of all else. Even
24 to an extent, to an extent Mr. Chapkis kind of gave you his
25 view of the world. But that's not what a motion, motion for

1 summary final judgment standard is.

2 As this Commission has recognized, the standard for
3 granting a motion for summary final order is essentially the
4 same as that for granting a judicial motion for summary
5 judgment. And the courts in this state have said that in
6 determining whether or not summary judgment should be issued, a
7 court, in this case a Commission, is to treat the allegations
8 of the complaint as true. That is, every well-pled allegation
9 that is before this Commission, and that includes the testimony
10 that was filed with the, with the petitions, are to be
11 considered as though they are perfectly true and factual.

12 So what the Commission needs to do then is -- and I'm
13 just going to look at the petitions. I'm not even going to try
14 and go through all the testimony, but we can start with the
15 allegations in Sprint-Florida's petition. Sprint's amended
16 petition and associated amended testimony and exhibits
17 accompanying this amended petition together with the associated
18 testimony, exhibits, et cetera, address and fully satisfy each
19 of the provisions of the 2003 Act to be considered by the
20 Commission. The evidence presented by Sprint demonstrates that
21 reducing intrastate switched access rates to interstate parity
22 in a revenue-neutral manner over a two-year period will achieve
23 the goals of the 2003 Act by removing current support for basic
24 local telecommunication services that prevents the creation of
25 a more attractive competitive local exchange market for the

1 benefit of residential customers and by inducing induced,
2 enhanced market entry.

3 Is that statement true? The evidence in this case
4 will ultimately bear out whether that statement is true. But
5 for purposes of a determination of this summary final order,
6 that statement is true, and this Commission has to accept that
7 statement as true.

8 There are other statements that are of a similar
9 nature in Sprint's. Verizon's petition; Verizon states that
10 rebalancing retail rates in this fashion will promote
11 competition by enhancing the ability of competitors to enter
12 and serve the basic local exchange market. Enhanced
13 competition will benefit consumers by forcing all competitors
14 to operate more efficiently and lower their prices whenever
15 possible. It will also benefit residential consumers in
16 particular by making them a more attractive target for
17 efficient competitors that have every incentive to meet their
18 demands with new and innovative product and services. Is that
19 statement true? The evidence and the testimony that you will
20 hear throughout this proceeding will ultimately bear that out.
21 But for purposes of this summary final order, that statement is
22 true, and this Commission must accept that statement as true.

23 BellSouth's petition, in its -- they allege the
24 revised testimony clearly shows that BellSouth meets the
25 criteria set forth in 364.164, Florida Statutes, that is to be

1 considered by the Commission in granting this petition. Is
2 that statement true? Again, you're going to hear an amazing
3 amount of testimony. I've seen the, the testimony books and
4 they're, they're much more than the few pages that have been
5 given to you, and you're going to have to make that decision.
6 But for purposes of this summary final order, that statement
7 made by BellSouth in its amended petition is absolutely true
8 and must be accepted by the Commission as such.

9 So assuming these statements that I've just read, and
10 those are just pieces, little excerpts out of the amended
11 petitions, there are more statements in there that support that
12 general theme, but in order to save time I'm going to go -- I'm
13 going to not deal with them. Assuming those allegations are
14 true, the Commission cannot now as a matter of law determine
15 that the petitions do not meet the statutory criteria. That is
16 going to have to be a decision that's made after a review and
17 consideration of all the evidence that's going to be presented
18 to you over the course of the next few days.

19 I think there can be some consideration of what
20 constitutes a benefit, and I was going to kind of talk about,
21 you know, is a benefit necessarily a dollar or is it something
22 else? Is competition a benefit?

23 I believe in this case that the Legislature has
24 determined that the value of competition is a benefit to the
25 residential consumer. And this is not unlike the situation

1 that was faced when the original Bells were broken up and long
2 distance was segregated out. And this Commission and the
3 Supreme Court in the, in Microtel versus PSC, which is at
4 464 So.2d 1189, the Supreme Court recognized that the
5 Legislature looked at the benefit of competition and basically
6 made a fundamental primary policy decision that competition was
7 something that was advantageous to the public. So, so we, we
8 suggest that when the Commission reviews what is a benefit to
9 the consumer, that it not limit the scope of its review to a
10 very narrow decision of is a penny here going to be a penny
11 there. There is a bigger picture here. And competition in
12 general has to be factored into the Commission's decision.

13 In any event and in conclusion, the statements and
14 allegations that were made by the three ILECs in their amended
15 petitions must be considered by this Commission as being true
16 in its determination as to whether or not to grant a summary
17 final order. If those statements are true, this Commission
18 cannot, as a matter of law, determine that the Commission
19 should, or that the petition should be dismissed. And AT&T and
20 MCI requests that the Commission deny the motion for summary
21 final order.

22 CHAIRMAN JABER: Mr. Meros, did you file a written
23 response?

24 MR. MEROS: We did not file a written response, Your
25 Honor. We would like to briefly discuss the, some of the

1 factual underpinnings or the lack of underpinnings of the
2 Attorney General's motion.

3 CHAIRMAN JABER: Commissioners, let me open up that
4 question to you. I don't have a written response by Knology.
5 We've heard much argument. On the other hand, if you'd like to
6 hear from Knology, I certainly don't have any objection.
7 Commissioner Davidson.

8 COMMISSIONER DAVIDSON: I think it could be useful.
9 I personally would like to hear the comments.

10 CHAIRMAN JABER: Mr. Meros, go ahead.

11 MR. MEROS: Thank you, Madam Chair and Commissioners.
12 I will be brief, but I think it is particularly important that
13 Knology speak here because I think the motion misunderstands
14 what this statute is and what, what the determination of this
15 Commission must be. This statute is titled, "Competitive
16 Market Enhancement." Frankly, I do not believe and Knology
17 does not believe that this procedure -- this proceeding is
18 really about the ILECs. This is about competition in Florida
19 for the benefit of residential consumers and customers. And
20 the evidence, frankly, Commissioners, is unrebutted that the
21 grant of these petitions will enhance that competition to the
22 benefit of residential customers.

23 The file testimony of Mr. Felix Boccucci of Knology,
24 which again is essentially unrebutted, makes it clear that
25 Knology of Florida is just the type of company that wants to

1 come in, wants to compete aggressively throughout the state,
2 wants to offer lower services to residential customers, but is
3 limited dramatically in its ability to do so until there is a
4 more reasonable and efficient rate for local telephone services
5 so that it can compete in a, in a market where those
6 residential customers will ultimately substantially benefit.
7 And for the sake of time, I will not go over many of those
8 provisions in the testimony. But both in Mr. Boccucci's
9 written testimony and in discovery answers and in his
10 deposition, Mr. Boccucci of Knology makes it abundantly clear
11 that the benefits of competition will inure substantially to
12 residential customers if they have the ability to compete in
13 Florida. I'd urge the Commission to be looking at the
14 competition, the Knologys of the world that want to assist
15 residential customers, that want to provide the benefits, but
16 cannot do so in the absence of implementation of this
17 legislative mandate. Thank you.

18 CHAIRMAN JABER: Thank you, Mr. Meros.

19 General Crist, Mr. Shreve had asked for an
20 opportunity to rebut.

21 ATTORNEY GENERAL CRIST: Very briefly, Madam Chair.
22 Thank you.

23 You have ruled very well today that, in fact, it must
24 be considered the impact of this on the residential consumer.
25 It would defy logic not to. In all due respect to my friend

1 Justice Harding, the Attorney General's intent for filing a
2 motion for summary final order is not to dismiss the new law,
3 but rather to enforce the new law, and the new law calls for
4 revenue neutrality. And as we stated at the outset, it is
5 abundantly clear to me that when you're asking for a
6 \$350 million increase and you don't have a corresponding
7 decrease, common sense tells you that's anything but revenue
8 neutral. It just isn't so. And so I think what this motion is
9 about is fundamental fairness, it is about enforcing the law as
10 passed. We don't take issue with the law. We think it's a
11 good law. But only good law can be so if it's enforced
12 appropriately, and that's what we're asking for today. That's
13 what we're asking in terms of granting the Attorney General's
14 motion for summary final order; to reject this massive increase
15 on the backs of the Florida consumer, and we hope that you will
16 rule that way today. Thank you.

17 CHAIRMAN JABER: General Crist, let me -- we're done
18 with the presentations; correct? There are no other arguments?

19 Let me tell you just from the onset this is not a
20 motion I personally took lightly. I think my colleagues can
21 say the same, and they can speak for themselves. But I don't
22 have any questions on the motion. My decision on this motion
23 is purely based on legal grounds. I have, for the last four
24 years now, expressed concerns about motions for summary final
25 orders, and our former esteemed or esteemed former General

1 Counsel can attest to that. I asked, actually back in 2001
2 asked him to give me a legal opinion about the law as it
3 relates to motions for summary final orders and how they are
4 applied in administrative agencies, and he confirmed what
5 parties have beat into me, but our General Counsel confirmed
6 for me that the standard is a tough one. And when motions for
7 summary final orders are filed, they are filed, it's my
8 understanding, with the, the preference that all -- leniency is
9 not the right word. I think the exact word is we're supposed
10 to give the, the benefit of the doubt, the possible inference
11 in favor of the party who the motion for summary final order is
12 brought against. And that's tough; that's a very tough
13 standard to meet. And the very fact that we asked, I
14 personally asked Mr. Beck those questions as it relates to the
15 confidential exhibits, leaves in my mind that there are genuine
16 issues of material fact. The very fact that we've got
17 conflicting testimony and an opportunity to cross-examine, I
18 think, leaves the notion that there's a genuine issue of
19 material fact.

20 Saying all of that, in a case like this, if it's
21 going to be dismissed at the end of the day, I would much
22 rather dismiss it on the merits. And -- but that's the
23 opportunity I'd like. That's just where I'm coming from. I'm
24 not going to support the motion for summary final order, but it
25 was important to me to put on the record that that is not to

1 say that this is a case that won't warrant many, many
2 questions, and that is not to say that your arguments don't
3 further support my desire to have the information from the
4 IXC's. I think Mr. Beck has shown a great -- has done a great
5 job in further reinforcing my initial desire to have that
6 information, but I'm not going to support it, and it's purely
7 on the legal standard.

8 Commissioners, do you have questions, a motion or
9 comments? Commissioner Deason.

10 COMMISSIONER DEASON: I suppose I have a comment.
11 Madam Chairman, I agree with your comments, and I do agree that
12 a motion for summary final order, that the standard for
13 granting such a motion is an extremely high one. And I do
14 believe that there are issues of fact that if we take this
15 matter to hearing will better enable this Commission to
16 exercise our discretion, however we define that discretion to
17 be under the statute.

18 Having said that, though -- and, Madam Chairman, I
19 also agree with your statement that if, if motions, I'm
20 sorry -- if these petitions are going to be denied, it's best
21 to do that on the merits. And I don't know if these petitions
22 are going to be granted or denied, but I would agree that if
23 the burden is not met, and we had much discussion about burden
24 earlier today, if the burden is not met, it's best to make that
25 determination after there has been a full evidentiary hearing

1 and opportunity for all to present their evidence.

2 So having said all that though, let me maybe revert
3 back to something that was said at the November 3rd agenda
4 conference about burden of proof. It's squarely on the
5 petitioners in this case. And while I do recognize there are
6 issues of material fact and there are some broad policy
7 implications and the testimony will help us address that, the
8 fact remains that Mr. Beck has indicated some numbers to us
9 that are confidential which to me are troubling. The numbers
10 presented there, they may be the best result that can be
11 achieved considering broader policy implications and the effect
12 and benefits associated with competition. But I'm here saying
13 right now there is a mighty high burden in my opinion that has
14 to be met, if those numbers which Mr. Beck has indicated are,
15 are, in fact, accurate. And I have no basis to disagree; it's
16 in the prefiled testimony.

17 So while I agree that it's best to -- if a petition
18 is to be denied, deny it on the merits after a full opportunity
19 for hearing. My concern is that at the end of the day -- I
20 just think there needs to be some soul-searching done by the
21 petitioners in this case. And if they want to go forward with
22 it, fine, realizing what their burden is. It may be best to
23 withdraw these petitions, reevaluate the numbers which Mr. Beck
24 gave to us concerning allocations of benefits, and have that
25 for further consideration. That would save a lot of time and

1 effort at this point.

2 CHAIRMAN JABER: Uh-huh.

3 COMMISSIONER DEASON: I think I made that assessment
4 on November the 3rd --

5 CHAIRMAN JABER: Uh-huh.

6 COMMISSIONER DEASON: -- when I tried to indicate
7 that it would behoove those who have the burden to recognize
8 that there should be a broader reading of the statutory
9 criteria than what they were applying at that particular time.

10 But having said that, I am fully -- you know, I'm
11 prepared to go forward with the hearing. I think that we have
12 to deny -- in my opinion, we have to deny the motion for
13 summary final order. We have to give the parties an
14 opportunity to carry this matter to hearing and hear all of the
15 evidence. There are issues of material fact, there are some
16 broad policy implications. I welcome the opportunity to hear
17 from everyone involved, all of the experts, and hear the
18 cross-examination, and I will certainly endeavor to, to
19 consider all of that and make an informed, fair, impartial
20 decision.

21 However, there is a lingering question about the
22 share of the burden on residential customers and the allocation
23 of benefits to residential customers, which I think is a high
24 burden to meet. And I'm just laying it out for everyone at
25 this point.

1 CHAIRMAN JABER: Commissioners, questions or any
2 other comments or a motion?

3 COMMISSIONER DEASON: I would move that we would deny
4 the motion for summary final order consistent with the
5 discussion just taken place.

6 COMMISSIONER BAEZ: Second.

7 CHAIRMAN JABER: Okay. And just to be clear,
8 Commissioner Deason, this would be all motions for summary
9 final order?

10 COMMISSIONER DEASON: That's correct.

11 CHAIRMAN JABER: And a second. All those in favor,
12 say aye.

13 (Unanimous affirmative vote.)

14 CHAIRMAN JABER: The motions for summary final order
15 are denied unanimously.

16 Ms. Keating, that addresses all of the preliminary
17 motions.

18 MS. KEATING: That is correct, Madam Chairman.

19 CHAIRMAN JABER: Commissioners, let me take an
20 opportunity to thank the parties for their very, very
21 informative, concise presentations on the motions we discussed
22 this morning. We appreciate it. I hope that's a sign of
23 what's to come.

24 We are going to take a break. Before we take a
25 break, I want to, true to form, I'd like to go ahead and send

1 some directives out to folks that are participating in this
2 proceeding with a request that you listen to these comments
3 because this is the approach and the procedure we will follow
4 for the rest of this proceeding.

5 Commissioner Bradley, I want to commend and
6 congratulate you for an outstanding prehearing order. I intend
7 to follow it to the T, which means, parties, you should be
8 aware that I have read that order thoroughly, and it's my
9 understanding direct and rebuttal will be taken up at the same
10 time. It's my understanding the prehearing officer has
11 directed your witnesses to start their responses with a yes or
12 no first. The prehearing officer has directed you all to use
13 these red folders for confidentiality, to caution your
14 witnesses not to release that confidential information, and I
15 extend the same caution to you. It's my understanding the
16 prehearing officer has established a five-minute time period
17 for summary of testimony. I would add to that that if the
18 testimony is five pages, we don't expect five minutes of
19 summary.

20 I understand that parties have waived opening
21 arguments, but have reserved the opportunity to have
22 eight-minute closing arguments. That's fine. I will hold you
23 to that at the end of this proceeding.

24 You should also know that we are prepared to go late
25 in the evenings. You should be prepared to go late in the

1 evenings. Do not approach this Commission about taking
2 witnesses out of order unless it's an extreme emergency. I
3 want your witnesses to be prepared when they are called.
4 Please also take notice that Saturday is a possibility. That
5 doesn't make for a friendly group of Commissioners, so you need
6 to govern yourselves accordingly.

7 I think, Commissioners, I haven't forgotten anything.
8 I hope you've captured the tone of what I'm trying to send to
9 you in terms of signaling.

10 With that, we are going to break for an hour.
11 Thanks, and let's come back and do good.

12 (Recess taken.)

13 CHAIRMAN JABER: Ms. Keating, are we ready to get on
14 the record?

15 MS. KEATING: Yes, Madam Chair.

16 CHAIRMAN JABER: Let's see. We've resolved all of
17 the outstanding motions. I understand that there are some
18 outstanding confidentiality matters. Do you want to brief me
19 on that? Although it doesn't look like there's any action to
20 be taken, but --

21 MS. KEATING: There are a few pending requests for
22 confidential classification that came in just within the past
23 24, 48 hours that we have not been able to have addressed yet.
24 Those will be addressed by separate order as expeditiously as
25 possible. But until those are ruled on, all the parties are

1 aware that the information needs to be treated as confidential
2 information until otherwise ruled on.

3 CHAIRMAN JABER: Okay. And it's my understanding you
4 have some stipulated exhibits. I need to resolve the, whether
5 the exhibits that were submitted at some of the service
6 hearings were admitted into the record or not. You'd initially
7 told me that the exhibits were not admitted into the record.
8 The court reporter's office has given me a list that indicates
9 the first three were.

10 MS. KEATING: Okay.

11 CHAIRMAN JABER: In the abundance of caution, what
12 I'll do -- there are four exhibits total. What I'd like to do
13 is go ahead and say what those exhibits are and readmit them
14 into the record just so that we're absolutely sure.

15 MS. WHITE: Madam Chairman, I'm going to object to
16 moving one of those exhibits in.

17 CHAIRMAN JABER: Which one, Ms. White?

18 MS. WHITE: I'm not sure what the number is. It's
19 Number 4.

20 CHAIRMAN JABER: Okay. Let me read, read them out
21 then separately.

22 Exhibit 1 was the statement of Tanner Andrews, and
23 without objection that will be admitted into the record.

24 Composite Exhibit 2 was a white paper by Bob Sears,
25 and without objection that will be admitted into the record.

1 Exhibit 3 was a Beth Anne Algie letter from
2 BellSouth, and without objection that will be admitted into the
3 record.

4 (Exhibits 1, 2 and 3 admitted into the record.)

5 CHAIRMAN JABER: Composite Exhibit 4, this just says,
6 "Ms. Padron's packet." I don't know what that is.

7 MS. KEATING: Ms. Padron's packet.

8 CHAIRMAN JABER: Padron. Okay.

9 MS. KEATING: It was -- later the full thing was
10 submitted by -- the Office of Public Counsel provided that in
11 the file.

12 CHAIRMAN JABER: Okay. And, Ms. White, you have an
13 objection to that exhibit?

14 MS. WHITE: Yes, ma'am.

15 CHAIRMAN JABER: What's the nature of your objection?

16 MS. WHITE: My objection is that this package is a
17 compilation of anonymous letters, of newspaper articles, of
18 e-mails between Ms. Padron and the staff. I think it comprises
19 hearsay and prejudicial information and shouldn't be allowed
20 into the record.

21 CHAIRMAN JABER: Did I understand you correctly,
22 staff, that Public Counsel put this exhibit into the, or
23 identified the exhibit at one of the service hearings,
24 Mr. Beck?

25 MR. BECK: I think Commissioner Baez asked that we

1 put it into the record. Commissioner Baez asked me to
2 distribute copies to all the parties. I think it was
3 identified when the witness offered it. And as with any, any
4 other thing, any other exhibit that a witness offered, you
5 know, we put it forth.

6 CHAIRMAN JABER: Okay. You've heard the objection.
7 Do you have a response to the objection?

8 MR. BECK: I think it ought to be treated the same as
9 the other exhibits. I see no distinction, and the Commission
10 can give it the weight it deserves.

11 CHAIRMAN JABER: Staff, do you have a recommendation?
12 Mr. Twomey.

13 MR. TWOMEY: Yes, ma'am. Just briefly I'd note, as
14 y'all know, as counsel knows, that hearsay is not strictly
15 precluded in administrative hearings, and I would urge you to
16 do the same with Mr. Beck.

17 CHAIRMAN JABER: Ms. Keating, do you have a
18 recommendation?

19 MS. KEATING: Yes, Madam Chairman. Staff would
20 recommend that it be allowed in and, again, as indicated by
21 Mr. Beck, given the weight that it's due.

22 CHAIRMAN JABER: Okay. I have to tell you, I'm going
23 to accept your recommendation, recognizing for the record that
24 I have not seen this information. I was not at that service
25 hearing. Ms. White, I am aware of your objection and that it

1 does contain anonymous letters, and I think for the record we
2 should state that those people aren't testifying here in this
3 proceeding. And recognizing all of that, Mr. Twomey and
4 Ms. Keating are correct, that in administrative hearings
5 hearsay evidence is allowed and must be corroborated if it's to
6 be relied upon.

