

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of Verizon)
Northwest Inc. for an Order Approving)
Commencement Of Bifurcated General Rate)
Case and Waiver of WAC 480-07-510(2)) **DOCKET NO. UT-040788**

DIRECT TESTIMONY OF
ORVILLE D. FULP
ON BEHALF OF
VERIZON NORTHWEST INC.

AUGUST 23, 2004

1 **INTRODUCTION**

2

3 **Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, EMPLOYER AND**
4 **TITLE.**

5 A. My name is Orville D. Fulp. My business address is 600 Hidden Ridge Drive, Irving,
6 Texas 75038. I am employed by Verizon as Director-Regulatory.

7

8 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND WORK**
9 **EXPERIENCE IN THE TELECOMMUNICATIONS INDUSTRY.**

10 A. I have a Bachelor of Arts degree in Economics from the University of California, San
11 Diego, and a Master of Science degree in Economics from the University of Wyoming.

12

13 In 1981, I began working at the Illinois Commerce Commission in the Economics and
14 Rates Department as Senior Economist, where I analyzed filings and testified in utility
15 rate proceedings in the areas of pricing, cost of service, and demand analysis. In January
16 of 1984, I transferred to the Policy Analysis and Research Division as Director of the
17 Pricing Program. My responsibilities included developing policy concerning pricing in
18 the telecommunications and energy fields.

19

20 In 1985, I joined Contel as Manager-Revenue Requirements/Pricing for the Company's
21 eastern region, and was responsible for rate case activity, tariff maintenance, surveillance
22 of regulatory activities, and pricing of local exchange, toll and access services in six
23 states.

1 In 1991, I became a Manager-Access Pricing for GTE Telephone Operations, and was
2 responsible for the development of access pricing plans and rates for interstate and
3 intrastate purposes in 40 states. Since that time I have held various positions in GTE and
4 Verizon involving pricing and product management and operations. In December 2001, I
5 assumed my current position of Director – Regulatory. My current responsibilities
6 include national public policy and pricing matters.

7
8 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE STATE REGULATORY**
9 **COMMISSIONS?**

10 A. Yes, I have testified on national public policy and pricing matters, including several
11 generic access charge dockets and other pricing related dockets over the last 15 years, on
12 behalf of various Verizon telephone companies before state commissions in California,
13 Florida, Illinois, North Carolina, South Carolina, Georgia, Alabama, Maine, Vermont,
14 New Hampshire, Pennsylvania, and Washington.

15
16 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

17 A. The purpose of my testimony is twofold. First, I will provide a description of the
18 products and services Verizon Northwest Inc. (Verizon NW) proposes for increases to
19 generate \$110 million in additional revenue. Second I will provide the rationale and
20 justification for the pricing approach we have proposed in this case. Mr. Collins will
21 provide testimony on the cost (Verizon NW calculated direct and shared TSLRIC)
22 associated with the products and services contained in my pricing proposals.

1 **Q. IS VERIZON NW SEEKING A \$240 MILLION INCREASE IN ITS REVENUE**
2 **REQUIREMENT?**

3 A. Yes. Verizon NW is requesting the Commission approve its \$240 million revenue
4 requirement even though it has filed tariffs for a \$110 million price increase. My
5 testimony does not obviate the \$240 million revenue requirement. Verizon NW is asking
6 for \$110 million in price increases based on cost, product, and customer considerations.

7

8 **PRODUCTS AND SERVICES SELECTED FOR INCREASES**

9 **Q. WHAT ARE THE NON-BASIC PRODUCTS AND SERVICES VERIZON NW**
10 **PROPOSES TO INCREASE PRICES FOR IN THIS FILING?**

11 A. Verizon NW is proposing price increases to the following non-basic categories and
12 services:

13 1. Special Access – Special Transport Per Mile, Special Access Line Two-Wire and
14 Special Access Line Four-Wire;

15 Digital Data Services – Special Transport-All Speeds and Special Access Lines
16 All speeds;

17 High Capacity DS1 – DS1 Special Access Line-First System and DS1 Special
18 Access Line-Additional System.

19 2. Remote Call Forwarding – Business and Residential

20 3. Custom Calling Features (Residential) – Call waiting/cancel call waiting; call
21 forwarding; 3-way calling; speed dialing 8; speed dialing 30; call block; priority call-
22 VIP alert; call trace PPU; custom calling packages-big deal option A; big deal option
23 B; GTE basic pack; GTE complete pack.

1 4. Custom Calling Features (Business) – call waiting/cancel call waiting; call
2 forwarding; 3-way calling; call trace PPU.

3 5. Custom Calling Package Discounts – Flexible package discount reduced to 30%.