7 MS. WHITE: Well, Madam Chair, if you're going to
8 allow that information in, then I would move to enter a United
9 States District Court, Southern District of Florida order as
10 well as a United States Court of Appeals, 11th Circuit order
11 that goes to this person's motive and credibility for filing
12 such a packet.

13 CHAIRMAN JABER: Let me finish the exhibit, and we'll
14 entertain that.

15 As such, composite Exhibit 4 will be admitted into
16 the record and given the weight it deserves.

17 (Exhibit 4 admitted into the record.)

18 CHAIRMAN JABER: Now in that regard, Ms. White,
19 you're seeking to officially recognize orders?

20 MS. WHITE: We can officially recognize them. I have
21 copies I can hand out to you, if you'd like. It is the United
22 States District Court, Southern District of Florida, Miami
23 Division, order granting motion for summary judgment in the
24 case of Padron versus BellSouth Telecommunications, Case Number
25 00-3489, and United States Court of Appeals for the 11th

1 Circuit, judgment in Number 02-12441, again, Sandra Padron
2 versus BellSouth. I'll be happy to hand out copies of these,
3 but I feel they're appropriate to be admitted into the record
4 because it goes to motive and credibility.

5 CHAIRMAN JABER: Okay. Go ahead and pass out the
6 copies. We won't rule on your request for official recognition
7 until that happens. We'll go forward with the stipulated
8 exhibits. And, Ms. White, between you and Ms. Keating, after
9 parties have taken a look at that documentation, we'll
10 entertain your request.

11 MS. WHITE: Yes, ma'am. Thank you.

12 CHAIRMAN JABER: Okay. Ms. Keating.

13 MS. KEATING: Excuse me. Madam Chairman, there are a
14 number of stipulated discovery exhibits that we've reached
15 agreement with the parties can be entered into the record at
16 this time. The list that you received yesterday had a couple
17 of errors in it. We have passed out a highlighted revision to
18 that list to you now and have discussed these revisions with
19 the parties. And as I understand it, there are no objections
20 to the corrections we've made to the list.

21 CHAIRMAN JABER: The revised list, have you given it
22 to the court reporter?

23 MS. KEATING: Yes, ma'am.

24 COMMISSIONER JABER: You've given it to the
25 Commissioners?

1 MS. KEATING: Yes, ma'am.

2 CHAIRMAN JABER: And to all the parties?

3 MS. KEATING: That is correct.

4 CHAIRMAN JABER: Here what's we're going to do.

5 Stipulation-1, Stip-1 is identified as composite Exhibit 5.

6 Stip-2 is identified as composite Exhibit 6. Stip-3 is

7 identified as composite Exhibit 7. Stip-4 is identified as

8 composite Exhibit 8. Stip-5 is identified as composite Exhibit

9 9. Stipulation-6 is identified as composite Exhibit 10.

10 Stipulation-7 is identified as composite Exhibit 11. The

11 highlighted stipulations are confidential exhibits or --

12 MS. KEATING: No, Madam Chairman. Those are the
13 corrections that we made.

14 CHAIRMAN JABER: Okay. Stip-8 is identified as
15 Exhibit 12. Stip-8A is identified as composite Exhibit 13.

16 Stip-9 is identified as Exhibit 14. Stip-10 is identified as

17 Exhibit 15. Stipulation-11 is identified as composite Exhibit
18 16.

19 MS. KEATING: Madam Chairman.

20 CHAIRMAN JABER: Yes.

21 MS. KEATING: I need to correct the next one. The
22 last item in that list should be 25 through 26 on Item 4 of
23 Stip-12. I mean, it should be 25 through 27.

24 CHAIRMAN JABER: Oh, okay.

25 MS. KEATING: I'm sorry. Other than that, it's

1 correct.

2 CHAIRMAN JABER: Stipulation-12 as corrected by Ms.
3 Keating is identified as composite Exhibit 17. Stipulation-13
4 is identified as composite Exhibit 18. Stipulation-14 is
5 identified as composite Exhibit 19. Stipulation-15 is
6 identified as Exhibit 20. Stipulation-16 is identified as
7 composite Exhibit 21. Depo-1 will be Exhibit 22. Depo-2 will
8 be Exhibit 23. Depo-3 will be Exhibit 24. Depo-4 will be
9 Exhibit 25. Depo-5 will be Exhibit 26. Depo-6 will be Exhibit
10 27. Depo-7 will be Exhibit 28. Depo-8 will be Exhibit 29.
11 Depo-9 will be Exhibit 30. Depo-10 will be identified as
12 Exhibit 31. Depo-11 will be identified as Exhibit 32. Depo-12
13 will be identified as Exhibit 33. Depo-13 will be identified
14 as Exhibit 34. Depo-14 will be identified as Exhibit 35.
15 Depo-15 will be identified as Exhibit 36. Depo-16 will be
16 identified as Exhibit 37. Depo-17 will be identified as
17 Exhibit 38.

18 (Exhibits 5 through 38 marked for identification.)

19 CHAIRMAN JABER: Now all of the confidential exhibits
20 that have Verizon in them, Ms. Keating, I'm looking at
21 confidential Stipulation-1 through Stipulation-9, can I
22 identify those as a composite exhibit?

23 MS. KEATING: That seems fine to me.

24 CHAIRMAN JABER: Mr. Chapkis, do you need them
25 separate or --

1 MR. CHAPKIS: No objection to a composite exhibit.

2 CHAIRMAN JABER: Okay. Confidential

3 Stipulation-1 through confidential Stipulation-9 are identified
4 as composite Exhibit 39.

5 (Exhibit 39 marked for identification.)

6 CHAIRMAN JABER: And I'm assuming the same is true,
7 Ms. White, for the BellSouth exhibits?

8 MS. WHITE: Yes, ma'am, that will be fine.

9 CHAIRMAN JABER: Confidential Stipulation-12 and
10 confidential Stipulation-13 are identified as composite Exhibit
11 40.

12 (Exhibit 40 marked for identification.)

13 CHAIRMAN JABER: Sprint, I can do the same with
14 yours?

15 MR. FONS: Yes, you may.

16 CHAIRMAN JABER: Confidential Stipulation-14 through
17 confidential Stipulation-21 are identified as composite Exhibit
18 41. Confidential Stipulation-22 will be identified as Exhibit
19 42. Confidential Stipulation-23 will be identified as Exhibit
20 43. Confidential Stipulation-24 will be identified as Exhibit
21 44.

22 (Exhibits 41 through 44 marked for identification.)

23 CHAIRMAN JABER: Seeing no objections to Exhibits
24 5 through 44, they'll be admitted into the record.

25 (Exhibits 5 through 44 admitted into the record.)

1 CHAIRMAN JABER: Are there other exhibits, stipulated
2 exhibits?

3 MS. KEATING: The remaining stipulated exhibit that
4 I'm aware of is the 2003 Competition Report.

5 CHAIRMAN JABER: Did I just see that? Where did I --
6 that was not previously identified?

7 MS. KEATING: Well, let me check this list again.
8 Maybe I'm wrong.

9 CHAIRMAN JABER: Yeah. Stipulation-10 identified and
10 admitted Exhibit 15 into the record, and that's the 2003
11 Competition Report.

12 MS. KEATING: You're correct, Madam Chairman. I
13 apologize. I had, was anticipating seeing it at the end of our
14 list.

15 COMMISSIONER JABER: No problem. Parties, do you
16 have any other stipulated exhibits?

17 Okay. Does that take us to the first witness?

18 MS. KEATING: I believe it does, Madam Chairman.

19 CHAIRMAN JABER: I believe it does. Okay. If you're
20 a witness in this case and you are in the room, please stand,
21 raise your right hand.

22 (Witnesses collectively sworn.)

23 CHAIRMAN JABER: Is Mr. Gordon our first witness?

24 MR. FONS: Yes. Dr. Gordon is the first witness, and
25 Dr. Gordon is being sponsored by BellSouth, Verizon Florida and

1 Sprint-Florida.

2 CHAIRMAN JABER: Okay. Mr. Fons, is he your witness?

3 MR. FONS: Yes. He's my witness.

4 CHAIRMAN JABER: Go right ahead.

5 KENNETH GORDON

6 was called as a witness on behalf of Verizon Florida, Inc,
7 BellSouth Telecommunications, Inc, and Sprint-Florida, Inc,
8 and, having been duly sworn, testified as follows:

9 DIRECT EXAMINATION

10 BY MR. FONS:

11 Q Dr. Gordon, will you state your full name, please.

12 A Kenneth Gordon.

13 Q And, Dr. Gordon, did you previously cause to be
14 prepared and prefiled in this proceeding direct, amended direct
15 testimony consisting of 44 pages on September 30th, 19 -- 2003?

16 A Yes, I did.

17 Q And do you have any corrections or changes to that?

18 A I do not.

19 Q And if I were to ask you the same questions today,
20 would your answers be the same?

21 A They would.

22 MR. FONS: Madam Chairman, I would ask that Dr.
23 Gordon's amended direct testimony be inserted into the record
24 as though read.

25 CHAIRMAN JABER: The amended direct testimony of Dr.

1 Kenneth Gordon shall be inserted into the record as though
2 read.

3 BY MR. FONS:

4 Q And, Dr. Gordon, were there two attachments to your
5 testimony?

6 A Yes, there were.

7 Q And one was Attachment A, your curriculum vitae?

8 A I'm sorry. I can't hear you.

9 Q Was your Attachment A your curriculum vitae?

10 A Yes, it was.

11 Q And consisting of 16 pages?

12 A I believe that's right.

13 Q And was that prepared under your direction and
14 control?

15 A It was.

16 Q And did you also have an Attachment B, which is
17 titled, "Percent of CLEC Lines Sold to Residential and Small
18 Business Customers by State as of December 31, 2002," a
19 one-page document?

20 A Yes.

21 Q Was that prepared by you or under your direction and
22 control?

23 A It was.

24 MR. FONS: Madam Chair, I would ask that the
25 Attachment A and Attachment B be designated an exhibit number.

1 A composite would be fine.

2 CHAIRMAN JABER: Sure. Attachment A and Attachment B
3 with Mr. Gordon's direct testimony shall be identified as
4 composite Exhibit 45.

5 (Exhibit 45 marked for identification.)

6 BY MR. FONS:

7 Q And do you have any corrections or changes to
8 exhibit, composite Exhibit 45?

9 A No.

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AMENDED DIRECT TESTIMONY OF
DR. KENNETH GORDON

1 **AMENDED DIRECT TESTIMONY OF DR. KENNETH GORDON**

2

3 **I. PURPOSE & SUMMARY OF CONCLUSIONS**

4 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

5 A. My name is Dr. Kenneth Gordon. My business address is One Main Street, Cambridge,
6 Massachusetts 02142. My C.V. is provided as Attachment A.

7

8 **Q. WHAT IS YOUR CURRENT POSITION?**

9 A. I am a Special Consultant of National Economic Research Associates, Inc. ("NERA").
10 Previously, I was Senior Vice President at NERA.

11

12 **Q. WILL YOU PLEASE SUMMARIZE YOUR EDUCATION AND PROFESSIONAL**
13 **QUALIFICATIONS?**

14 A. I am an economist and former Chairman of the Maine Public Utilities Commission
15 ("Maine Commission") and the Massachusetts Department of Public Utilities ("Mass.
16 DPU"). The Mass. DPU is now known as the Massachusetts Department of
17 Telecommunications and Energy. I have been an economist since 1965, and I have been
18 directly involved with developing and establishing regulatory policy at the federal and
19 state levels since 1980, when I became an industry economist at the Federal
20 Communications Commission ("FCC").

21

22 I received my A.B. degree from Dartmouth College in 1960. I received my M.A. degree
23 in 1963 and my Ph.D. degree in 1973, both in economics, from the University of Chicago.
24 I have taught applied microeconomics, industrial organization, and regulation (as well as
25 other subjects) at Georgetown University, Northwestern University, University of

1 Massachusetts at Amherst, and Smith College.

2

3 From 1980 to 1988, I was an industry economist at the FCC's Office of Plans and Policy,
4 where I worked on a full range of regulatory issues, including telecommunications, cable,
5 broadcast, and intellectual property rights. At the FCC, one of the major focuses of my
6 work was activity aimed at introducing competition into communications markets.

7

8 Prior to joining NERA in November 1995, I chaired the Maine Commission (1988 to
9 December 1992) and the Mass. DPU (January 1993 to October 1995). During my term as
10 Chairman of the Mass. DPU, the DPU investigated and approved a price cap incentive
11 regulation plan for NYNEX and also undertook a proceeding to examine interconnection
12 and other issues related to the development of competition at all levels of
13 telecommunications, including basic local service.

14

15 While a regulator, I was active in the National Association of Regulatory Utility
16 Commissioners ("NARUC"), serving on its Communications and Executive Committees.
17 In 1992, I served as President of NARUC. I was also Chairman of the BellCore Advisory
18 Committee and the New England Governor's Conference Power Planning Committee.

19

20 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

21 A. Verizon Florida Inc., BellSouth Telecommunications, Inc., and Sprint-Florida Inc., ("the
22 companies") are seeking to restructure their rates for intrastate network access services
23 ("intrastate access") and basic local telecommunications services ("basic local") in

1 accordance with recently passed legislation by the Florida Legislature.¹ The companies'
2 revised plans—which must address the criteria established in the legislation—call for
3 them to restructure their intrastate access and basic local rates in a revenue-neutral
4 manner.

5

6 The companies have asked me to provide an economic and policy analysis of their revised
7 rate plans and to testify on whether I believe those revised plans meet the criteria laid out
8 in the legislation.

9

10 **Q. WHAT ARE YOUR MAJOR CONCLUSIONS?**

11 A. After reviewing the newly-enacted legislation, the evidence in this case—specifically the
12 companies' revised plans and the cost evidence submitted by the companies' witnesses—
13 and based on my general knowledge and expertise on telecommunications economic and
14 regulatory matters, I conclude that the revised plans submitted by the companies meet the
15 criteria contained in the legislation. Specifically, upon implementation, the revised plans
16 will, *inter alia*:

- 17 • Reduce current support for basic local telecommunications services that prevents
18 the creation of a more attractive competitive local exchange market for the benefit
19 of residential consumers; and
20 • Induce enhanced market entry.

21 The companies' revised plans significantly decrease support for basic local service by
22 reducing prices for a service that has historically and purposely been an important
23 source—but by no means the only source—of support for basic local services, namely

¹ See Section II below.

1 intrastate access. In order to achieve revenue neutrality, the companies' revised plans
2 increase residential basic local prices towards cost-based levels, thus creating a more
3 attractive market for potential entrants, ultimately for the benefit of residential consumers.
4 Both theory and empirical evidence show that low residential basic local prices have
5 hindered the development of residential competition. By better aligning residential basic
6 local prices with cost, competitors will have increased incentives to target a broader mix
7 of residential consumers, which is the intent of the Florida legislature.

8
9 In addition, I conclude that the revised plans will enhance economic welfare in Florida by
10 increasing economic activity. As described in the respective testimonies of the
11 companies' cost witnesses, the cost evidence submitted in this proceeding demonstrates
12 that rates for residential basic local service diverge significantly from their underlying
13 costs. A movement toward costs—and, therefore toward more rational economic
14 pricing—will bring with it several economic benefits. These benefits include providing
15 market participants—i.e., customers, the companies and potential and actual
16 competitors—with more cost-based price signals, which will improve economic decision
17 making and lead to more economically rational utilization of telecommunications services.
18 Economic activity in Florida will increase as a result of the companies' revised plans
19 because rebalancing generates substantial consumer benefits. Telephone consumers are
20 better off as a result of moving prices more in line with costs, and will likely increase their
21 purchases of those services whose price has come down. Perhaps of even greater
22 significance, competitive telephone service providers will be seeing better price signals
23 for local service, and will be able to invest without having to face the level of subsidized
24 competition they have faced in the past. New investment by these providers should, at the
25 margin, increase.

1

2 The cost evidence presented by the companies demonstrates that basic local prices are
3 receiving an economic subsidy from other services. The companies submitted forward-
4 looking direct cost evidence to demonstrate that their residential basic local services are
5 priced below the costs the companies incur to provide the services. Forward-looking
6 direct cost is the basis for determining whether a service is receiving an economic subsidy.
7 Moreover, consistent with this Commission's ruling, the companies' cost witnesses, when
8 measuring the economic subsidy flowing to basic local services, correctly assign the entire
9 cost of the loop to basic local.

10

11 I also conclude that the companies' revised plans will not jeopardize universal service in
12 the state of Florida. The companies' residential basic local prices are substantially below
13 the national average and Florida is not a poor state. The Florida Public Service
14 Commission ("Commission") has the flexibility to approve the companies' revised plans
15 and still have residential basic local prices remain affordable. The Florida Legislation
16 requires that any price increase in basic local service not apply to Lifeline consumers and
17 also increased the income eligibility for Lifeline consumers to 125 percent, thus protecting
18 those customers most likely to be sensitive to potential price increases from a rebalancing
19 plan. Importantly, the companies' revised rebalancing plans will lead to lower intrastate
20 toll prices for all consumers. At the end of the day, the mix of services that consumers
21 purchase as a result of the companies' revised plans will make consumers better off
22 overall.

23

24 Finally, the fact that some customers may experience unwanted rate changes should not be
25 an argument for the status quo. Good policy requires weighing and balancing the costs

1 and benefits of particular actions. While it may seem that maintaining current prices is the
2 least objectionable thing to do from a policy perspective, there is an implicit but very real
3 cost to continuing the status quo. The deployment of next generation, advanced networks
4 depends crucially on providing all market participants the sound economic signals that
5 will encourage efficient investment and innovation. Cost-based prices provide the
6 incentives needed to bring to market the new services that customers demand. This
7 cannot be accomplished by distorted prices.

8

9 **Q. YOU HAVE NOTED IN YOUR MAJOR CONCLUSIONS THAT VERIZON**
10 **FLORIDA INC., BELLSOUTH TELECOMMUNICATIONS, INC., AND SPRINT-**
11 **FLORIDA INC. HAVE REVISED THEIR RESPECTIVE RATE REBALANCING**
12 **PLANS FILED ON AUGUST 27, 2003 TO EXTEND THE TIME OVER WHICH**
13 **INTRASTATE NETWORK ACCESS AND BASIC LOCAL**
14 **TELECOMMUNICATIONS RATES WILL BE REFORMED. HAVE YOU**
15 **REVIEWED THESE COMPANIES' REVISED PLANS?**

16 A. Yes, I have.

17

18 **Q. DO THESE REVISIONS AFFECT YOUR ANALYSIS OF THE COMPANIES'**
19 **PLANS OR YOUR TESTIMONY?**

20 A. No. With the exception of the minor changes — changing “plans” to “revised plans” —
21 as well as this and the previous question and answer, my testimony remains unchanged
22 from the testimony that I filed on August 27, 2003.

23

1 **II. BACKGROUND**

2 **Q. PLEASE DESCRIBE THE BASIS FOR THE COMPANIES' REQUEST TO**
3 **INCREASE BASIC EXCHANGE PRICES.**

4 A. From an economic perspective, the fact that the companies' current residential basic local
5 prices are not fully recovering their forward-looking economic cost is, by itself, a good
6 enough reason to begin the process of moving them to more economically rational levels.
7 Both theoretical and empirical research have shown that rebalancing rates and moving
8 them toward levels more commensurate with their underlying costs results in significant
9 benefits to telecommunications consumers and, by so doing, benefits the economy as
10 well.² Rebalancing rates has also been demonstrated to have a positive effect on
11 competitive entry into the local exchange market.³

12

13 The immediate catalyst for the companies' revised plans is the recent changes in Florida
14 laws. I have been informed by counsel that the legal authority for the companies' request
15 arises from recent changes in the statutory framework in Florida. During the 2003 regular
16 legislative session, the Legislature passed Senate Bill 654, the Tele-Competition
17 Innovation and Infrastructure Enhancement Act ("Tele-Competition Act"). The Tele-
18 Competition Act implements several important policies, but for our purposes the relevant
19 Section of the Tele-Competition Act is § 364.164 "Competitive market enhancement."

20

21 **Q. WHAT ARE THE IMPORTANT PROVISIONS OF § 364.164?**

22 A. § 364.164 permits local exchange telecommunications companies to petition the

² See Section IV below.

³ See Section III.