4 6. Directory Listings – Non-published; additional listing; non-listing.

5 See Exhibit ODF-2 for a listing of all products and services current and proposed prices.
6

7 **Q. WHAT OTHER NON-BASIC PRODUCTS AND SERVICES IS VERIZON NW**
8 **PROPOSING TO ADD OR CHANGE?**

9 A. Verizon NW is proposing to implement a late payment charge. Also, Verizon NW is
10 proposing to decrease the directory assistance call allowance from 2 to 0 for residential,
11 and from 1 to 0 for business. See Exhibit ODF-2 for a listing of these products and
12 services current and proposed rates.
13

14 **RATIONALE FOR THE PRICING APPROACH**

15 **Q. PLEASE PROVIDE THE PRICING RATIONALE FOR THE NON-BASIC**
16 **SERVICES PRICE INCREASES.**

17 A. Verizon NW's proposal takes into account cost and customer considerations. In some
18 cases, prices were below cost and have been increased to bring them closer to their
19 respective cost. In other cases, product and services have been priced above cost in order
20 to provide contribution to Verizon NW's overall revenue requirement and lessen the
21 increase to basic residential rates. In the instances where we have priced our products
22 and services above cost, Verizon NW may incur a customer risk and will have to closely
23 monitor demand for these services, as well as competitive actions of other carriers.

1 Given the competitiveness of the current and future market, pricing of our products and
2 services is not an exact science but rather informed judgment based on various
3 considerations. In this case, one of our main objectives was to minimize, to the extent
4 possible, basic rate increases for residential services. I will address each product and
5 service later in my testimony.

6
7 **Q. PLEASE EXPLAIN VERIZON NW'S RATE DESIGN APPROACH.**

8 A. Verizon NW first looked at all non-basic (services that are not residential and business
9 basic dial tone) products and services that, given customer concerns, could potentially
10 sustain price increases. The relationship of the product and service prices with their
11 associated cost (Verizon NW calculated cost contained in Mr. Collins testimony) was
12 then assessed. Finally, the market prices for these products and services were examined
13 to determine what price alignment could be proposed. For basic services, (residential and
14 business basic dial tone) Verizon NW looked at residential and business basic rates
15 charged by other companies in Washington and determined that a monthly increase of
16 \$9.80 to residential/ business basic rates would produce rates within the range of rates
17 that currently exist in the state. We also took into consideration the current cost/price
18 relationship that showed residential rates are far below Verizon NW's calculated cost
19 (direct and shared TSLRIC) of providing residential service. Price-outs were then
20 developed based upon test year units and the new prices. This price-out equates to the
21 proposed \$110 million revenue increase.

1 **Q WHAT COST STUDIES IS VERIZON NW USING FOR THE BASIC AND NON-**
2 **BASIC PRODUCTS AND SERVICES.**

3 A. Mr. Collins has provided testimony on the cost studies (direct and shared TSLRIC)
4 utilized to support my pricing proposals. He explains the cost model (VzCost) used for
5 his studies, and the general approach VzCost utilizes for calculating recurring cost, as
6 well as other cost considerations and issues germane to our pricing and cost filing.

7
8 **Q. PLEASE EXPLAIN WHY BOTH DIRECT AND SHARED COSTS ARE**
9 **INCLUDED.**

10 A. Retail products and services, in the aggregate, should recover both their direct and shared
11 cost and make a contribution to common cost. The pricing of the products and services
12 included in this filing therefore should recover, in the aggregate, both their direct and
13 shared cost and make some contribution to common cost. Direct costs are commonly
14 used for calculating the price floors for retail services. These are the costs that vary with
15 the output of a service or with the output of the entire service. Shared costs are those
16 costs that are required for the production of two or more services and do not vary with
17 increases or decreases in output. Total or average costs are defined as the sum of the
18 direct and shared costs. These are the costs that should be considered for recovery when
19 pricing products and services.

20
21 **Q. PLEASE ADDRESS THE SPECIFIC PRICING FOR EACH PRODUCT AND**
22 **SERVICE.**

23 A. See below.

1 **Special Access- Voiceband Facilities**

2 All the special access voiceband facilities are priced below their current Verizon NW
3 calculated cost today. The proposed price increases for the two and four wire access line
4 rates, while still not covering Verizon NW calculated cost, move these rates towards their
5 respective cost while maintaining market based rates. Special transport (per mile) is
6 priced above cost in order to provide more contribution from these rates while still
7 attempting to maintain an overall market based set of rates for the Voiceband services.

8
9 **Special Access- Digital Data Services**

10 Both the special transport and special access line rates are priced above cost in order to
11 provide more contribution to Verizon NW's overall revenue requirement.