1 Commission to reduce their intrastate access rates in a revenue-neutral manner. In
2 reaching its decision, § 364.164 (1) states that the Commission shall consider whether
3 granting the petitions will:

- 4 a. Remove current support for basic local telecommunications services that
5 prevents the creation of a more attractive competitive local exchange
6 market for the benefit of residential consumers;
- 7 b. Induce enhanced market entry;
- 8 c. Require intrastate switched network access rate reductions to parity over a
9 period of not less than 2 years or more than 4 years; and
- 10 d. Be revenue neutral as defined in subsection (7) within the revenue
11 category defined in subsection (2).

12 Throughout my testimony, I will focus on whether the companies' revised plans are
13 consistent with and meet the criteria provided in § 364.164 (1) (a) and (b). Other
14 company witnesses discuss how the companies' revised plans would meet criteria (c) and
15 (d).

16

17 **Q. IN ORDER TO REDUCE INTRASTATE ACCESS RATES IN A REVENUE**
18 **NEUTRAL MANNER, RATES FOR OTHER SERVICES NEED TO BE**
19 **INCREASED. WHAT SERVICES DO YOU BELIEVE SHOULD BE**
20 **INCREASED?**

21 A. The first category of services that should be considered are those services whose current
22 prices do not recover fully their underlying costs, such as residential basic local
23 telecommunications services. Rates for these subsidized services should be increased in
24 order to better reflect their real economic cost. This is confirmed in §364.164 (2), where
25 the legislation calls for the creation of a revenue category mechanism consisting of basic

1 local telecommunications service revenues and intrastate switched network access
2 revenues in order to achieve revenue neutrality. That is, the legislation states that in order
3 to achieve revenue neutrality, if intrastate access prices are reduced, then basic local
4 service prices need to be increased.

5
6 The current rate design for telephone services—where basic local services are priced
7 below cost and other services, including intrastate access service, are priced in such a way
8 so as to provide the support—while in the process of being reduced or eliminated in a
9 number of states, continues to be encountered in state regulation of telephone services.
10 However, as the Florida Legislature wisely recognized, whatever benefits such a rate
11 design policy has arguably achieved in the past, such as helping the United States achieve
12 universal telephone service—the continuation of such policies frustrates another important
13 policy goal of Federal and state regulators, namely, the establishment of efficient
14 competition to as broad a base of business and residential consumers as is economically
15 feasible—not to mention the economic costs that arise from price-cost distortions, *per se*,
16 as I discuss further below.

17
18 The current rate design policy as it pertains to residential basic local services, frustrates
19 that policy goal and by enacting § 364.164, the Florida Legislature has provided the
20 Commission with the direction it needs to make competition work better for all Florida
21 consumers.

22 **Q. ARE THE COMPANIES' REVISED PLANS CONSISTENT WITH § 364.164 (1) (a)**
23 **and (b)?**

24 A. Yes. The companies' revised plans are consistent with and meet the criterion of §
25 364.164(1)(a) and (b). Below in Section III, I fully describe why I believe that the

1 companies' revised plans are consistent with and meet those criteria.

2

3 **Q. DR. GORDON, FROM A POLICY PERSPECTIVE DO YOU BELIEVE THAT IT**
4 **IS APPROPRIATE TO ENGAGE IN THE TYPE OF REBALANCING THAT IS**
5 **BEING CONTEMPLATED BY THE COMPANIES' PLANS?**

6 A. Yes, I do. In this testimony, I describe fully why I believe that the companies' revised
7 plans are consistent with the criteria of the Tele-Competition Act that the Commission
8 shall consider and why the revised plans would likely result in increasing competitive
9 activity in the state of Florida. Specifically, the revised plans will create a more attractive
10 local exchange market for residential consumers and lead to enhanced market entry—two
11 criteria that need to be considered by the Commission in addressing the companies'
12 revised plans. By making the residential local exchange market more attractive,
13 residential consumers will likely see more companies competing for their business, which
14 will, in turn, result in more options for residential consumers, improved services and
15 lower prices for their telecommunications services. From a policy perspective, it is
16 appropriate to accomplish these tasks.

17

18 In addition, I describe below the history of rate design for basic local services in the
19 United States and how the end result of these policies has been uneconomically low
20 residential basic local prices; lower than what one would expect to find in undistorted
21 competitive markets. Of course, states have differed in their implementation of these
22 policies and, as a result, residential basic local service prices vary quite a bit from state to
23 state. In Florida, residential basic local prices are quite low when compared to prices in
24 other states. In Table I below, I list the flat-rate charges for each of the three companies'
25 lowest and highest rate groups compared to the national average flat-rate charges. As can

1 be seen in the table, each of the companies' highest rate group is well below the national
2 average of \$14.55 per month.

3

4 **Table I – Comparison of Verizon, BellSouth and Sprint's flat-rate residential basic**
5 **local charges and National Average flat-rate charges**

Company	Lowest Rate Group	Highest Rate Group	Unweighted Average	National Average (2002)
Verizon	\$9.72	\$12.06	\$10.89	
BellSouth	\$7.57	\$11.04	\$9.31	
Sprint	\$7.63	\$11.48	\$9.56	
National Average (2002)				\$14.55

6 Source: Florida Senate Staff Analysis And Economic Impact Statement, p. 4, April 8, 2003; FCC *Reference*
7 *Book of Rates, Price Indices, and Household Expenditures for Telephone Service*, Table 1.1 July 2003, rates
8 exclude Federal and State subscriber line charges, touch tone charge and taxes, 911 and other charges.

9

10 **Q. HOW DOES THE FACT THAT FLORIDA HAS LOW RESIDENTIAL BASIC**
11 **LOCAL TELECOMMUNICATIONS PRICES RELATE TO THIS**
12 **PROCEEDING?**

13 A. It relates to this proceeding in two important ways. First, the Legislature has correctly
14 perceived that low residential basic local prices have led the residential local exchange
15 market to be less attractive to competitors than would be the case with more economically
16 rational residential basic local prices. In Section III below, I describe fully why, from an
17 economic perspective, I believe the Legislature is absolutely correct on this point. Put

1 simply, holding all other factors constant, the lower the residential basic local price (when
2 set governmentally without regard to whether the prices cover cost), the more unattractive
3 those customers are to actual and potential competitors. Since Florida residential basic
4 local prices are lower than those in many other states, and in fact lower than the national
5 average, the problem facing potential new entrants as a result of these low rates is likely to
6 be even more severe and pronounced in Florida than in other states. For this reason, it is
7 even more important that Florida policymakers tackle this problem sooner rather than
8 later.

9

10 **Q. IS THERE ANY SUPPORT FOR YOUR ASSERTION THAT THE PROBLEM OF**
11 **AN UNATTRACTIVE RESIDENTIAL MARKET MAY BE WORSE IN FLORIDA**
12 **THAN IN OTHER STATES?**

13 A. Yes, there is some support for my assertion. The FCC compiles data on local telephone
14 competition. Its most recent report, released June 12, 2003 included a table that lists, for
15 each state available, the percentage of lines provided to residential and small business
16 customers by ILECs and CLECs.⁴ The FCC provided data on 40 states and of those 40
17 states Florida ranked 30th in the percent of CLEC lines that were sold to residential and
18 small business customers. This means that in 29 out of 40 states, CLECs' served
19 proportionately greater residential customers than in Florida (see Figure 1 at the end of
20 this testimony). Florida ranks below states such as Georgia (58%), Alabama (52%),
21 Louisiana (61%) and Virginia (70%) to name a few, all of which have higher residential
22 prices. This provides some evidence that low residential basic local prices are having a

⁴ See, *Local Telephone Competition: Status as of December 31, 2002*, Table 11, Industry Analysis and Technology Division Wireline Competition Bureau, Federal Communications Commission.

1 negative impact on residential competition in Florida.

2

3 **Q. YOU MENTIONED THAT THERE WAS A SECOND REASON WHY YOU**
4 **BELIEVE THAT FLORIDA'S LOW RESIDENTIAL BASIC LOCAL PRICES, IN**
5 **COMPARISON WITH OTHER STATES, ARE RELEVANT IN THIS**
6 **PROCEEDING. WHAT IS THAT SECOND REASON?**

7 A. The second reason has to do with affordability considerations and the flexibility this
8 Commission has in rebalancing rates while still maintaining basic residential local rates
9 that are quite affordable for most Florida consumers. As mentioned above, the
10 companies' prices for residential basic local services are generally well below the national
11 average. However, Florida is not a poor state. According to data from the U.S. Bureau of
12 Economic Analysis, Florida is on par with the national average in personal income per
13 capita.⁵ Specifically, as of 2001, the data show that personal income per capita in Florida
14 was \$29,047 compared to the national average of \$30,413. Thus, the Commission has the
15 flexibility to increase residential basic local prices, which are currently well below the
16 national average, to more economically reasonable levels without making the services
17 unaffordable to Florida consumers.

18

19 At the same time, Florida consumers will pay less for intrastate toll calls. The companies'
20 rebalancing plan will lower the access charge component of the cost of producing
21 intrastate toll calls. IXCs are required to pass these cost savings through to consumers in
22 the form of lower prices. Thus, even with the increase in basic residential local rates,
23 telecommunications will be just as affordable to Florida consumers as before, yet

⁵ Bureau of Economic Analysis, Regional Economic Information System, Table SA1-3.

1 consumers will be better off because they will be consuming a different mix of
2 telecommunications services that provides more value than they are currently receiving.

3
4 In addition, the Tele-Competition Act also requires that any increase in basic local service
5 rates not apply to Lifeline customers and that the ILECs increase Lifeline participation to
6 125 percent of federal poverty income level.⁶ These requirements further protect low-
7 income consumers—and it is low-income consumers who would be most prone to
8 disconnections in the face of price increases—thus providing the Commission with even
9 more flexibility to approve the companies' rate rebalancing request with minimal concern
10 that such a rate restructuring would negatively affect subscribership. I discuss this point,
11 and other reasons why I believe the companies' revised plans will not negatively affect
12 subscribership in Florida, in more detail in Section VI below.

13

14 **Q. VERIZON, BELLSOUTH AND SPRINT ARE FILING THEIR REVISED PLANS**
15 **AT THE SAME TIME. IS THERE ANY PUBLIC POLICY BENEFIT TO**
16 **HAVING THE COMMISSION REVIEW THE COMPANIES' REVISED PLANS**
17 **AT THE SAME TIME?**

18 A. Yes. The benefits are at least threefold. First, to the extent that basic local rates are
19 simultaneously adjusted closer to their costs throughout the territory of the three
20 companies serving 98 percent of the ILEC customers, the better competition will be
21 benefited and market entry enhanced. Certain providers who might be positioned to
22 provide facilities-based basic local service (e.g. cable telephony, electric and wireless
23 providers) will not necessarily configure their coverage areas based on the ILECs service

⁶ § 364.10(3)(a).

1 territories. For them the potential staggered implementation of the rebalancing could be
2 an obstacle to competitive entry. There are several areas within Florida where at least
3 two of the three major ILECs provide service where it may be economical for a new
4 entrant to provide service regardless of the ILEC boundary. For example, the
5 Orlando/Central Florida (BellSouth/Sprint) area, Southwest Florida (between Sarasota and
6 Ft. Myers (Verizon/Sprint)) area and the Pensacola – Ft. Walton – Destin -- Panama City
7 (BellSouth/Sprint/BellSouth) area are three relatively compact geographic areas served in
8 part by at least two of the three companies. Each of these areas might appropriately
9 comprise the service territory of a single facilities-based entrant. When the price
10 increases contained in the company plans are implemented and signal to these entrants that
11 pricing distortions are being reduced on a broad basis, the competitors may be able to
12 more efficiently execute their business plans.

13

14 Second, it is also important to avoid unnecessary marketplace distortions that could affect
15 the purchase decisions of end-users. End-users normally make their purchase decisions
16 based in large part on relative price differences among providers. If the rate-rebalancing is
17 not implemented across all companies simultaneously, end-users will make these
18 decisions based on incomplete and imperfect information as they see some providers'
19 rates increasing while other providers' rates remain the same (at least temporarily). The
20 risk will be that regulatory scheduling rather than the relative costs and benefits of various
21 service offerings becomes the driving force behind consumers' decisions. For example, it
22 is easy to imagine a situation involving two or more of the ILECs —where a CLEC might
23 be able to offer service at a legitimate cost savings to all customers, but if re-balancing is
24 not done simultaneously perhaps only one firm's customers would respond to the
25 competitive offer, because the other firm's rate increase had yet to be implemented.

1 Coordinated rate rebalancing across all companies will ensure that potential competitors
2 are not artificially disadvantaged when introducing new service offers by artificial
3 boundaries, and that customers are not disadvantaged by incorrect and incomplete
4 information driving their purchase decisions.

5

6 Third, the magnitude and timing of the access charge price reductions for the three
7 companies would also benefit end users statewide. IXCs will be able to implement more
8 meaningful price reductions if they can aggregate their access cost reductions into a single
9 round of pricing changes.

10

11 **Q. THE LEGISLATION PERMITS A COMPANY TO RESTRUCTURE ITS RATES**
12 **OVER A MINIMUM OF TWO YEARS AND A MAXIMUM OF FOUR. EACH OF**
13 **THE COMPANIES PLANS TO HAVE INTRASTATE ACCESS RATES REACH**
14 **PARITY WITH INTERSTATE RATES OVER A TWO-YEAR PERIOD. DO YOU**
15 **BELIEVE THIS IS A GOOD IDEA?**

16 A. Yes I do, for several reasons. First, it is clearly permitted by the Tele-Competition Act.
17 Second, it is a matter of economic principle that economic welfare is at its highest when
18 prices are based on their underlying forward-looking costs and are not distorted. As I
19 discuss in greater detail in Section III, prices that are distorted provide inferior signals for
20 market participants and result in losses in consumer welfare because investment and
21 purchase decisions by firms and consumers do not reflect the true costs that society incurs
22 to provide the services. The companies' revised plans reduce these pricing distortions in
23 the Florida telecommunications markets sooner rather than later and, by so doing, achieve
24 economic efficiency gains sooner as well.

25

1 Third, a possible reason why one would prefer a more gradual rate restructuring time
2 frame has to do with avoiding consumer “rate shock”. As the words imply, rate shock
3 implies that the increase in price proposed by the company is so high, that consumers
4 would be obviously and adversely affected. However, based upon my personal
5 experience as a former commissioner, as well as what I have observed in other states, I do
6 not believe that the yearly increase in basic local prices will result in rate shock.

7

8 **Q. PLEASE EXPLAIN WHY YOU BELIEVE THAT THE COMPANIES’ PLANS**
9 **WILL NOT RESULT IN RATE SHOCK.**

10 A. The companies’ revised plans will result in relatively minor increases in a customer’s
11 basic local price. In addition, as I stated earlier, these price increases will not even apply
12 to current Lifeline consumers and new Lifeline consumers who have become eligible as a
13 result of the Tele-Competition Act raising the income threshold to 125% of the poverty
14 level.

15

16 In addition, with the reduction and elimination of the in-state connection fees, many
17 customers might not even experience a significant change in their total bill. If there is an
18 increase in the customers’ bill, it will likely result in large part from increased stimulation
19 from lower long distance charges that represent real gains to consumers because they are
20 now able to make more calls at the new lower prices.

21

22 Finally, the companies’ revised plans compare favorably with other states that have
23 approved rate-rebalancing plans that approved much larger increases than the companies’
24 request. Importantly, these states’ price adjustments did not jeopardize universal service.
25 In Section VI, I also discuss the experience of some of the states that have already

1 implemented serious rate rebalancing plans, including Massachusetts where I presided as
2 Chairman through one such adjustment.

3

4 **III. THE COMPANIES' REVISED PLANS WILL RESULT IN A**
5 **"MORE ATTRACTIVE COMPETITIVE LOCAL EXCHANGE**
6 **MARKET FOR THE BENEFIT OF RESIDENTIAL CONSUMERS"**
7 **AND WILL INDUCE "ENHANCED MARKET ENTRY"**

8

9 **Q. HOW DO YOU JUDGE WHETHER THE COMPANIES' REVISED PLANS**
10 **MEET THE CRITERIA OF § 364.164 (1) (a) AND (b)?**

11 A. § 364.164 (1) (a) states that the companies' plans should remove the current support for
12 basic local telecommunications services that is impeding the creation of a more attractive
13 competitive local exchange market for the benefit of residential consumers. In order for
14 the companies' revised plans to meet the first criterion, they must show that the revised
15 plans remove—or at a minimum reduce—support for basic local telecommunications. By
16 so doing, they create a more "attractive" competitive local exchange market, because the
17 price to be competed against by new entrants is raised to more closely reflect the real
18 economic costs of doing business. The second criterion for the Commission's
19 consideration is § 364.164 (1) (b) which simply states that the plans should induce
20 enhanced market entry and no distinction is made between residential or business
21 consumers.⁷

22

⁷ There are other criteria in § 364.164 (1) that I do not discuss but that are the subject of the companies' respective witnesses.

1 Therefore, in evaluating whether the companies' revised plans meet the criteria in these
2 sections, I must ascertain whether the revised plans: (1) remove current support for basic
3 local telecommunications services, and (2) will likely result in a more attractive
4 competitive environment that would benefit residential consumers and induce enhanced
5 market entry.

6

7 **Q. DO THE COMPANIES' REVISED PLANS REMOVE CURRENT SUPPORT FOR**
8 **BASIC LOCAL TELECOMMUNICATIONS SERVICES?**

9 A. Yes, the companies' revised plans significantly decrease current support for basic local
10 telecommunications services. The revised plans do this by reducing the prices of a service
11 that has historically been set by regulators to provide an important source—but by no
12 means the only source—of support for basic local services, namely, intrastate switched
13 network access.

14

15 **Q. WHY DO YOU BELIEVE THAT INTRASTATE SWITCHED NETWORK**
16 **ACCESS CURRENTLY SUPPORTS BASIC LOCAL TELECOMMUNICATIONS**
17 **SERVICES?**

18 A. There are two reasons. The first is the historical rate design policy prevalent in
19 telecommunications regulation in Florida and throughout the United States. As I
20 mentioned earlier, historically, telecommunications rate design was premised on the
21 policy goal—at times stated and sometimes left implicit—of keeping the price of basic
22 local telecommunications low or as low as possible. This policy began early on in
23 telecommunications regulation and was accomplished through the rate design mechanisms
24 that were part and parcel of traditional regulation. Traditional regulation required two
25 broad steps. The first was to determine a revenue requirement that was sufficient to meet

1 the prudently incurred operating expenses and a reasonable return on prudently invested
2 capital. The second broad step was the rate design process, which determined the price of
3 each regulated service to ensure that the regulated company had the opportunity to recover
4 its revenue requirement from its regulated service.⁸ Normally, a proper rate design
5 process would require that the price of any service recover at least its underlying cost and,
6 in addition, contribute to the firm's shared and common cost in some manner. At times
7 that manner was consistent with economic efficiency goals—as when demand
8 considerations were taken into account—and at other times it was more reflective of other
9 policy considerations—as when an equal percentage markup was applied across the board
10 to the different services.

11

12 For basic local services, however, in most instances the price was set on a residual basis
13 without taking into consideration the underlying cost of providing basic local
14 telecommunications. That is, the goal of residual pricing was to keep basic local prices
15 low, or as low as possible, and to recover more revenue from other telecommunications
16 services, constrained by what consumers were willing to pay for the non-basic
17 telecommunications services and by—as competition began to become more prevalent in
18 telecommunications markets—the threat of customers bypassing the public switched
19 telecommunications network.

20

21 Prior to divestiture of AT&T in 1984, toll prices provided the bulk of support for basic
22 local telecommunications services. As technological advances lowered the cost of

⁸ I say opportunity to recover its revenue requirement because the regulatory process does not generally guarantee a regulated company a certain return, it only provides the regulated company the opportunity to earn a certain return.

1 providing toll services, toll prices did not decrease commensurately and were used as a
2 means to support basic local telecommunications services—i.e., to keep the prices of basic
3 local lower than would otherwise be the case. After divestiture of AT&T, interstate and
4 intrastate switched network access services were substituted as a means of supporting
5 basic local telecommunications services.

6

7 Notably, even after the substitution of price cap regulation for traditional regulation, the
8 cross subsidies that were present under traditional regulation have been maintained.

9

10 The notion that intrastate switched network access services have been used as a source of
11 support for basic local telecommunications is confirmed in the Florida *Senate Staff*
12 *Analysis and Economic Impact Statement on the Tele-Competition Act*, where it states:

13 According to the commission, intrastate network access service rates were set
14 well above the incremental cost of providing the service in order to keep rates
15 for basic local telecommunications service as low as possible and to encourage
16 subscribership.⁹

17

18 The second reason why I believe that intrastate access services currently support basic
19 local service is cost considerations. As described in the testimonies of their witnesses, the
20 companies have established that the price of residential basic local telecommunications
21 services is below forward-looking direct cost estimates. From an economic perspective,
22 whenever the revenues from a service are insufficient to recover its forward-looking direct
23 costs, that service is said to be in receipt of an economic subsidy. The source of the

⁹ See Senate Staff Analysis and Economic Impact Statement on CS/SB 654, April 8, 2003.

1 subsidy—including that for residential basic local services—comes from all those services
2 that are priced above their respective forward-looking direct costs. As a whole, these
3 services contribute to the support of residential basic local. Because intrastate access
4 services are priced significantly above their forward-looking direct costs, this means that
5 intrastate switched network access services are supporting basic local service.

6

7 **Q. DOES THIS IMPLY THAT THERE MAY BE OTHER SERVICES, BESIDE**
8 **INTRASTATE ACCESS SERVICES, THAT MAY ALSO BE SUPPORTING**
9 **BASIC LOCAL TELECOMMUNICATIONS SERVICES?**

10 A. Yes, that is correct. In general, for multi-product firms, where there are significant
11 amounts of shared and common costs, firms must, in the aggregate, price their services
12 above forward-looking direct costs in order to earn sufficient revenues to remain viable.
13 When one service is priced below its forward-looking direct costs, as is the case for
14 residential basic local telecommunications services, other services that are priced above
15 forward-looking direct costs are supporting the service that is priced below its own
16 forward-looking direct costs.

17

18 The Florida Legislature, however, has specifically determined that it is the support
19 provided by intrastate switched network access that is to be reduced. The Tele-
20 Competition Act calls for rebalancing to take the form of lowering intrastate access rates
21 to parity—over a 2 to 4 year period—with interstate switched network access rates and to
22 simultaneously increase basic local telecommunications services by an amount sufficient
23 to make up the revenue over the same time period. Under this approach, there is still no
24 guarantee that residential basic local services recover at least their forward-looking direct
25 costs once intrastate access rates are set to parity with interstate switched access rates. In

1 fact, according to the companies' evidence, residential rates will still be below forward-
2 looking direct costs even when intrastate switched network access rates reach parity with
3 the interstate rates.

4

5 Therefore, while the companies' revised plans are consistent with the criteria to be
6 considered by the Commission, the plans do not result in the complete rebalancing of
7 rates. Thus, there will still likely be some (lesser) distortions in prices even after the
8 implementation of the plans.

9

10 **Q. AS AN ECONOMIST, DO YOU BELIEVE THAT REBALANCING IS**
11 **COMPLETED ONCE BASIC RESIDENTIAL PRICES ARE SET AT FORWARD-**
12 **LOOKING DIRECT COSTS?**

13 A. While having basic local services recover at least their underlying forward-looking direct
14 costs is a good first step, it would not necessarily result in economically efficient prices.
15 As I discuss in greater detail below in Section IV, economically efficient prices require
16 that a multi-product firm's shared and common costs be recovered through markups on
17 each service or product above forward-looking direct costs in a manner that least distorts
18 economic efficiency. Therefore, to have economically efficient basic local prices would
19 likely require that basic local services be priced above forward-looking direct costs.
20 However, as markets become more competitive, markups will be limited by the need to be
21 competitive with other firms in the market.

22

23 **Q. HAVING ESTABLISHED THAT THE REVISED PLANS REMOVE CURRENT**
24 **SUPPORT FOR BASIC LOCAL, § 364.164 (1) (a) PROVIDES THAT, AS A**
25 **RESULT OF THE REMOVAL, THEY WILL RESULT IN A MORE**

1 **ATTRACTIVE COMPETITIVE LOCAL EXCHANGE MARKET FOR THE**
2 **BENEFIT OF RESIDENTIAL CONSUMERS. WILL THE COMPANIES’**
3 **REVISED PLANS MEET THIS CRITERION?**

4 A. Yes, the companies’ revised plans will create a more attractive competitive local exchange
5 market for the benefit of residential consumers. Economic theory and empirical research
6 both indicate that this will likely be the case. I discuss these two factors below.

7

8 **Q. PLEASE DISCUSS WHY YOU BELIEVE THAT ECONOMIC THEORY**
9 **SUGGESTS THAT THE COMPANIES’ REVISED PLANS WILL LIKELY**
10 **RESULT IN A MORE ATTRACTIVE COMPETITIVE LOCAL EXCHANGE**
11 **MARKET FOR THE BENEFIT OF RESIDENTIAL CONSUMERS?**

12 A. One of the key components of the companies’ revised plans is that intrastate access
13 revenues will be decreased in a revenue-neutral manner by increasing the price of (and
14 revenue from) basic local telecommunications services for residential consumers. The
15 cost information provided by the companies in this proceeding indicates that residential
16 basic local telecommunications prices are currently below forward-looking direct costs.
17 Increasing the price of a service, especially a service that is below forward-looking direct
18 costs, will make for a more attractive market for actual and potential competitors.
19 Competitors will not rationally try to compete against heavily subsidized prices.

20

21 **Q. WOULD YOU PLEASE EXPLAIN WHY YOU BELIEVE THIS TO BE THE**
22 **CASE?**

23 A. In a market economy, prices are the essential tool that send signals to market participants
24 that, in turn, determine market behavior and outcomes. For example, as prices increase or
25 decrease, consumers alter their consumption decision because the value consumers place

1 on goods and services changes in relation to price. Producers alter their production,
2 investment and research and development decisions as well, because as prices increase or
3 decrease, profits change along with them. It is the search for profits that drives firms to
4 enter or expand into new markets. As prices change, potential entrants into the market
5 will be affected as well. Lower prices may act to keep new firms from entering the
6 market and higher prices more reflective of cost will tend to attract new firms into the
7 market.

8

9 Like any other firm, the investment decision of a telecommunications competitor is based
10 on the present value of the cash flows that the investment project is likely to generate over
11 the useful economic life of the project. Holding all other factors constant, when the price
12 of a service increases, a cash flow analysis would show that the investment project
13 becomes more profitable (or less of a loss) and thus more attractive. In the case before us,
14 an increase in the price of basic local telecommunications service would increase the
15 revenues from residential basic local services in a cash flow analysis, thus increasing the
16 attractiveness of providing those residential services. As a result of rate rebalancing,
17 where the companies plan to raise residential basic local prices, the residential local
18 exchange market will look more attractive to all actual and potential telecommunications
19 providers of residential services.

20

21 **Q. WILL THE COMPANIES' REVISED PLANS ALSO PROVIDE INCREASED**
22 **INCENTIVES FOR OTHER COMPETING TELEPHONY TECHNOLOGIES?**

23 A. Yes. An important reason for opening local telecommunications markets to competition is
24 the belief that technological change is proceeding so rapidly that competitive markets will
25 do a much better job than monopoly of discovering which technologies can or cannot

1 succeed in the long run. For example, access to customers for their telecommunications
2 needs comes in the form of fixed-wireline access, wireless access, cable telephony,
3 Internet, and potentially satellite and even access via electric utilities. Of course, not all of
4 these technologies will necessarily survive in the long run and competition will likely lead
5 to a mix of technologies surviving and providing the lowest possible cost for each
6 consumer's telecommunications needs.

7

8 However, in order for the lowest-cost mix of technologies to remain in the market, prices
9 and the signals they send must not be distorted and must reflect the underlying cost of
10 providing service. The companies' revised plans move positively in this direction and
11 encourage new entrants—regardless of the chosen technology—to enter or expand in the
12 marketplace because even competitors using lower-cost (or more attractive) technologies
13 may not be able to compete against a subsidized ILEC price that does not fully reflect its
14 own costs. This would be a loss for consumers and the Florida economy.

15

16 **Q. IS THERE EVIDENCE THAT OTHER FORMS OF ACCESS ARE COMPETING**
17 **WITH FIXED-WIRELINE ACCESS?**

18 A. Yes. The Florida Commission has recognized the actual and potential substitution
19 occurring between fixed-wireline and other forms of access, including wireless and
20 emerging IP-telephony providers. As the Commission states:

21 Regarding the substitution of technology and services, as they are being found
22 to be close substitutes to traditional wireline services, both wireless and

1 emerging broadband IP-telephony providers must be included in the analysis.¹⁰

2

3 In the same report, the Florida Commission cites nation-wide data indicating that about
4 5% of U.S. wireless subscribers have disconnected wireline service and conclude that
5 substituting wireless for wireline services appears to be a national trend.¹¹ Moreover, as
6 the same report concludes, Florida may be especially susceptible to this phenomenon
7 because of the large population in Florida that also has residences in other states. For
8 many of these consumers, “it makes little sense to continue paying for telephone service
9 that sits idle much of the year when wireless enables them to stay connected wherever
10 they are.”¹²

11

12 The Florida Commission has also concluded that cable providers are competing directly
13 with fixed-wireline providers. The Commission cites to national data that shows that by
14 second quarter of 2002, there were 2.5 million cable telephony subscribers and that cable
15 companies expect to see one-third of their digital cable households take cable telephony
16 service by 2005.¹³

17

18 There is evidence that the Tele-Competition Act is already having a positive impact on
19 competitors’ incentive to enter and expand in the Florida market. On July 18, 2003,
20 Knology, a provider of broadband and voice telephony services, announced it has entered

¹⁰ See, Florida Public Service Commission, *Telecommunications Market in Florida Annual Report on Competition As of June 30, 2002*, December 2002, p. 6.

¹¹ *Ibid.*, at 7.

¹² *Ibid.*, at 9.

¹³ *Ibid.*, at 10.

1 into a definitive agreement to purchase certain assets from Verizon Media Ventures, Inc.¹⁴
2 Knology offers local and long distance telephone service and its purchase of Verizon's
3 Americast cable system will permit it to compete directly with Verizon. In its press
4 release announcing its decision, Knology stated:

5 In commenting on this transaction, Knology noted that the Tele-Competition
6 Act recently enacted in Florida positively influenced its decision to expand
7 operations in the state. This Act, as written by the Florida Legislature and
8 supported by Governor Bush, laid the foundation for companies like Knology
9 to enter the Florida market, and offer competitive services and products to
10 consumers.

11

12 **Q. IS THERE EMPIRICAL EVIDENCE THAT SUPPORTS YOUR VIEW THAT**
13 **RATE REBALANCING WILL LIKELY MAKE THE RESIDENTIAL LOCAL**
14 **EXCHANGE MARKET MORE ATTRACTIVE?**

15 A. Yes, there is empirical evidence. Two of my colleagues at NERA investigated empirically
16 whether low residential basic local rates were having any impact on competition in the
17 states and, specifically, whether low rates were hindering the development of residential
18 competition.¹⁵ In that paper, the authors hypothesized that inefficient local exchange
19 prices are having an impact on competition and that, specifically, low residential prices
20 are inhibiting competition for residential customers. To test their hypotheses, the authors
21 compared how local competition varied across the different states depending on how

¹⁴ See, Knology Press Release July 18, 2003, *Knology Announces Agreement to Purchase Broadband Asset*.

¹⁵ See, Agustin J. Ros and Karl McDermott, "Are Residential Local Exchange Prices Too Low? Drivers to Competition in the Local Exchange Market and the Impact of Inefficient Prices," in Michael Crew, *Expanding Competition in Regulated Industries*, Kluwer Academic Publishers, 2000.

1 “unbalanced” were local exchange prices. Specifically, the authors estimated several
2 cross-section econometric models of facilities-based competition, controlling for things
3 such as cost and demand considerations in the different states. The authors also included
4 several policy variables, including one that measured the degree to which residential local
5 exchange prices were “distorted” in each state. The authors summarized their results, as
6 they pertained to residential competition, as follows:

7 Using OLS and GLS estimates we found a significant and positive association
8 between states that have more “balanced” tariffs and residential competition.
9 For two measures of residential competition used in our data, we found that
10 “rebalancing” tariffs by 10% leads to approximately a 9% and 13% increase,
11 respectively, in residential competition.¹⁶

12
13 In addition, James Eisner (an FCC staff member) and Professor Dale E. Lehman
14 performed a somewhat similar study.¹⁷ Eisner and Lehman state in their conclusion:

15 ...in some specifications, there appears to be less competitive entry
16 (principally facilities-based) where residential rates are lower. These findings
17 are generally statistically significant at the 90% level.¹⁸

18
19 Finally, another empirical study examined rate rebalancing in Latin America and found
20 that rate rebalancing in some Latin American countries has led to increases in the supply

¹⁶ *Ibid.*, at 167.

¹⁷ See, James Eisner and Dale E. Lehman, *Regulatory Behavior and Competitive Entry*, presented at the 14th Annual Western Conference Center for Research in Regulated Industries, June 28, 2001. The authors’ main motivation appears to have been ascertaining how regulatory behavior—as it pertains to unbundled loop prices and 271 entry—affects competitive entry. Nevertheless, they control for local exchange prices as well.

¹⁸ *Ibid.*, p. 25.

1 of main telephone lines by providing better incentives to market participants.¹⁹

2

3 In summary, both economic theory and the empirical literature suggest that the
4 companies' revised plans—by setting residential rates at more economically efficient
5 levels—would likely make the residential local exchange marketplace more attractive to
6 actual and potential competitors.

7

8 **Q. BUT ISN'T IT THE CASE THAT CLECS ALREADY HAVE ENOUGH**
9 **INCENTIVES TO SERVE LUCRATIVE RESIDENTIAL CUSTOMERS?**

10 A. Yes, it is probably the case that CLECs have enough incentive to serve a subset of
11 residential customers, namely those customers that are very profitable either because the
12 cost of serving them is especially low or because their volumes are unusually high. But
13 the promise of the Tele-Competition Act is to ensure that competition for residential
14 customers is as broad and diffuse as is economically feasible, and by better aligning the
15 prices of residential basic local services with their underlying costs, a broader base of
16 residential customers will obtain the benefits of competition.

17

18 **Q. § 364.164 (1) (b) PROVIDES THAT THE COMPANIES' PLANS CONSIDER THE**
19 **EFFECT ON ENHANCED MARKET ENTRY. WILL THE COMPANIES'**
20 **REVISED PLANS MEET THIS PROVISION?**

21 A. Yes, the companies' revised plans will induce enhanced market entry. Above, I have
22 discussed how the revised plans would likely create a more attractive competitive local

¹⁹ See, Agustin J. Ros and Aniruddha Banerjee, "Telecommunications Privatization and Tariff Rebalancing: Evidence from Latin America," *Telecommunications Policy*, 24 (2000) 233-252.

1 exchange market for the benefit of residential consumers. This is an example of how the
2 revised plans will induce enhanced market entry.

3
4 In general, the companies' revised plans will provide for improved entry signals into the
5 local exchange market by diminishing distorted price signals that may encourage
6 uneconomic entry into the overpriced markets. Prices that are free of distortions will lead
7 to several economically-efficient outcomes known as allocative, technical and dynamic
8 efficiencies. First, efficient pricing assumes that the marginal cost that society incurs to
9 produce goods and services reflects the value that consumers place on the good or service
10 consumed, (allocative efficiency). Second, optimal signals are provided to firms in the
11 industry (e.g., whether to increase production or exit the industry) and to potential entrants
12 contemplating entering the market. This ensures that it is the lowest cost firms that stay in
13 the market and provide goods and services. In this way the use of society's scarce
14 resources is minimized (technical efficiency). Third, prices that adequately cover costs
15 ensure that appropriate incentives exist for improvement in technology, increased research
16 and development and higher quality goods and services (dynamic efficiency).

17

18 **Q. UNDER WHAT CONDITIONS CAN IT BE SAID THAT PRICES ARE FREE OF**
19 **DISTORTION, AND ARE THE COMPANIES' CURRENT PRICES FOR BASIC**
20 **LOCAL SERVICES FREE OF DISTORTIONS?**

21 A. Prices are free of distortion when: (1) they recover at least the forward-looking
22 incremental cost of production and (2) for multi-product firms, markups above
23 incremental costs take into account demand characteristics in the market, subject, of
24 course, to the need for the firm to meet competition. As described in the companies' cost
25 testimonies, the companies' prices for basic local residential services are not recovering

1 the forward-looking direct cost of production. As such, prices for these services do not
2 meet the economic criterion that prices should at a minimum recover the forward-looking
3 direct cost of production.

4

5 By adopting the companies' revised plans, however, the Commission will be reducing
6 significantly the distortions in the price of intrastate access and residential basic local
7 services and achieving the economically efficient outcomes described above.

8

9 **IV. OTHER ECONOMIC BENEFITS FROM THE COMPANIES'**
10 **REVISED PLANS**

11

12 **Q. ARE THERE OTHER ECONOMIC BENEFITS THAT WILL LIKELY ARISE**
13 **FROM THE COMPANIES' REVISED REBALANCING PROPOSAL?**

14 A. Yes, there are other economic benefits that will likely arise from the companies' revised
15 rebalancing proposals. Both economic theory and empirical research suggest that rate
16 rebalancing will likely increase economic activity in Florida as increased competition
17 brings benefits to Florida consumers of telecommunications services.

18

19 **Q. WOULD YOU PLEASE DESCRIBE WHY ECONOMIC THEORY SUGGESTS**
20 **THAT RATE REBALANCING WILL INCREASE ECONOMIC ACTIVITY IN**
21 **FLORIDA?**

22 A. Rate rebalancing consists of increasing the prices of services that are priced below
23 forward-looking direct costs and reducing the prices of services that are priced
24 significantly above forward-looking direct costs. As mentioned earlier in my testimony,
25 the history of telecommunications rate design is such that residential basic local prices

1 were set low and usage services (such as toll and intrastate access services) were set high.

2

3 However, economic theory teaches that economic efficiency (and overall consumer
4 welfare) is at its highest level when prices of goods and services in an economy are set at
5 forward-looking direct cost. Of course, in industries where there are significant fixed
6 costs—that give rise to economies of scale—and in multi-product firms where there are
7 significant amounts of shared and common costs, pricing services at forward-looking
8 direct cost does not permit the firm to earn sufficient revenues to recover all its costs.
9 Under such conditions, markups above forward-looking direct costs are required.
10 Specifically, as competition develops, those services that are more price elastic will likely
11 receive a proportionately lower markup above cost than those services that are more price
12 inelastic.

13

14 **Q. PLEASE DESCRIBE HOW REBALANCING RESULTS IN INCREASED**
15 **ECONOMIC ACTIVITY IN FLORIDA?**

16 A. The companies' revised plans will lower intrastate access prices, which will in turn result
17 in lower intrastate toll prices, as required by the Tele-Competition Act. As a result of the
18 reduction in intrastate toll prices, Florida consumers will use more toll services. This will
19 create value for them that they are not now receiving. This, in turn, will reflect an
20 increase in economic activity in Florida. In addition, and of more direct importance to this
21 proceeding, more cost reflective prices for local service will send signals to competitors
22 that will more efficiently guide their investment decisions, and in all likelihood, increase
23 their investment beyond what it is in the face of today's artificially low prices. Thus,
24 rebalancing will generate significant gains in economic activity in Florida. It is important
25 to stress the point that demand for access to the network by consumers depends not only

1 on the price of network access but it also depends on the value that consumers obtain
2 (consumers' surplus) from using the network. While higher network access prices may, in
3 theory, decrease the quantity of access consumed, the concomitant decrease in long
4 distance price will increase the quantity of access consumed. Empirical evidence suggests
5 that, in net, we may well find that rebalancing leads to more consumers subscribing to the
6 network.²⁰

7

8 **Q. IS THERE EMPIRICAL EVIDENCE THAT QUANTIFIES THE AMOUNT OF**
9 **ECONOMIC BENEFIT THAT A REBALANCING PLAN CAN GENERATE?**

10 A. Yes, there is empirical support. There have been several studies that have examined the
11 welfare gains arising from rate rebalancing. One of the first studies found that, for the
12 U.S. as a whole, the loss from overpricing long distance service to business and residential
13 consumers in 1983 was around \$10 billion, a finding that was confirmed in subsequent
14 research.²¹ More recent research confirms the significant gains in economic welfare that
15 can be achieved from more economically rational prices. For example, a 2000 study by
16 Robert Crandall and Leonard Waverman (a NERA colleague) found the total cost of the
17 current rate design—i.e., lower basic local prices and higher long distance prices—to be
18 anywhere between \$2.5 to \$7.0 billion per year, depending on the assumptions made.²²

19

²⁰ See, Hausman, J., T. Tardiff, and A. Belinfante, "The Effects of the Breakup of AT&T on Telephone Penetration in the United States," *The American Economic Review*, Vol. 83, May 1993, pp. 178-184.

²¹ See, John T. Wenders and Bruce L. Egan, "The Implications of Economic Efficiency for U.S. Telecommunications Policy." *Telecommunications Policy* 10 (1986): 33-40 and Lewis Perl, "Social Welfare and Distributional Consequences of Cost-Based Telephone Pricing." Paper presented at the Thirteenth Annual Telecommunications Policy Research Conference, Airlie, Va. April 23, 1985.

²² See, Robert Crandall and Leonard Waverman, *Who Pays for Universal Service?: When Telephone Subsidies Become Transparent*, Brookings Institute, (2000), p. 119.

1 **V. COST ISSUES**

2

3 **Q. WHAT IS THE CORRECT COST CONCEPT TO USE FOR DETERMINING**
4 **WHETHER A SERVICE IS RECEIVING AN ECONOMIC SUBSIDY?**

5 A. From an economic perspective, use of forward-looking direct costs (economic costs as
6 opposed to embedded or historical costs) is the proper basis for determining whether a
7 specific service is in receipt of an economic subsidy. The embedded cost or historical cost
8 of an activity is a record of the costs a firm attributes to the pursuit of its activity in a
9 given (past) accounting period. That cost reflects what the firm actually paid for capital
10 equipment,²³ its actual costs of operating and maintaining that equipment, and other costs
11 incurred in operating the enterprise. By contrast, the economic cost of an activity is the
12 actual forward-looking cost of accomplishing that activity in an efficient manner. In
13 contrast to embedded costs, forward-looking costs are those associated with present and
14 future uses of the firm's (or society's) resources. Only these forward-looking costs are
15 relevant for making present and future production and investment decisions, for placing
16 resources in alternative uses, and for setting efficient prices for the services to be provided
17 presently or in the future.

18

19 According to the evidence presented by the companies, their residential basic local rates
20 are below forward-looking direct costs and I conclude, therefore, that those rates are in
21 receipt of an economic subsidy.

22

²³ Embedded costs also include the annual depreciation expenses associated with the stock of equipment that (1) was purchased in the current and previous years and (2) is still in use.

1 Q. THE COMPANIES' REVISED PLANS ARE BASED UPON THE FACT THAT
2 THE LOCAL LOOP IS NOT A SHARED OR COMMON COST AND THAT ITS
3 COST IS CAUSED SIMPLY BY PROVIDING CUSTOMERS ACCESS TO THE
4 TELEPHONE SYSTEM AND CANNOT APPROPRIATELY BE SPREAD
5 AMONG THE REMAINING TELEPHONE SERVICES. DOES THE FLORIDA
6 COMMISSION AGREE WITH THIS APPROACH REGARDING THE LOCAL
7 LOOP?

8 A. Yes, it does. In a report to the Florida Legislature in 1999, the Commission explicitly
9 rejected the notion that the cost of the loop should be recovered from non basic local
10 telecommunications service.²⁴ In that report, the Commission stated:

11 Is the cost of local loop facilities properly attributable to the provision of basic
12 local telecommunications service? By definition, yes. Section 364.02(2),
13 Florida Statutes, defines "basic local telecommunications service as"

14 Voice grade, flat-rate residential and flat-rate single-line business local
15 exchange services which provide dial tone, local usage necessary to
16 place unlimited calls within a local exchange area, dual tone multi-
17 frequency dialing, and access to the following emergency services such
18 as "911," all locally available interexchange companies, directory
19 assistance, operator services, relay services, and an alphabetical
20 directory listing.

21

²⁴ See, "Report of the Florida Public Service Commission on the Relationship Among the Costs and Charges Associated with Providing Basic Local Service, Intrastate Access, and Other Services Provided by Local Exchange Companies, in Compliance with Chapter 98-277, Section 2(1), Laws of Florida," Florida Public Service Commission Tallahassee, Florida February 15, 1999.

1 Given such an identification of the cost object to be studied, the principle of
2 cost causation leads one to the unavoidable conclusion that the decision to
3 have local service leads to the incurrence of loop costs.²⁵

4

5 **VI. UNIVERSAL SERVICE WOULD NOT BE PUT AT RISK AS A**
6 **RESULT OF THE COMPANIES' REVISED PLANS**

7

8 **Q. SHOULD THE COMMISSION BE CONCERNED ABOUT UNIVERSAL**
9 **SERVICE?**

10 A. While it is true that, in theory, as the price of basic local service increases, some
11 consumers may decide the new price is above the value he or she places on the service—
12 and may, as a result, decide to do without telephone service—I do not believe that, in
13 practice, this would occur, or occur to such an extent as to jeopardize universal service in
14 Florida. There are several reasons why I believe this is the case.

15

16 First, although low-income subscribers may be more sensitive to price increases than are
17 middle and higher income users, the Tele-Competition Act does two things to help low
18 income consumers. It provides that, in the event of an increase in residential basic local
19 service prices, low-income consumers who are Lifeline customers will be exempted from
20 the price increase; and, it expands the number of Lifeline-eligible customers to 125
21 percent of the federal poverty level. These steps should go far to address any problems of
22 affordability.

23

²⁵ *Ibid*, at 51.

1 Second, the price elasticity of demand for access to the network is quite low, meaning that
2 the vast majority of consumers will continue to subscribe. Specifically, the price elasticity
3 of demand measures the percentage impact on demand given a percentage change in price.
4 Previous research has demonstrated that customers generally do not disconnect their
5 phone service when prices for basic local service increase.²⁶

6
7 Third, and very importantly, in addition to its own price, the demand for residential basic
8 local service is determined by the amount of value consumers obtain from using the
9 services produced by the network, i.e., local calling, intraLATA toll, interLATA toll,
10 vertical services and newer services such as broadband Internet access. As prices for
11 these services decrease over time due to competitive pressure and technological
12 innovation, the value that consumers place on having access to the network increases and
13 so, therefore, does their demand to stay on the network.²⁷ The companies' revised plans
14 call for rate increases phased in over a two year period and to the extent that prices for
15 complementary goods decrease so will consumers' desire to remain on the network
16 increase. This helps reduce, or may even offset, the negative effect of the price increase.

17
18 Finally, as discussed above, less distorted prices should provide better incentives for
19 competitors to compete for residential consumers. Competition brings with it improved
20 quality, different selection of goods and services bundled together in a way that customers
21 find attractive, and lower prices. These factors provide additional reasons why during the

²⁶ See, Lester D. Taylor, (1994), *op. cit.*

²⁷ Hausman, J., T. Tardiff, and A. Belinfante, "The Effects of the Breakup of AT&T on Telephone Penetration in the United States," *The American Economic Review*, Vol. 83, May 1993, pp. 178-184.

1 phase-in period, customers will likely place increased value on subscribing to the network,
2 thus mitigating the effects of any local rate increase.

3

4 To the extent the Florida Commission is concerned with the few remaining users who may
5 decide to drop off the network it is also important to be aware that alternatives to the fixed
6 network are growing and at least some customers may be turning to alternative means of
7 meeting their communications needs. For example, the extraordinary growth of wireless
8 service, driven by lower wireless prices and pricing plans that include a “bucket” of
9 minutes provides customers with more meaningful opportunities to use wireless service as
10 a substitute to wireline service.

11

12 **Q. SHOULD THE COMMISSION BE CONCERNED IF CUSTOMERS DROP OFF**
13 **THE FIXED NETWORK BUT INSTEAD RELY PRIMARILY ON OTHER**
14 **FORMS OF ACCESS?**

15 A. No. An important goal for policymakers has been to ensure that as many consumers as
16 possible have access to the public switched telecommunications network, irrespective of
17 how that access is obtained. When a customer drops off the fixed-line network and
18 accesses the public network via wireless access, this is simply a substitution effect caused
19 by the customer choosing between fixed and wireless access. This is not a universal
20 service concern for policymakers.

21

22 **Q. DR. GORDON, HAVE OTHER STATES IMPLEMENTED RATE**
23 **REBALANCING?**

24 A. Yes, there are other states that have implemented rate rebalancing including California,
25 Illinois, Ohio, and in Massachusetts where I served as Chairman. Even in Maine, where

1 by statute basic residential services are to be set as low as possible and where I also served
2 as Chairman, they have recently approved a rebalancing plan.

3

4 **Q. WOULD YOU PLEASE DESCRIBE THE RATE REBALANCING PROCESS IN**
5 **MASSACHUSETTS?**

6 A. The process for changing prices in Massachusetts began before I became Chairman of the
7 Massachusetts Commission and continued during my tenure. In Massachusetts,
8 residential fixed monthly charges were increased significantly, with offsetting decreases in
9 business, toll, and carrier access prices. The Massachusetts Commission early on after
10 divestiture recognized the problems that historic pricing policies were creating, as other
11 (especially institutional) barriers to market entry were being eliminated, and thus ordered
12 a change in price structure:

13 "properly defined incremental costs should be used as the primary basis for
14 pricing all services, including local exchange service ...to the extent that
15 current rates do not reflect an appropriate allocation of costs, the [MDPU] will,
16 consistent with the need to avoid major discontinuities in rate levels, move
17 toward that goal." IntraLATA Competition, D.P.U. 1731 (1985), p. 36-38.

18

19 "Traditionally, the pricing of telephone service was based on a method
20 whereby residential monthly exchange rates were priced below cost in order to
21 promote universal service; and long-distance, toll, and business rates were
22 priced above cost in order to subsidize residential exchange rates. While this
23 system succeeded in serving a social purpose, it was a pricing scheme not
24 conducive to the development of a fully-competitive market, in which the
25 benefits associated with competition would be realized by all customers."

1 NET, D.P.U. 93-125 (1994), pp. 10-11.

2

3 In Massachusetts, moving prices more in line with incremental costs required a significant
4 shift in revenue recovery from usage-based prices, such as intraLATA toll and intrastate
5 carrier access, to fixed monthly prices for all classes of customers. In addition, because
6 the MDPU found that there were no significant cost differences in serving different
7 classes of customers, the price-rebalancing process also entailed a further shift in revenue
8 recovery from business customers to residential customers. Of course, the necessary
9 changes were not made overnight. The MDPU established a series of annual, revenue-
10 neutral, price-rebalancing investigations in order to achieve its goal over time.

11

12 When the Massachusetts price-rebalancing process ended in January of 1994 (with the
13 adoption of a price cap plan), the price for basic residential dial-tone service (1MR) had
14 risen from about \$3.00 per month in 1990 to \$9.91 per month in 1994 (net of the SLC).²⁸
15 Comparable increases also occurred for residential flat-rate service (1FR), which was the
16 most popular service in Massachusetts, at that time. Flat rate residential prices had ranged
17 from \$9.95 in rural areas to \$12.38 in urban areas. The rebalancing process moved flat
18 rate residential prices to \$16.85 state wide. During this period, the average increase for
19 residential consumers was \$2.18 per year over four years and, according to the DTE,
20 record evidence shows virtually no impact on residential telephone subscriber
21 penetration.²⁹ Because the price-rebalancings were revenue-neutral, these increases were

²⁸ I was Chairman of the MDPU for the last of these annual investigations.

²⁹ See, "Re Verizon New England, Inc. dba Verizon Massachusetts D.T.E. 01-31-Phase II," *Public Utilities Reports – 223 PUR4th*, p. 397.

1 completely offset by decreases in prices for other services, notably residential and
2 business intraLATA toll and carrier switched access.

3

4 Massachusetts was one of the first states to open toll and local markets to competitive
5 entry, and the price rebalancing helped to lessen opportunities for uneconomic bypass and
6 thus promoted the development of an efficient competitive process.

7

8 More recently, Massachusetts has continued to better align prices with their underlying
9 costs by reducing switched access and increasing residential dial-tone rates. Specifically,
10 the DTE authorized the ILEC to implement a one-time increase of \$2.44 to its residential
11 dial-tone line charge. In commenting on its decision, the DTE stated:

12 Moreover, the department finds that with the \$2.44 increase in the dial-tone
13 line charge, competitive local exchange carriers (CLECs) can profitably enter
14 and serve the residential telephone market in Massachusetts.³⁰

15

16 The DTE concluded that a \$2.44 increase will not harm the Department's universal
17 service goals, based on similarity to the several, annual \$2.18 increase in the early 1990s
18 rebalancing plans and comparable increases in several other states and in the Federal
19 subscriber line charge since 2000. For example, the Maine PUC approved a \$1.78
20 increase in Verizon's basic monthly per line rate in May 2001 and the New York Public
21 Service Commission authorized a two-year Incentive Plan which permitted an increase of
22 \$1.85 on March 1, 2002 and another \$0.65 on March 1, 2003 for a total increase of \$2.50
23 in the space of a year. The FCC's Federal subscriber line charge has increase from \$4.35

³⁰ *Ibid*, p. 361.

1 in July 2000 to \$6.50 in July 2003.

2

3 **Q. PLEASE DISCUSS MAINE'S EXPERIENCE WITH RATE REBALANCING?**

4 A. Significant rate rebalancing has been achieved in Maine in recent years, with no
5 noticeable impact on telephone subscribership levels. In 1997, the Maine legislature
6 (M.R.S.A. 35-A, §7101-B) directed the Maine Public Utility Commission to establish,
7 notwithstanding any other provision of state law, intrastate access rates that are less than
8 or equal to interstate access rates established by the FCC (*i.e.*, parity with interstate access
9 rates) by May 30, 1999. At the time, Bell Atlantic's intrastate access rates were \$0.26 per
10 minute, significantly higher than its then-current Federal interstate access rate of about
11 \$0.07 per minute.

12

13 Subsequently, on March 17, 1998, the Commission approved an Order (Docket No. 94-
14 123 reopened) that approved a stipulation between Bell Atlantic-Maine (now known as
15 Verizon-Maine) and a group of intervenors, including the Commission's Advocacy Staff
16 and the Public Advocate. This stipulation allowed Bell Atlantic-Maine to increase its
17 basic local exchange rates by a total of \$3.50 by May 30, 1999, with steps of \$1.50 in
18 1998 and \$2.00 in 1999. This was followed by another increase of \$1.78 in 2000.

19

20 Maine continues to have the highest telephone penetration rate in the country—about 98
21 percent of Maine's households have telephone service.³¹ In addition, lower intrastate toll
22 rates have benefited some customer classes, especially those customers in rural areas with
23 relatively small toll-free calling areas.

³¹ MPUC Annual Report 2002, pp. 43.

1

2 **Q. WHAT OTHER STATE EXPERIENCES DO YOU BELIEVE ARE RELEVANT?**

3 A. In California in 1994, the Commission approved a rebalancing plan for GTE and Pacific
4 Bell. GTE's residential rates immediately went from \$9.75 to \$17.25 while Pacific's
5 residential rates went from \$8.35 to \$11.25.³² Recently, as part of a rebalancing plan for
6 Sprint's local telephone company in Ohio where intrastate access fees were lowered to
7 mirror Federal charges, the Commission approved the creation of an end user charge of
8 \$4.10 for residential customers and \$6.00 for single-line business.³³

9

10 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

11 A. Yes.

³² See, Decision 94-09-065, *et. al.*, September 15, 1994.

³³ See, The Public Utilities Commission of Ohio, Case No. 00-127-TP-COI and 01-1266-TP-UNC, June 28, 2001.

1 BY MR. FONS:

2 Q And, Dr. Gordon, did you also cause to be prepared
3 and be prefiled in this proceeding rebuttal testimony
4 consisting of 22 pages of questions and answers dated November
5 the 19th, 2003?

6 A Yes.

7 Q And do you have any corrections or changes to that
8 rebuttal testimony?

9 A No.

10 Q And if I were to ask you the same questions today as
11 were put to you in your prepared rebuttal testimony, would your
12 answers be the same today?

13 A Yes.

14 MR. FONS: Madam Chairman, I would ask that Dr.
15 Gordon's rebuttal testimony consisting of 22 pages be inserted
16 into the record as though read.

17 CHAIRMAN JABER: The prefiled rebuttal testimony of
18 Dr. Kenneth Gordon will be inserted into the record as though
19 read.

20 BY MR. FONS:

21 Q And, Dr. Gordon, did you have attached to that
22 rebuttal testimony an exhibit identified as Exhibit I?

23 A I'll have to refresh myself. Yes, I have it.

24 Q And was that exhibit, does that consist of one page
25 and its title, "CLEC Margin Comparisons"?

1 A Correct.

2 Q And was this exhibit prepared by you or under your
3 direction and control?

4 A It was.

5 Q Do you have any changes to that exhibit?

6 A No.

7 Q And I don't remember if I asked you, do you have any
8 changes to your prefiled rebuttal testimony? I think you said
9 you had no changes.

10 A I think I said no.

11 MR. FONS: And can we have marked as the next exhibit
12 Exhibit 46?

13 CHAIRMAN JABER: Exhibit I will be identified as
14 hearing Exhibit 46.

15 (Exhibit 46 marked for identification.)
16
17
18
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24
25

**REBUTTAL TESTIMONY OF DR.
KENNETH GORDON**

1 **REBUTTAL TESTIMONY OF DR. KENNETH GORDON**

2

3 **I. PURPOSE & SUMMARY OF CONCLUSIONS**

4

5 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

6 A. My name is Dr. Kenneth Gordon. My business address is One Main Street, Cambridge,
7 Massachusetts 02142.

8

9 **Q. ARE YOU THE SAME DR. GORDON THAT FILED TESTIMONY IN THIS**
10 **PROCEEDING ON SEPTEMBER 30, 2003?**

11 A. Yes, I am.

12

13 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

14 A. Verizon Florida Inc., BellSouth Telecommunications, Inc., and Sprint-Florida Inc., (“the
15 companies”) have asked me to review the direct testimonies of Dr. David J. Gabel and Dr.
16 Mark N. Cooper and to provide rebuttal testimony.

17

18 **Q. WHAT ARE YOUR GENERAL OBSERVATIONS FROM REVIEWING THESE**
19 **WITNESSES TESTIMONIES?**

20 A. These witnesses share an outdated view of the telecommunications market, one that sees
21 incumbent local exchange carriers (“ILECs”) as monopoly providers that face little
22 competition and that are constrained only by the fist of regulators. These witnesses
23 ignore the importance of the type of pricing reform to better reflect industry conditions
24 being proposed by the companies and advance old arguments using the same type of
25 pricing policy (e.g. residual telephone pricing) that prevailed in the industry at the time

**REBUTTAL TESTIMONY OF DR.
KENNETH GORDON**

- 2 -

1 when there was only one provider of telecommunication services that operated in an
2 exclusive franchise territory.

3 These views and positions are simply inconsistent with the current market environment.
4 ILECs operate in increasingly competitive markets where they are not the only providers
5 of telecommunication services. CLECs are able to provide telecommunications services
6 without regulatory intervention and competitors are using alternative technologies to
7 provide traditional telephony service—be it through coaxial cable, wireless or increasingly
8 Internet-based voice services. Nevertheless, these competitors face a serious problem in
9 competing with firms whose prices are set at artificially low levels. In spite of this, many
10 customers have choices and are increasingly exercising those choices.

11 The companies' rebalancing proposals recognize this new environment, as does the
12 TeleCompetition and Innovation Act of 2003 ("The Act") passed by the Florida
13 Legislature. Competition can only succeed and be as broad based as economically
14 feasible if the old vestiges of telecommunications pricing are done away with.
15 Specifically, the historic policy of pricing residential network access as low as possible
16 (residual telephone pricing) and of supporting companies through a complex set of
17 implicit support mechanisms is reducing the amount of competition for residential
18 consumers and is providing reduced incentives for CLECs to enter the market and serve
19 these customers.

20 The opinions of CLECs in this proceeding are particularly revealing since they are putting
21 their shareholders' money at risk by providing competitive telecommunications services
22 in Florida. They are in the best position to state whether the companies' plan would have
23 any impact on their incentive to enter new markets. Contrary to the position of Dr. Gabel,
24 Knology, a competitive local and long distance telephone company, believes the

1 companies' plan should be granted because it will "enhance the competitive choices
2 available to Florida citizens."¹ AT&T and its witnesses make the same point.²

3

4 **Q. WOULD YOU PLEASE SUMMARIZE YOUR MORE SPECIFIC**
5 **DISAGREEMENTS WITH DR. GABEL AND DR. COOPER?**

6 A. Yes. There are two major disagreements that I have with these witnesses. The first deals
7 with their position or implication that basic residential service is not receiving a subsidy;
8 while the second deals with the argument that the companies' plan will not result in a
9 more attractive market for the benefit of residential consumers.

10 Both positions are erroneous. Dr. Cooper uses the same old argument that he has
11 previously used in Florida, that is the cost of the local loop is a common cost of providing
12 telecommunications services and the pricing of other services, such as intraLATA toll or
13 exchange access services, should be set so as to recover a portion of loop costs. I describe
14 below why this is economically incorrect and remind the Commission of its own report
15 where it specifically (and correctly) rejected this way of viewing the costs of the local
16 loop.³

17 Dr. Gabel uses a somewhat different approach to achieve his goal of removing many of
18 the loop costs from the direct cost of residential network access. As described below, Dr.

¹ Testimony of Felix L. Boccucci, Jr. on Behalf of Knology of Florida, Inc. p.3.

² Direct Testimony of John W. Mayo on Behalf of AT&T Communications and MCI Worldcom Communications, October 31, 2003, p. 12.

³ See, "Report of the Florida Public Service Commission on the Relationship Among the Costs and Charges Associated with Providing Basic Local Service, Intrastate Access, and Other Services Provided by Local Exchange Companies, in Compliance with Chapter 98-277, Section 2(1), Laws of Florida," Florida Public Service Commission Tallahassee, Florida February 15, 1999.

1 Gabel begins with the economic definition of TSLRIC but then misapplies it to basic
2 residential service. Dr. Gabel's approach incorrectly defines the service in question by the
3 nature of the customer rather than correctly defining it according to the nature of its
4 production. The service that is being "costed" for purposes of this proceeding is network
5 access—i.e., the service that consists of all the costs associated with providing a customer
6 with dial tone service, irrespective of the type of customer. Network access most certainly
7 has a direct cost associated with it and that direct cost appropriately includes all the costs
8 of achieving it, including the support structures mentioned in Dr. Gabel's testimony—i.e.,
9 telephone poles, trenches, ducts, conduits, etc. They are all direct costs of network access.

10 The second major disagreement I have with Dr. Gabel is his contention that the
11 rebalancing plans will not enhance market entry. I have already mentioned that perhaps
12 the most important parties in this proceeding that can attest to what the plans are likely to
13 mean for actual and potential market entrants are the competitors who believe that the
14 companies' plans to rebalance rates will lower an important barrier to market entry.

15 Moreover, I do not think it is necessary for this Commission to resolve the debate about
16 what changes in telecommunications regulation will do more for local competition,
17 reforming pricing as the companies' plans do, or other actions that Dr. Gabel seems to
18 suggest—such as reducing UNE prices. The Legislature specifically mentioned the role
19 of retail pricing as a tool to enhance market entry and that is the tool that the Commission
20 should examine irrespective of whether other reforms might also have an impact on
21 residential competition.

22 Finally, I also discuss why it is perfectly consistent to say that the companies' plans will
23 enhance market entry while at the same time acknowledging that the investment decision
24 of a firm is based on comparing total revenues and total costs. Holding all other factors

1 constant, a rebalancing plan that better aligns prices with costs and lowers the support
2 needed from other services will reduce the risk of providing telecommunications service
3 and this will make the cash flow equation more positive for CLECs interested in targeting
4 residential consumers.

5

6 **II. THE LOCAL LOOP IS NOT A SHARED COST OF RESIDENTIAL**
7 **BASIC SERVICE OR A COMMON COST OF**
8 **TELECOMMUNICATIONS SERVICES**
9

10 **Q. DR. GABEL (SECTION 3) ARGUES THAT THE COMPANIES' POSITION**
11 **THAT THERE IS A SUBSIDY IN THE PROVISION OF LOCAL SERVICE IS**
12 **FLAWED BECAUSE THE COMPANIES INCORRECTLY USE TELRIC AS THE**
13 **COST STANDARD AND ASSUME THAT THE ENTIRE COST OF THE LOCAL**
14 **LOOP IS A DIRECT COST OF BASIC RESIDENTIAL SERVICE. DR. COOPER**
15 **(AT 3) ARGUES THAT THE LOOP IS A COMMON COST OF BASIC**
16 **RESIDENTIAL LOCAL SERVICE. HOW DO YOU RESPOND?**

17 A. The intervenors are incorrect. Economic theory and this Commission's own position
18 contradict their position that the local loop is anything other than a direct cost of providing
19 network access to consumers, irrespective of whether that customer is a residential or
20 business customer. Once it is established that the local loop is not a shared cost of basic
21 service it becomes evident that basic residential services are not recovering fully their
22 forward-looking direct costs.

23

1 Q. HAS THIS COMMISSION STATED PREVIOUSLY THAT THE LOCAL LOOP
2 IS NOT A SHARED COST OF BASIC SERVICE AND THAT ALL THE COSTS
3 ASSOCIATED WITH PROVIDING BASIC SERVICE SHOULD BE
4 RECOVERED FROM BASIC SERVICE?

5 A. Yes. As stated in my Amended Direct Testimony (at 36), in a report to the Florida
6 Legislature in 1999, the Commission explicitly rejected the notion that the cost of the loop
7 should be recovered from non-basic local telecommunications service.⁴ In that report, the
8 Commission stated:

9 Is the cost of local loop facilities properly attributable to the provision of basic
10 local telecommunications service? By definition, yes. Section 364.02(2),
11 Florida Statutes, defines “basic local telecommunications service as”

12 Voice grade, flat-rate residential and flat-rate single-line business local
13 exchange services which provide dial tone, local usage necessary to
14 place unlimited calls within a local exchange area, dual tone multi-
15 frequency dialing, and access to the following emergency services such
16 as “911,” all locally available interexchange companies, directory
17 assistance, operator services, relay services, and an alphabetical
18 directory listing.

19

⁴ See, “Report of the Florida Public Service Commission on the Relationship Among the Costs and Charges Associated with Providing Basic Local Service, Intrastate Access, and Other Services Provided by Local Exchange Companies, in Compliance with Chapter 98-277, Section 2(1), Laws of Florida,” Florida Public Service Commission Tallahassee, Florida February 15, 1999.

1 Given such an identification of the cost object to be studied, the principle of cost causation
2 leads one to the unavoidable conclusion that the decision to have local service leads to the
3 incurrence of loop costs.⁵

4

5 **Q. BUT DR. GABEL (AT 30) STATES THAT HIS APPROACH IS CONSISTENT**
6 **WITH THE COMMISSION'S DETERMINATION BECAUSE "WHEN THE**
7 **COST OF THE RESIDENTIAL BLTS LOOP IS ESTIMATED, COSTS SHARED**
8 **WITH OTHER SERVICES, SUCH AS SPECIAL ACCESS, DATA AND**
9 **BUSINESS BLTS, SHARED COSTS SHOULD NOT BE TREATED AS A DIRECT**
10 **COST." HOW DO YOU RESPOND?**

11 A. Dr. Gabel argues that the companies have performed their cost studies for basic residential
12 incorrectly because they consider the costs of equipment such as ducts, trenches and poles
13 as incremental to basic service when in reality in many instances they are shared between
14 residential, business, DSL and ISDN. Dr. Gabel begins with the economic definition of
15 TSLRIC but then misapplies it to basic residential service. He states that TSLRIC is
16 determined by examining the change in the total cost of producing telecommunications
17 when a service is added (or discontinued). He further states that if basic residential
18 service were no longer provided the company would still need to incur the costs of ducts,
19 trenches, poles, cabinets, etc. From this he concludes that these costs would not be
20 included in a theoretically pure TSLRIC study.

⁵ *Ibid*, at 51.

1 The problem with Dr. Gabel's approach is that it is based on an unrealistic implementation
2 of TSLRIC. It is dependent on conducting a thought experiment that bears no
3 resemblance to what a real world incumbent telephone company would ever conceive of
4 doing. In order to be useful and relevant for business decision-making and for regulatory
5 purposes, TSLRIC calculations should be consistent with realistic business practices and
6 decisions. They should not be based on hypothetical situations that are unlikely to arise.

7 According to Dr. Gabel's TSLRIC interpretation, if the incumbent telephone company no
8 longer provides residential service—presumably because the residential population just
9 disappeared—this means that there would be little reason for businesses to locate to where
10 they are because there would be much less demand for business services. In fact, the
11 location of businesses is tied to the location of residential customers in a given serving
12 territory. It is then illogical to assume that if residential customers vanished there would
13 still be the same number of businesses or that they would locate in the same geographic
14 area.

15 Even if we were to carry this argument out a bit further, one would have to reach the
16 conclusion that the network built for serving only business customers would likely be
17 significantly different from the current network. Not only because business locations
18 would likely change but technology choices may change as well. But this invalidates the
19 thought experiment that is Dr. Gabel's basis for measuring TSLRIC. This is the case
20 because when one examines the impact of ceasing to offer residential service, the change
21 in total costs resulting from Gabel's thought experiment is not meaningful; the network
22 would have to be vastly re-engineered and re-configured.

23 Fortunately, it is not necessary to engage in this type of hypothetical analysis, as there is a
24 more straightforward and practical way of implementing the TSLRIC standard.

1

2 **Q. PLEASE DESCRIBE THE CORRECT WAY OF IMPLEMENTING THE TSLRIC**
3 **STANDARD IN THIS PROCEEDING?**

4 A. Dr. Gabel's approach incorrectly defines the service in question by the nature of the
5 customer rather than by the correct way of defining it according to the nature of its
6 production. The service that is being "costed" for purposes of this proceeding is network
7 access, i.e., the service that consists of all the costs associated with providing a customer
8 with dial tone service—irrespective of the type of customer. Network access most
9 certainly has a direct cost associated with it and that direct cost appropriately includes all
10 the costs of support structures mentioned in Dr. Gabel's testimony—i.e., telephone poles,
11 trenches, ducts, conduits, etc. They are direct costs of network access. In order to arrive
12 at the average direct cost of residential or business basic service one would take the direct
13 cost of network access and add other direct cost (if any) that are specific to business or
14 residential customers.

15

16 **Q. DR. COOPER (AT 17) ARGUES THAT THE LOOP IS A COMMON COST OF**
17 **TELECOMMUNICATIONS SERVICE. PLEASE EXPLAIN WHY YOU**
18 **BELIEVE THAT LOOP COSTS ARE NOT A COMMON OR SHARED COSTS?**

19 A. First, it is important to note that Dr. Cooper's arguments are the same arguments that he
20 has been making for years before this Commission. As I mentioned above, this
21 Commission has clearly rejected Dr. Cooper's view that the loop is a common cost of
22 telecommunications service.

1 Nevertheless, I will repeat, briefly, the arguments against Dr. Cooper's position. While it
2 is correct that the local loop is necessary in order to provide various telecommunications
3 services—such as network access (dialtone), intraLATA and interLATA usage and
4 vertical services—the cost of the local loop only varies in relation to changes in the
5 demand for network access and not in relation to changes in the demand for other
6 telecommunications services. Thus, it stands as a separate service. For example, when
7 the demand for toll services increase, a telephone company may need to augment capacity
8 on its switches and transmission routes but this would not increase the number of local
9 loops that it serves or the costs of operating those loops. Because of this fact, in a
10 forward-looking direct cost study for toll services—the investment and expenses
11 associated with the local loop would be excluded. On the other hand, when the demand
12 for network access increases (i.e., dialtone), a telephone company would need to incur the
13 costs associated with adding additional local loops, and these costs would be part of a
14 forward-looking direct cost study for network access.

15 This concept is best captured in the following quote by Alfred E. Kahn and William B.
16 Shew:

17 ...does subscriber access have a separate identifiable incremental cost
18 associated causally with providing it? The answer is, unquestionably, yes.
19 Connecting a customer to the network uses scarce resources, even if he or she
20 never uses the connection. The customer who subscribes to two access lines

1 imposes a greater cost on the system than the customer who subscribes to one,
2 even if they make the same number of calls, at the same times and places.⁶

3

4 **III. THE REBALANCING PLAN WILL PROVIDE INCREASED**
5 **INCENTIVES TO ENTER RESIDENTIAL MARKETS**

6

7 **Q. DR. GABEL SPENDS A GOOD PORTION OF HIS TESTIMONY (SECTION 3.3)**
8 **ARGUING THAT THE REBLANCING PLAN WILL NOT LIKELY STIMULATE**
9 **ENTRY. DR. COOPER (AT 12) MAKES A SIMILAR POINT. HOW DO YOU**
10 **RESPOND?**

11 A. I describe below some of the economic flaws in Dr. Gabel's arguments. I would like to
12 start off, however, by pointing to the testimony of CLECs in this proceeding which argue
13 —contrary to the view of Dr. Gabel or Dr. Cooper—that less support for basic
14 telecommunications service will in fact provide increased entry incentives. The
15 importance of these testimonies is that they present the viewpoint of the parties in this
16 proceeding who are actually putting shareholder money on the table.

17 For example, Knology of Florida, Inc. through the Testimony of Felix L. Boccucci, Jr.
18 believes that the companies' plans will have a positive impact on Knology's ability to
19 provide services in Florida. Mr. Boccucci states:

⁶ See, Alfred E. Kahn and William B. Shew, "Current Issues in Telecommunications Regulation: Pricing," *Yale Journal on Regulation*, Vol. 4(2) Spring 1987.

1 If these petitions are granted, Knology will be able to attract and deploy new
2 capital investment in Florida, thereby offering consumers a choice in facilities-
3 based providers for new and advanced high-tech services.⁷

4 Moreover, Mr. Boccucci states:

5 Knology believes that the petitions filed in these dockets should be granted,
6 because that decision will help to implement the policy underlying 364.14, and
7 it will enhance the competitive choices available to Florida citizens.⁸

8 In addition, Professor John W. Mayo on behalf of AT&T and MCI Worldcom
9 Communications states:

10 Higher prices relative to cost provide greater inducements for entry. In this
11 regard, the historical practice of residual pricing of local exchange services in
12 Florida has contributed to an environment that is relatively unattractive for
13 market entry.⁹

14

15 **Q. DR. GABEL (AT 34-35) DISPUTES YOUR CLAIM THAT “THE LEGISLATURE**
16 **HAS PERCIEVED THAT LOW RESIDENTIAL BASIC LOCAL PRICES HAVE**
17 **LED THE RESIDENTIAL LOCAL EXCHANGE MARKET TO BE LESS**
18 **ATTRACTIVE TO COMPETITORS THAN WOULD BE THE CASE WITH**

⁷ Testimony of Felix L. Boccucci, Jr. on Behalf of Knology of Florida, Inc. p.9.

⁸ *Id.* At 3.

⁹ Direct Testimony of John W. Mayo on Behalf of AT&T Communications and MCI Worldcom Communications, October 31, 2003, p. 12.

1 **MORE ECONOMICALLY RATIONAL RESIDENTIAL BASIC LOCAL**
2 **PRICES.”¹⁰ HOW DO YOU RESPOND?**

3 A. My assertion comes from a fair reading of the Act. While the Legislature was free to
4 consider all the reasons that may impact competition—including some of the reasons
5 mentioned by Dr. Gabel—it chose to include the following: “current support for basic
6 local telecommunications services that prevents the creation of a more attractive
7 competitive local exchange market for the benefit of residential customers.” This leads
8 me to conclude that the Legislature was persuaded that the current system of support for
9 basic local services is preventing the creation of a more attractive residential competitive
10 market as directly reflected in the Act.

11

12 **Q. DR. GABEL (AT 37-38) POINTS OUT THAT YOUR COMPARISON OF**
13 **FLORDIA RATES VS. THE NATIONAL AVERAGE IS MISLEADING AND IS**
14 **COMPARING APPLES TO ORANGES; AND THAT WHEN THE THREE**
15 **MAJOR CITIES IN FLORIDA (MIAMI, TAMPA AND WEST PALM BEACH)**
16 **ARE COMPARED TO THE NATIONAL AVERAGE, FLORIDA’S RATES ARE**
17 **NOT AS LOW AS YOU IMPLY. HOW DO YOU RESPOND?**

18 A. Even if Dr. Gabel’s methodology of comparing residential prices in Florida urban cities
19 with residential prices in U.S. urban cities is accepted, it still leads to the conclusion that
20 Florida prices are below the national average. For example, the average residential flat-
21 rate price for the 95 cities is \$23.38 while the same rates in West Palm Beach, Miami and

¹⁰ Direct Testimony of Dr. Kenneth Gordon on Behalf of Verizon Florida, Inc; BellSouth Telecommunications, Inc; and Sprint Florida Inc. Before the Florida Public Service Commission, August 27, 2003, pages 10-11.

1 Tampa are \$19.41, \$20.24 and \$22.45, respectively.¹¹ Every one of the Florida cities has
 2 rates below the national average. This is true even though, based on Dr. Gabel's own data
 3 (discussed below), it seems that Florida is a more costly state to serve than states such as
 4 Michigan and Illinois which have higher residential rates.

5

6 **Q. DR. GABEL DISPUTES YOUR SUGGESTION THAT THE DIFFERENCE IN**
 7 **ENTRY IS ATTRIBUTABLE TO THE UNREASONABLE RATE STRUCTURE**
 8 **IN FLORIDA. WHEN COMPARING ILLINOIS TO FLORIDA HE STATES, "IT**
 9 **CERTAINLY CAN NOT BE THE RATE OF RESIDENTIAL BLTS...THE PRICE**
 10 **OF RESIDENTIAL BLTS IS ESSENTIALLY THE SAME IN THE [SIC]**
 11 **ILLINOIS AND FLORIDA." HOW DO YOU RESPOND?**

12 A. Dr. Gabel is incorrect and his own data should have led him to the correct conclusion.
 13 Dr. Gabel's Table 1 compares Florida, Illinois and Michigan in terms of residential rates
 14 and UNE prices. From that he concludes that a more "plausible explanation for the
 15 comparative lack of CLEC entry in Florida vis-à-vis Illinois is that Florida's UNE prices
 16 are not as conducive to profitable CLEC entry into the market as the UNE prices found in
 17 Illinois."

18 What Dr. Gable fails to note, however, is that average costs in Illinois and Michigan are
 19 significantly lower than costs in Florida, according to the UNE prices set by the different
 20 Commissions. That is, in principle UNE prices reflect the underlying cost of providing

¹¹ FCC *Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service*, Table 1.1 July 2003, rates include Federal and State subscriber line charges, touch tone charge and taxes, 911 and other charges.

1 service and Dr. Gabel's data show that Florida is a more costly environment in which to
2 operate than the other states he chose to look at. According to Dr. Gabel's Table 1, costs
3 in the metro area are only \$2.59 in Illinois compared to \$9.77 in Florida and \$8.47 in
4 Michigan. Florida is the more costly state to serve yet Dr. Gabel's own data show that
5 prices in Florida are below those in Illinois and Michigan.

6 Table A in Exhibit I reproduces Dr. Gabel's Table and shows the margins available to
7 CLECs in Florida, Illinois and Michigan in the metro areas using UNE-L, assuming that
8 the remaining usage costs to provide service are comparable among the three states. As
9 can be seen, Table A indicates that—contrary to Dr. Gabel's assertion—the rate structure
10 in Florida can be impacting entry in Florida vis-à-vis other states such as Illinois and
11 Michigan. The margins available to CLECs in Florida in the metro areas are significantly
12 less than the margins available to CLECs in Illinois and Michigan due to a higher cost
13 structure in Florida and a lower rate structure.

14

15 **Q. DR. GABEL (AT 39-40) ARGUES THAT THE REASON THAT FLORIDA**
16 **RANKS LOWER THAN OTHER STATES IN LOCAL COMPETITION MAY**
17 **HAVE MORE TO DO WITH THE PRICING OF UNES AND UNE-P THAN**
18 **RETAIL RATES. HOW DO YOU RESPOND?**

19 A. Dr. Gabel has not conducted a study to demonstrate that the reduction of UNE-P or UNE-
20 Ls has an impact on local competition or that it has a greater impact than establishing
21 more efficient retail rate structure. The point is a red herring because even if it were to be
22 shown that reductions in UNEs favorably impact competitors that does not take away
23 from the fact that a more efficient rate structure can also spur competition. The

1 Legislature specifically identified the inefficient retail rate structure as a tool to use in
2 enhancing market entry. It did not—although it was free to do so—identify the issues
3 mentioned by Dr. Gabel. The issue of whether artificially low UNE-P has more or less of
4 an impact on enhancing market entry is not relevant to the Commission’s decision. It is
5 simply a red herring meant to distract from the issue at hand.

6 Moreover, relying too heavily on UNE-P to enhance market entry is bad public policy if
7 one ever hopes to achieve facilities based competition. Finally, such changes should not
8 be made at a time when the states are in the process of implementing the Triennial Review
9 Process, which may lead to the eventual elimination of unbundled switching.

10

11 **Q. DR. GABEL (AT 46) ARGUES THAT THE ENTRY DECISIONS OF CLECS ARE**
12 **BASED ON A COMPARISON OF TOTAL REVENUE FROM ALL SERVICES**
13 **WITH THE TOTAL TSLRIC OF ALL SERVICES AND THAT THE**
14 **COMPANIES’ APPROACH OF EXAMINING JUST THE COST AND REVENUE**
15 **OF BASIC SERVICE IS FLAWED. IS HE CORRECT?**

16 A. The correct entry decision for a firm deciding whether to enter a given market is an
17 examination of total costs and total revenues achievable from the investment and
18 calculation of the present value of the cash flows generated by the investment. However,
19 Dr. Gabel is incorrect in suggesting that the companies’ examination of one component of
20 that equation—the price of residential BLTS—is flawed or irrelevant. It is certainly not
21 irrelevant for the following reasons.

22 The entry decision of any firm is based on an evaluation of the net cash flows generated
23 by the investment; naturally this includes all costs and all revenues associated with the

1 investment. This is basic economics so in that sense it is hard to disagree with Dr. Gabel's
2 assertion. However, this has no bearing on the issue before the Commission in this
3 proceeding: whether removing support will make for a **more** attractive marketplace for
4 residential consumers. Holding all other factors constant, a rebalancing plan that better
5 aligns prices with costs and lowers the support needed from other services will reduce the
6 risk of providing telecommunications service and will make the cash flow equation more
7 positive for CLECs interested in targeting residential consumers. A cash flow analysis
8 requires a risk-adjusted cost of capital in order to discount cash flows over time and a
9 lower cost of capital makes investment projects more attractive compared to a higher cost
10 of capital.

11 Given that residential basic service is being supported by other services—as the
12 Legislature correctly noted—the support provided by those other services can continue
13 only to the extent that competitive alternatives are not sufficiently robust to drive those
14 service prices to their underlying costs. That is, if rates are not rebalanced and driven to
15 more cost-based levels it will be other service's revenues that are used to support
16 residential basic services. But those revenues are only an uncertain and temporary tool,
17 and as competition and other technologies advance, the ability to use them to support
18 basic residential services is likely to become limited. The risk of providing
19 telecommunications services is higher when a firm is dependent on support from other
20 services than when all prices are more reflective of underlying costs.

21 A rate structure that more adequately aligns prices with costs and reduces the amount of
22 support from other services should be more attractive to CLECs—as CLECs have attested
23 to in this proceeding. CLECs would not be dependent on the proliferation of other
24 services as a source to support basic residential services, thus lowering the risks of

1 providing telecommunications services. These factors would be reflected in a properly
2 conducted cash flow analysis.

3

4 **Q. DR. GABEL (AT 49) ARGUES THAT REBALANCING MAY NOT LEAD TO**
5 **ANY INCREASE IN CLEC INCENTIVE TO ENTER BECAUSE WHILE THE**
6 **PRICE OF ONE SERVICE INCREASES, THE PRICE OF OTHER SERVICES**
7 **WILL DECREASE. HOW DO YOU RESPOND?**

8 A. For the reason discussed above, even if there were no net change in revenue, the risk of
9 providing telecommunications services would decrease, thus positively impacting a CLEC
10 entry-decision model.

11 In addition, it is correct that in a cash flow analysis, a CLEC would want to include the
12 revenues and costs (profits) that are earned from selling intrastate access services and a
13 reduction in intrastate access rates would, holding other factors constant, lower the
14 attractiveness of the local market. However, the CLEC's intrastate access prices are not
15 directly affected by the companies' plan. CLEC intrastate access charges are not
16 regulated. In fact, terminating intrastate access services are the services whose prices are
17 being reduced by the companies' plan because originating rates are much lower. And it is
18 on the terminating side that CLECs arguably are less constrained by the incumbent
19 companies' terminating rates.

20 While the companies' intrastate access prices are being reduced significantly, no such
21 requirement exists for the CLECs. The CLECs will now be able to charge higher
22 residential basic local prices but not have a concomitant reduction in their intrastate access

1 prices. This will have a positive impact on CLECs' incentive to target residential
2 customers.

3

4 **Q. DR. GABEL (AT 43) CRITICIZES A PAPER THAT YOU CITE THAT SHOWED**
5 **A POSITIVE RELATION BETWEEN RATE REBALANCING AND**
6 **RESIDENTIAL COMPETITION. HOW DO YOU RESPOND?**

7 A. Dr. Gabel questions the paper because it does not use cost information but rather attempts
8 to rank the differences in the level of rate distortion by examining the ratio of business to
9 residential prices. As with any empirical study, when the ideal variable is not available (in
10 this instance cost information) proxies must be used, and the use of a ratio between
11 business and residential prices can reveal useful information about the extent that prices
12 are distorted in the different states. The history of residual residential telephone pricing in
13 the U.S. reveals that several sources have been used to support residential services and
14 that one of those sources has been business service. Businesses tend to be located closer
15 to the central office than residential customers yet business prices tend to be higher than
16 residential. In fact, in the paper the authors found that the average ratio of monthly
17 business to residential prices was approximately 2.89.¹² So the use of examining this ratio
18 across the different states to determine how the states rank in terms of one component of
19 the distorted rate structure is justified.

¹² Agustin J. Ros and Karl McDermott, "Are Residential Local Exchange Prices Too Low? Drives to Competition in the Local Exchange Market and the Impact of Inefficient Prices," p. 160, in Michael A. Crew Ed., *Expanding Competition in Regulated Industries*.

1 Moreover, some of Dr. Gabel's criticisms of the paper are off point. For example, Dr.
2 Gabel states that when explaining the variation in the number of CLECs assigned
3 numbering codes in each state, the authors do not control for the size of the state. But an
4 examination of the equation shows that the authors used Gross State Product for the
5 industries finance, insurance and real estate. Surely, this variable is highly related to "size
6 of the state." Dr. Gabel continues by stating that the authors fail to control for 47 U.S.C. §
7 251 exemption to rural carriers of unbundling requirements. However, the authors used
8 data from the RBOCs, GTE and Sprint, none of which received a rural exemption. Dr.
9 Gabel also incorrectly assumes that the business and residential price ratio was uniform
10 throughout the state and that the study is based on aggregate state data when in fact the
11 rate data and other data were based on a weighted average for the RBOC, GTE and Sprint
12 in each state.

13 In summary, Dr. Gabel's criticisms of the study are off point. The paper was peer
14 reviewed and published in a book on competition in regulated industries that included a
15 range of academic and professional economists.

16 Finally, it is interesting that Dr. Gabel does not comment on the other paper I mentioned
17 in my testimony co-written by James Eisner (an FCC staff member) and Professor Dale E.
18 Lehman which supports the hypothesis that residential rates do matter for competition.¹³
19 Eisner and Lehman state in their conclusion:

¹³ See, James Eisner and Dale E. Lehman, *Regulatory Behavior and Competitive Entry*, presented at the 14th Annual Western Conference Center for Research in Regulated Industries, June 28, 2001. The authors' main motivation appears to have been ascertaining how regulatory behavior—as it pertains to unbundled loop prices and 271 entry—affects competitive entry. Nevertheless, they control for local exchange prices as well.

1 ...in some specifications, there appears to be less competitive entry
2 (principally facilities-based) where residential rates are lower. These findings
3 are generally statistically significant at the 90% level.¹⁴

4

5 **Q. DR. GABEL (SECTION 4.3) SUGGESTS THAT PRICING BEHAVIOR IN OTHER**
6 **MARKETS SHOWS THAT FIRMS CAN PRICE COMPLEMENTARY**
7 **SERVICES LOW IN ORDER TO ATTRACT ADDITIONAL USAGE AND HE**
8 **CITES TO RAZOR BLADES AND TO WIRELESS PHONES AS EXAMPLES.**
9 **HOW DO YOU RESPOND?**

10 A. There are some differences between wireline telephony and the razor blade example.
11 While it is true that network access and usage are complementary services, it is also true
12 that they are separate standalone services that are demanded in their own right. For
13 example, a wireline customer could demand network access services on a stand-alone
14 basis without ever having an interest in usage. That is not the case with razor blades and
15 razors because both are required in order to be of use to customers; without the blade the
16 razor is of no value, and vice versa. The service in question is the razor **and** the razor
17 blade and one would expect that in competitive markets a razor company would recover
18 fully the incremental costs of the razor and razor blade through the sales of both.

19 Moreover, both the wireless and razor example that Dr. Gabel uses involve a form of
20 locking customers into a set technology that makes it costly to switch to competitors. For
21 example, once a consumer obtains a certain razor or cellular phone, they cannot be used

¹⁴ *Ibid.*, p. 25.

1 with other competitors services. That is, I cannot use my Gillette Mach 3 razor with the
2 Schick Quattro razor blades. Nor can I use my VoiceStream cell phone with Verizon's
3 wireless service. The same does not apply with wireline service. I can use the same loop
4 to access a different long distance company or, in the case of UNE-L and UNE-P, I can
5 use the same loop to access a different LEC.

6 This lock-in of technology permits a company like Gillette to price the razor below cost
7 (at times giving the razor away) and recover that loss by pricing the razor blade above
8 incremental cost. There is no standalone competition that would force the price of the
9 razor blade down to incremental cost. If there were, this pricing strategy would not be
10 sustainable. In telephone, one cannot price network access below incremental cost in the
11 hope of recovering the loss through higher usage prices because there is standalone
12 competition for usage—and other services that support network access—that drives usage
13 prices down to incremental costs. Therefore, there are significant differences in the
14 examples that Dr. Gable mentioned and wireline telephony service.

15 Finally, Dr. Gabel fails to mention that razor or wireless companies choose to market their
16 product in such a manner; they are not required to do so. In this proceeding, Dr. Gabel
17 presumably would force the companies to pursue a pricing strategy rather than permit
18 them to implement such a strategy only if it makes commercial sense to them. As
19 telecommunications markets continue to become increasingly competitive, this type of
20 micromanaging of pricing decisions is counterproductive.

21

22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

23 A. Yes.

1 BY MR. FONS:

2 Q Dr. Gordon, would you please summarize your
3 testimony.

4 A Yes. Thank you. Good afternoon, Madam Chairman,
5 Commissioners.

6 The petitioners in this proceeding have asked me to
7 comment on and provide an overview of the economic issues that
8 are raised by their proposals to lower intrastate access
9 charges to parity with interstate access charges and to
10 increase local telephone rates to be closer to the cost of
11 providing local telephone service, and to do so on a
12 revenue-neutral basis.

13 My perspective is that of an economist and a former
14 regulator concerned with efficient use of the telephone system,
15 and also very much with enabling efficient entry to take place
16 so as to promote competition.

17 While I was chairman of the Massachusetts Commission,
18 I was directly involved in the same question that you are
19 facing today. That was back in the mid, early to mid-'90s. We
20 did, in fact, rebalance rates and briefly I think we thought it
21 was a success.

22 The central issues are will rebalancing rates enhance
23 competitive entry and will it be beneficial generally to the
24 Florida economy and consumers? I believe the answer is yes.
25 The plans proffered by all three operating petitioning

1 companies will meet these goals in my opinion, and do so as
2 laid out by the Legislature.

3 By way of background, local telephone service,
4 especially residential service in Florida, as in most or maybe
5 even all other states, has been the recipient of support and/or
6 subsidies from other services for some time, especially through
7 access charges in recent years. I say that based on looking --
8 an examination of the prices of telephone service and the cost
9 evidence provided by the companies, but also by my knowledge of
10 the historical record and how telephone prices were set.

11 Therefore, to provide all parties, consumers and
12 companies alike, especially potential entrants, with better
13 information about the real costs of providing service and the
14 real opportunities associated with providing service, to inform
15 their choices as to whether to, how to use the system, whether
16 to invest in the system, whether to enter a market or not, so
17 that all these things can take place correctly, the Commission
18 should lower the access charges and, I believe, raise the rates
19 that have been supported closer or hopefully all the way to
20 cost. Sending all parties accurate price signals that reflect
21 the costs of their choices is essential if efficient
22 competition is to have an opportunity to thrive.

23 And I would say parenthetically that I think that has
24 been Florida's policy. Florida, along with Massachusetts and
25 perhaps one or two others, were in the forefront of embracing

1 local telephone competition, moving in that direction, not
2 under the duress of the Telecommunications Act of '96, but
3 rather moving before that time; in fact, probably helped bring
4 about the specifics of that Act.

5 Some specifics. Obviously raising -- I believe it's
6 obvious that raising basic local telephone service prices and
7 especially residential prices will make entry by competitors
8 into this market a more attractive proposition than it is
9 today.

10 In addition, the CLECs that are already operating in
11 Florida will be able to target a much broader audience than
12 they have been able to do so far. I would expect as a result
13 more investment in local service, more innovative activity in
14 the local service area and better opportunities for alternative
15 technologies. I'm thinking of wireless and cable, voice over
16 Internet protocols and the like. Economic theory predicts
17 this, but simple observation as well as empirical evidence
18 confirms it. Clearly, competition will be enhanced. And all
19 of this means more long distance calling, more investment, more
20 competitive entry. It will increase economic activity and
21 economic welfare in Florida.

22 It's well-established nationally that this system
23 that we have been living with for the last several decades
24 filled with cross-subsidies is an extremely expensive, that is
25 to say wasteful way to reach or maintain any universal service

1 goals or other goals that we may have. The waste has been
2 estimated to be in excess of \$2.5 billion annually, perhaps as
3 high as \$7 billion a year annually. That, of course, is a
4 national figure and doesn't apply directly to Florida.

5 Two other points I want to make. The big cost, the
6 big basic local telephone service cost in all of this is the
7 local loop itself, and the local loop is what is needed for a
8 subscriber to have access to the system. It is what firms need
9 to know the full costs of if they're to decide whether to
10 deploy a loop or not deploy it in any particular situation.
11 Having a price that's high enough to cover those costs is a
12 critical part of all decision-makers' processes.

13 The last point I want to just touch on, we can come
14 back to it, of course, is universal service and rate shock. I
15 do not believe rebalancing of this character will have any
16 significant impact on universal service. And I think the
17 measured steps that have been proposed in the plans means that
18 there will not be rate shock. That is to say it comes in
19 gradually enough to be certainly, I think, acceptable. Careful
20 provision has been made for low income customers who might be
21 negatively impacted, and Florida generally is not a low income
22 state. Of course, I realize there are some low income
23 individuals, but there is a program to deal with that.

24 Speaking as a former regulator, I found in
25 Massachusetts when we rebalanced rates that it was a nonstory

1 in the end. It did not make Page 1, it didn't even make Page
2 1 of the second section, and I think it was because it didn't
3 have any major deleterious effect on people in the
4 Commonwealth. So rate shock has not been a major problem
5 elsewhere, and I'm convinced that it's a manageable issue here
6 as well. And with that, I'll close my introduction.

7 MR. FONS: Dr. Gordon is available for
8 cross-examination.

9 CHAIRMAN JABER: Okay. Thank you.

10 Just so you know, as it relates to the company
11 witnesses, I'll ask all the companies first whether they have
12 cross-examination questions, and then conclude with the
13 consumer advocates. And, consumer advocates, the reverse will
14 be true when your witnesses are, are up. In that regard, Mr.
15 Meros?

16 MR. MEROS: No questions.

17 CHAIRMAN JABER: Mr. Hatch? Ms. McNulty?

18 MR. HATCH: No questions.

19 MS. McNULTY: No questions.

20 CHAIRMAN JABER: Have you all agreed on an order, Mr.
21 Beck?

22 MR. BECK: They've agreed I can go first.

23 CHAIRMAN JABER: I shouldn't have asked. Go ahead.

24 MR. BECK: Thank you, Madam Chairman.

25 CROSS EXAMINATION

1 BY MR. BECK:

2 Q Dr. Gordon, good afternoon. My name is Charlie Beck
3 with the Public Counsel's Office.

4 A Okay. Good afternoon.

5 Q During your summary you mentioned some figure, I
6 believe you said \$2.5 billion. Is that --

7 A Perhaps ranging as high as seven.

8 Q And could you point to me where in the prefiled
9 testimony that figure is set forth?

10 A It's in connection with a reference to -- I'll try
11 and find it. The reference to some work done by Robert
12 Crandall and Leonard Waverman. It's, I believe, in a footnote,
13 but I don't remember off the top of my head which footnote.

14 MR. CHAPKIS: I see that footnote; 22.

15 THE WITNESS: Thank you.

16 MR. CHAPKIS: It might be the proper reference.

17 CHAIRMAN JABER: Mr. Chapkis, I appreciate your help,
18 but let's let the witness answer the question.

19 THE WITNESS: Yeah. I'm there. The reference is to
20 some findings in a book by Robert Crandall and Leonard Waverman
21 called, "Who Pays for Universal Service?: When Telephone
22 Subsidies Become Transparent."

23 Q And could you show me where in your Footnote 22 the
24 figure you gave in your summary is indicated?

25 CHAIRMAN JABER: Mr. Beck, I'm having a hard time

1 hearing you. I don't know if it's the microphone.

2 MR. BECK: I'll speak up.

3 CHAIRMAN JABER: Thank you.

4 BY MR. BECK:

5 Q I asked Dr. Gordon to show me where in Footnote 22
6 that the figure he gave in his summary is indicated.

7 A It's actually mentioned in the text itself.

8 Q So there's nowhere in your testimony, including the
9 footnote, where the figure you just gave in your summary is
10 actually indicated or is it?

11 MR. FONS: I object. If --

12 THE WITNESS: It's Line 18.

13 BY MR. BECK:

14 Q Okay. Thank you. You do have it.

15 Dr. Gordon, you've been on two different public
16 utility commissions; is that right?

17 A That's correct.

18 Q You were on the Maine Public Utility Commission from
19 October 1988 to December 1992?

20 A Yes.

21 Q And then I guess, did you go directly from that to
22 the Massachusetts Department?

23 A Yes, I did.

24 Q And you left there in October of 1995?

25 A I think that's right, to the best of my recollection.

1 Q And did you join NERA directly from leaving the
2 Massachusetts --

3 A Shortly after. Not immediately.

4 Q Uh-huh. Could you go to Page 12, please, of your
5 Attachment A.

6 A Of which one?

7 Q Page 12.

8 A Of the direct?

9 Q Yes. Attachment A where it lists your various
10 publications and testimonies.

11 A I don't -- actually I don't have that copy with my --
12 I don't have my CV with that. If you could provide me with a
13 copy, that would be helpful.

14 CHAIRMAN JABER: Mr. Fons, make sure he's got both
15 attachments while you're at it, please.

16 THE WITNESS: I do have the other attachment.

17 Thanks. What Page?

18 BY MR. BECK:

19 Q Page 12.

20 A Yes.

21 Q About a third of way down there's listed an affidavit
22 in support of the Florida Public Service Commission's appeal of
23 an FCC order. Do you see that?

24 A Yes.

25 Q How did it come about that you filed an affidavit in

1 support of the Florida Public Service Commission?

2 A I was asked to -- approached and asked to do so.

3 Q Did you -- was it the Commission itself that asked
4 you to file that? I mean, did they hire you?

5 A This was done for the Commission. I don't know
6 how -- I don't recall what the agency was. I honestly don't
7 recall how it came to be, and I didn't review it before this
8 meeting.

9 Q I guess my question is, do you know whether you were
10 actually hired by the Florida Public Service Commission or not
11 to do that?

12 A I'm not sure that it was, but I'm not sure who --
13 what the process was. It was quite a few years ago.

14 Q Could you turn, please, to Page 13 of your amended
15 direct testimony?

16 A I have it.

17 Q Okay. At the bottom, beginning on Line 22, you
18 state, "Thus, even with the increase in basic residential local
19 rates, telecommunications will be just as affordable to Florida
20 consumers as before, yet consumers will be better off because
21 they will be consuming a different mix of telecommunications
22 services that provides more value than they are currently
23 receiving." Do you see that?

24 A Yes.

25 Q Now when you say it will be affordable to Florida

1 consumers on Line 23 --

2 A Yes.

3 Q -- do you mean Florida residential consumers?

4 A Yeah. I'm talking about residential consumers.

5 Q Okay. And on what basis do you conclude that the,
6 the increase will be just as affordable after the local
7 increases?

8 A Because they will still be in a reasonable range of
9 --

10 Q So you're not saying --

11 A Not that it will be -- I'm not saying that it would
12 be exactly offset.

13 Q So you're saying the bill is to go up?

14 CHAIRMAN JABER: Dr. Gordon and Mr. Beck --

15 THE WITNESS: I'm sorry. I'll let him go.

16 CHAIRMAN JABER: We're going to have to let him ask
17 the question, and when we're sure you're done with the
18 response, he'll ask the next question. And I think you weren't
19 done with your response, so go ahead and finish your thought.

20 THE WITNESS: I think I lost it.

21 CHAIRMAN JABER: The question initially posed to you
22 was, on what do you base the statement that it will still be
23 affordable to the Florida residential consumers, and you were
24 explaining, I think, that it's within the range.

25 THE WITNESS: Thank you. It's still within a

1 reasonable range of cost so that it shouldn't be substantial
2 enough to price it out of anybody's reach. It wasn't meant to
3 be a specific mathematical equality.

4 BY MR. BECK:

5 Q Okay. So when you say just as affordable, you mean
6 that the rates could go up for residential customers?

7 A They could go up somewhat and still be affordable.

8 Q Have you reviewed any of the filings by the
9 interexchange carriers showing how they're going to flow
10 through the access reductions to their long distance customers?

11 A I've given them a general review. I haven't examined
12 them closely.

13 Q Do you know how they're going to do it? Are you
14 familiar with what rates they're going to reduce in response to
15 the access reductions?

16 A Not specifically.

17 Q Do you know whether interexchange carriers plan to
18 flow through access reductions to residential customers in the
19 same proportion that the residential customers are picking up
20 the local rate increases?

21 A I don't know that. I do know that they plan to flow
22 them through to both classes of customers.

23 Q Okay. Could you turn to Page 17 of your amended
24 direct testimony.

25 A Yes, I have it.

1 Q Beginning at Line 16. And what I'd like you to do,
2 if you would read Lines 16 through 20.

3 A Would you like me to read it out loud?

4 Q Either way. You can just read it to yourself. I'd
5 like to ask you some questions about it.

6 A Yes, I've read it.

7 Q Okay. And you mention that increased stimulation
8 from lower long distance charges would represent real gains to
9 consumers.

10 A Yes. That's right.

11 Q What's your basis for believing that there will be
12 reductions in the -- or I take it you mean by stimulation there
13 would have to be reductions in long distance per minute
14 charges, wouldn't there?

15 A Yes, that's right.

16 Q What's your basis for believing that's true, if you
17 do believe it's true?

18 A Well, I do believe it's true, and I believe it for
19 really two reasons. One, in Florida I gather there's a
20 requirement that it be -- that reductions be passed through.
21 But in -- whether or not that were the case, the long distance
22 market is a competitive one, and so cost reductions would find
23 their way through to consumers through the competitive process
24 if their legal requirements were not there.

25 Q Okay. If an interexchange carrier were only to

1 reduce its or eliminate its in-state connection fee, would
2 there be any stimulation in long distance usage in that case?

3 A If it reduced what?

4 Q If it only reduced its in-state connection fee -- are
5 you familiar with what the in-state connection fees are?

6 A No.

7 Q Would you accept, subject to check, that it's simply
8 a monthly fixed amount that some carriers have added or made
9 part of their long distance charges?

10 A Subject to check.

11 Q Okay. Now if -- assuming that the in-state
12 connection fee is simply a fixed monthly charge imposed by some
13 interexchange carriers, would a reduction to that charge
14 stimulate long distance usage?

15 A It would, it would -- might have some kind of a
16 wealth or an income effect, but it wouldn't have a price effect
17 of the substitution sort.

18 Q Okay. Do you know if there are any carriers in
19 Florida that do not charge the in-state connection fee?

20 A I don't know that.

21 Q Okay. Could you go to Attachment B to your amended
22 direct testimony.

23 A I have it.

24 Q And this chart shows the percent of competitive local
25 exchange company lines sold to residential and small business

1 customers by state; is that right?

2 A Yes.

3 Q Okay. And --

4 A As of December of 2002.

5 Q Okay. And I tried to count the number of bars here
6 and only came up to 39. Do you know whether all the states are
7 represented in this chart?

8 A Well, if it's 39, they're certainly not all
9 represented.

10 Q Okay.

11 A This is, this is a document that was obtained from
12 the FCC and just only contains that number of -- only contains
13 the states that are demonstrated there.

14 Q Okay. Do you know why there's 11 states missing?

15 A I do not.

16 Q There's some states that have a smaller percentage of
17 lines for residential --

18 A Yes.

19 Q -- than Florida?

20 A There are about ten or so to the right on the chart.

21 Q Okay. South Carolina and North Carolina are both
22 states that have a smaller percentage of lines serving
23 residential; is that correct?

24 A That's correct.

25 Q Okay. And do those states have higher local exchange

1 rates than Florida does?

2 A I don't know the answer to that.

3 Q Okay. Could you assume with me for the purposes of
4 these questions that they have higher local exchange rates, if
5 you would?

6 A If that is correct.

7 Q Okay.

8 A It has to be subject to check.

9 Q Okay.

10 A And we do need to check it.

11 Q Assuming that's so, why would South Carolina and
12 North Carolina have a smaller percentage of CLEC lines serving
13 residential consumers than Florida?

14 A The answer is I don't know because I haven't
15 investigated that question in detail. But those percentages
16 are driven by many factors, and I don't know what's going on in
17 addition to rate rebalancing and so forth.

18 MR. BECK: Dr. Gordon, thank you. That's all I have.

19 CHAIRMAN JABER: Attorney General's Office. Attorney
20 General's Office, any --

21 MR. TWOMEY: I'll just ask some very quick ones.

22 Good afternoon, sir.

23 CHAIRMAN JABER: Mr. Twomey, hang on. I don't --

24 MS. BRADLEY: That's okay.

25 CHAIRMAN JABER: Do you have any questions?

1 MS. BRADLEY: I don't have any questions.

2 CHAIRMAN JABER: Okay. Go ahead, Mr. Twomey.

3 CROSS EXAMINATION

4 BY MR. TWOMEY:

5 Q Dr. Gordon, am I correct from looking at your vitae
6 that you've only testified for industry since you left the
7 Massachusetts Commission?

8 A That's generally true. Not literally, but
9 generally -- for practical purposes.

10 Q Predominantly so; correct?

11 A Right.

12 Q Okay. You, you said in your, I think your opening
13 remarks, that, that you thought rate shock would be acceptable
14 or manageable; correct?

15 A I believe it is a manageable issue.

16 Q Do you know what the, do you know what the percentage
17 increases Dr. Cooper, or Gordon are for BellSouth's customers
18 over the transition period?

19 A I didn't calculate the percentage, but they're
20 increases of between \$1 and \$2 in steps.

21 Q Do you know what the total dollar increases are for
22 BellSouth?

23 A I do, but -- I mean, I do. I don't know them off the
24 top of my head.

25 Q Do you know -- let me ask you, are you aware that

1 the, the percentage increase for BellSouth's customers varies
2 by, by rate grouping?

3 A Varies by what?

4 Q Rate group.

5 A Yes.

6 Q So you're not aware then that the proposed rates
7 would result in, in rate increases that would vary from 35 to
8 some 51 percent?

9 A Yes, I am. And I -- yes was the answer to my last
10 question.

11 Q So 51 percent rate increases in your testimony are
12 manageable?

13 A It depends on the base. It's a relatively small base
14 and, yes, I think they are manageable.

15 Q I see. How about, how about Sprint's? Do you know
16 the range of Sprint's increases?

17 A Yes. They're considerably larger than either
18 BellSouth or Verizon. That being a function of the territory
19 that they serve.

20 Q Okay. Sir, would you -- given that they're larger,
21 would you concede that the rate shock is, is less manageable
22 than for BellSouth?

23 A Well, it's certainly more noticeable. Whether it's
24 less manageable is another issue.

25 Q Okay. Someplace in your testimony, I apologize, I've

1 lost it, in your direct testimony you, you indicated that the
2 Florida Legislature has seen that the Lifeline customers will
3 not be subject to the rate increases; is that correct?

4 A Correct.

5 Q Okay. And is it -- are you not aware, sir, that,
6 that that's only true until such time as parity is achieved
7 under the Florida Statutes?

8 A I know that, yes.

9 Q Would you concede then that the Lifeline customers
10 will, in fact, receive the same level of rate increases as the,
11 as the other customers when, when parity is reached?

12 A They may. I don't know what the pricing policies
13 will be at that point.

14 Q Are you aware of whether or not there will be
15 additional financial assistance for those Lifeline customers
16 with which to meet the increased rates?

17 A They have to be parity.

18 MR. FONS: I'm going to -- excuse me. I'm going to
19 object to the question. It calls for the witness to speculate.
20 There's been no foundation.

21 CHAIRMAN JABER: Okay. The objection is that the
22 question calls for speculation. Mr. Twomey, your response.

23 MR. TWOMEY: My response is his direct testimony says
24 that he doesn't think that, he doesn't think these increases
25 will harm Lifeline recipients. He has conceded thus far on

1 cross-examination that -- he says initially that it won't harm
2 Lifeline customers because they will not receive the rate
3 increases. He concedes on cross that, in fact, the, the
4 Lifeline customers will receive the same level of rate
5 increases.

6 MR. FONS: I object. That's not what the witness
7 testified to.

8 CHAIRMAN JABER: Okay. Mr. Twomey --

9 MR. TWOMEY: Yes, ma'am.

10 CHAIRMAN JABER: -- finish your statement without
11 putting words in the witness's mouth, and we'll take one
12 objection up at a time.

13 MR. TWOMEY: His, his testimony is, is that Lifeline
14 customers won't be harmed, that the -- and I'm just merely
15 trying to find out whether he knows if there's additional
16 assistance for those customers after, in fact, they get the,
17 the rate increases imposed. Either he does or he doesn't.

18 CHAIRMAN JABER: I'll allow the question.

19 Dr. Gordon, just for the future though so I can hear
20 what the objection is and pay attention to what's going on,
21 when you hear your attorney raise an objection, I need you to
22 stop answering the question and let him, let him finish
23 speaking.

24 Go ahead. Do you need the question repeated?

25 THE WITNESS: Yes, I do.

1 CHAIRMAN JABER: Mr. Twomey.

2 BY MR. TWOMEY:

3 Q Yes, sir. Do you know whether or not Lifeline
4 recipients will have available to them additional assistance,
5 financial assistance with which to help pay the increased rates
6 when they receive them?

7 A I cannot know that because it's in the future. I
8 don't know what the policies of the Legislature or anybody else
9 would be.

10 Q Okay. Would you agree if no such assistance was
11 available, that the ability of Lifeline customers to meet, pay
12 their phone bills would be degraded, given the increased rates?

13 MR. FONS: I'll object to the form of the question.
14 It calls again for the witness to speculate. It doesn't ask,
15 do you know whether or not. He's asking him what will happen
16 in some scenario that's in the future.

17 CHAIRMAN JABER: Mr. Fons, I specifically heard the
18 beginning of the question was, do you know.

19 MR. FONS: No. I think he asked, do you agree, would
20 you agree?

21 CHAIRMAN JABER: Mr. Twomey, what's your response?
22 The objection is the form of the question.

23 MR. TWOMEY: My response is it's pretty
24 straightforward. If, if I ask him to -- if he says he doesn't
25 know if there's money and I ask him, I think -- I intended to

1 ask him if there's not any money and additional assistance and
2 the rates, in fact, go up, don't you agree that it'll be harder
3 for them to pay their bills? That's the thrust of it.

4 CHAIRMAN JABER: I'll allow the question, Mr. Twomey.
5 Let's stay focused on what is in the scope of the testimony.
6 Reword your question so that it doesn't call for speculation.

7 Mr. Fons, just for the purpose of future objections,
8 your witness does make statements that are based on certain
9 things he expects will happen. And I think Mr. Twomey is not
10 far beyond that when he's asking if other conditions exist, do
11 you know? I will allow the question.

12 BY MR. TWOMEY:

13 Q Did you understand the question?

14 A I don't know. I think you better come around one
15 more time.

16 Q Yes, sir, I will.

17 I want you to assume that there's no, no additional
18 financial assistance made available to Lifeline customers, and
19 yet at some point they will receive the same level of rate
20 increases as all other customers of these three ILECs. That
21 being the case, don't you agree with me that it'll be more
22 difficult for them to pay their phone bills?

23 A In that case, if nothing else happens, for example,
24 to their income, if you hold literally everything in the system
25 constant, which I would not assume would be the case, but if

1 you did, then it would take a larger proportion of their
2 income.

3 MR. TWOMEY: Yes, sir. That's all I have.

4 CHAIRMAN JABER: Staff, Ms. Keating.

5 CROSS EXAMINATION

6 BY MS. KEATING:

7 Q Good afternoon, Dr. Gordon.

8 A Good afternoon.

9 Q First I'd like to go back over some of the areas that
10 we touched on in your deposition.

11 Can you hear me all right?

12 A Yeah. It's close, but I can hear you.

13 Q Just stop me if you can't hear me.

14 A I will.

15 Q First off, on Page 23, Lines 18 through 19 of your
16 direct testimony, this is your amended direct.

17 A Page 23?

18 Q Yes, sir.

19 A Line 18 and 19?

20 Q Yes, sir. You stated there that, "to have
21 economically efficient basic local prices would likely require
22 that basic local services be priced above forward-looking
23 direct costs."

24 A Yes, I see that.

25 Q Now if I recall correctly from your deposition, you

1 had indicated though that even if the ILECs' petitions in these
2 proceedings are granted, you don't think that the resulting
3 prices will be at or above forward-looking direct costs; isn't
4 that correct?

5 A That's correct. That is correct.

6 Q But you do still believe that the rebalancing will
7 induce competitive market entry.

8 A Oh, certainly.

9 Q Is that correct?

10 A Yes, I do.

11 Q And if I understood you correctly, was that because
12 of the ability to target customers with bundled offerings?

13 A That's certainly one -- being able to target
14 particularly likely profitable subgroups of customers. I mean,
15 that's already taking place, just not as on as large a scale as
16 perhaps one might hope. But this would widen the circle of
17 customers who might be approachable; those customers who are
18 particularly profitable to sell to or a particularly low cost
19 to serve, more of them would be brought into that circle. You
20 don't have to reach full economically efficient prices in order
21 for that to happen because the prices we're talking about here
22 are broad averages. And concealed in those averages are
23 substantial differences both on, on the revenue side and on the
24 cost side.

25 Q But in having that ability to target customers with

1 the bundled packages, do you believe that that's going to make
2 up for any shortfall in the difference between basic, the
3 actual prices that are being charged and the actual costs for
4 basic local service?

5 A I'm sorry.

6 Q Go ahead.

7 A My point there has nothing to do with whether the
8 services are bundled or not. Let's just simply look at --
9 suppose somebody were just buying pure access, pure basic local
10 telephone service. It's hard to believe, imagine that, but
11 take it for the moment. If that person that you were
12 approaching was a particularly low-cost person to serve, then
13 even with a retail price that is below the economically
14 efficient level, you might still be able to serve them
15 profitably. The reason is that their costs are very low.
16 Maybe they're in an extremely densely populated neighborhood,
17 maybe they live two doors down from a central office. In other
18 words, their costs are low and their cost isn't the average
19 cost of, you know, a typical customer in the system, it's well
20 below that, and so somebody can find it profitable to approach
21 them.

22 Now the higher and the closer the price is to the
23 economically efficient price, the larger that circle is going
24 to be, but it still will not include everybody because there
25 will be some people whose cost to serve is well above average.

1 And people who have no obligation to serve will not find it
2 reasonable to approach that group.

3 Q So I guess what you're saying is the high-cost
4 customers are not going to be targeted?

5 A Not first. That's for sure. They may be targeted,
6 of course, by somebody else with a different technology, for
7 example. It may not be so high cost for a wireless provider or
8 perhaps a cable provider.

9 Q I'd like to talk a little bit now about the, the
10 paper that you referenced in your direct testimony that was
11 done by Ross and McDermott. And we also talked --

12 A Ross and McDermott, yes.

13 Q And that paper provides empirical evidence, as you've
14 described it, that rate rebalancing will likely make the
15 residential local market more attractive; is that correct?

16 A The evidence in that paper suggests that, yes.

17 Q Okay. But as I understand it, the data that they
18 used in that paper was not Florida specific; is that correct?

19 A It was -- it couldn't be. It's a cross section study
20 across different states that have rebalanced to different
21 degrees, and it's not possible to make that comparison within
22 the State of Florida. You couldn't do a study that was
23 structured the way this one was. It's meant to ask the broad
24 question, if a state rebalances, other things equal, is it more
25 or less likely that there will be competitive entry. And

1 they -- Ross and McDermott found evidence that states that had
2 rebalanced would experience more entry than states that hadn't.
3 That's holding things constant, other factors that might affect
4 entry as constant as they could.

5 Q Well, I guess what I'm wondering is since the data in
6 that paper wasn't Florida specific, is that sufficient evidence
7 that granting the petitions will induce enhanced market entry
8 in the Florida market?

9 A Well, I think it's a piece of evidence that goes in
10 along with other arguments, but it certainly points in that
11 direction. But we're talking about a general economic
12 phenomenon that isn't specific to any particular state. It
13 just says that if consumers and producers in Florida have the
14 same characteristics generally as people in the rest of the
15 United States and behave the same way in response to economic
16 incentives, this will tend to be the case.

17 Q Well, let me ask you this: Do you believe that the
18 Commission can rely solely on economic theory as opposed to
19 empirical evidence in determining whether granting the
20 petitions will induce enhanced market entry?

21 A I don't think it has to. I mean, there is some
22 evidence out there and there's certainly some anecdotal
23 evidence. But I would suggest that the theory should not be
24 dismissed lightly because it's a rather simple theory. It
25 simply says if there are more profits to be made, there will be

1 more entry.

2 Q I realize you don't --

3 A That's a pretty widely supported proposition and
4 certainly not just restricted to regulated utilities. It's
5 just a general proposition in industry behavior.

6 Q I realize that you don't believe it has to rely
7 solely on economic theory. But if you could answer my
8 question, do you think it could rely solely on economic theory
9 to determine whether --

10 A I think, I think back when I was in Massachusetts and
11 we were considering this question there hadn't been a lot of
12 rebalancing, maybe Illinois, but we were pretty much riding on
13 economic theory and the conviction that those results would,
14 would be yielded.

15 Q Okay. I want to talk just a minute then about how
16 companies evaluate markets when deciding to enter a market.

17 A Yes.

18 Q And I want to talk about it from the perspective of a
19 UNE-P based CLEC. Okay?

20 A Okay.

21 Q Would you agree that a UNE-P based CLEC would
22 consider the revenues and costs for all services, not just
23 basic services, when evaluating markets for entry?

24 A That's one of the things they would evaluate. They'd
25 look at the overall costs and revenues. It wouldn't be the

1 only thing they looked at, but they'd look at it.

2 Q Those would be a couple of the primary concerns, do
3 you believe?

4 A They'd have a number of concerns in entering a
5 market. Whether they could come out of it financially whole
6 would obviously be one. But they would also be looking at how
7 they might approach their marketing, what kinds of services
8 they might sell, what kinds of customers they could best
9 target. They'd be looking to see what the various components
10 of their costs would be and so on. Now UNE-P based means that
11 they have a basic price for the connections.

12 Q Would you also agree that a UNE-P based CLEC would
13 likely consider sources of revenue such as basic and nonbasic
14 and access charges in its cash flow equation?

15 A Sure.

16 Q Okay. And as for costs, would you agree that a UNE-P
17 based CLEC would likely consider costs such as the cost of
18 UNE-P itself?

19 A I lost the last part of your question.

20 Q Would a UNE-P based CLEC likely consider costs such
21 as the cost of UNE-P itself?

22 A Yes.

23 Q And marketing costs I believe you've already
24 indicated.

25 A That would be their own retailing costs. Yeah.

1 Q And billing would be a cost?

2 A Yes.

3 Q And customer service?

4 A Hopefully.

5 (Transcript continues in sequence with Volume 3.)

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1 STATE OF FLORIDA)
 :
2 COUNTY OF LEON)
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CERTIFICATE OF REPORTER

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4 I, LINDA BOLES, RPR, Official Commission
5 Reporter, do hereby certify that the foregoing proceeding was
6 heard at the time and place herein stated.

7 IT IS FURTHER CERTIFIED that I stenographically
8 reported the said proceedings; that the same has been
9 transcribed under my direct supervision; and that this
10 transcript constitutes a true transcription of my notes of said
11 proceedings.

12 I FURTHER CERTIFY that I am not a relative, employee,
13 attorney or counsel of any of the parties, nor am I a relative
14 or employee of any of the parties' attorneys or counsel
15 connected with the action, nor am I financially interested in
16 the action.

17 DATED THIS 11th DAY OF DECEMBER, 2003.

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