12
13 **High Capacity DS1**

14 Both the DS1 special access line rates for the first and additional system are currently
15 priced below cost. Verizon NW's proposed increases put these rates above cost in order
16 to provide contribution.

17
18 **Custom Calling Features/Custom Calling Packages**

19 I will discuss all custom calling features versus addressing each feature on a case-by-case
20 basis. The rates for these discretionary services have been increased further above their
21 cost to generate additional contribution.

1 **Q. PLEASE PROVIDE THE RATIONALE FOR ESTABLISHMENT OF THE**
2 **PROPOSED LATE PAYMENT CHARGE?**

3 A. Under the existing tariff, Verizon NW has no method of prompting its customers to pay
4 their bills on time other than through service disconnections. Otherwise stated, there is
5 no penalty for paying late and Verizon NW is moved down in the priority some
6 customers pay bills. In order for a late payment charge to be effective, it must be
7 substantial enough to get a customer's attention without being excessive. Under our
8 proposal, the average customer will pay a \$5.00 late payment charge. A higher charge is
9 not assessed until the customer has an unpaid balance of at least \$334, at which point
10 they will pay 1.5% of the balance due. Currently, other ILECs and Verizon NW
11 competitors charge a late payment similar to this proposal.

12
13 **Q. ARE THE COSTS ASSOCIATED WITH THE LATE PAYMENT CHARGE**
14 **ALSO RECOVERED IN THE MONTHLY RECURRING COSTS (MRC),**
15 **CREATING A DOUBLE RECOVERY ISSUE?**

16 A. No. These costs are only incurred when the customer is actually late in making their
17 payment. There is no accurate way to forecast a quantity of late payments and then
18 calculate that recovery over a period of time that would be fair to the customers who pay
19 on time and ensure that Verizon NW collects the correct amount of funds to cover the
20 actual costs lost by Verizon NW from late payments. The only way to accurately recover
21 the costs associated with late payments is to have those customers who pay late to pay the
22 costs associated with the handling and loss of funds caused by their late payment.

23

1 **Q. HOW SHOULD THESE COSTS ASSOCIATED WITH LATE PAYMENT BE**
2 **RECOVERED?**

3 A. The most efficient and equitable means of recovery is to charge the cost causer for those
4 costs. Spreading such a directly identifiable cost over a general class of services or
5 products, ordered over time (as would be the case if the costs were recovered through
6 recurring rates), would be less direct, as well as far less efficient and equitable,
7 particularly if estimates of future quantities prove too high (or too low).

8
9 **Q. PLEASE DISCUSS THE RATIONALE FOR VERIZON NW'S DIRECTORY**
10 **LISTINGS PROPOSAL.**

11 A. Listing rates in Washington State are below market levels when compared to Verizon
12 NW Listing rates in other jurisdictions and current competitor rates in Washington State.
13 The current rates were reduced from \$2.25 in 2001 associated with a change to the
14 Directory assistance rates.

15
16 See table below:

17 **DIRECTORY LISTING PRICES**

	Additional Listings	NonPublished	NonListing
Verizon Average	\$1.87	\$2.10	\$1.45
AT&T	\$1.50	\$.75	\$.60
Comcast	\$1.00	\$.75	\$.60
Eschelon	\$1.85	\$2.00	\$1.00
Global Crossing Local Services	\$1.75	\$2.25	\$2.25
Integra Telecom	\$5.00	\$.75	\$.50

18
19

1 **Q. PLEASE PROVIDE THE RATIONALE FOR REDUCING THE DIRECTORY**
2 **ASSISTANCE CALL ALLOWANCE FOR BOTH BUSINESS AND**
3 **RESIDENTIAL?**

4 A. Verizon NW's proposal for Directory Assistance rates is justified based upon current
5 market pricing. The following provide some current market rates for DA in Washington:

- 6 ♦ Qwest charges \$1.25 for local DA
- 7 ♦ Sprint charges \$1.50 for local DA calls
- 8 ♦ AT&T/Comcast charges \$1.25 and has one call allowance
- 9 ♦ Verizon NW's rate would remain at \$.95 cents but call allowances would be
10 eliminated.

11
12 **Q. PLEASE DISCUSS VERIZON NW'S PROPOSAL TO INCREASE BASIC**
13 **RESIDENTIAL RATES BY \$9.80 PER MONTH?**

14 A. As stated earlier, Verizon NW took into account factors such as the current rates charged
15 by other companies, the Verizon NW calculated cost of service for residential service,
16 and the current market for this service. A survey of other ILEC rates in Washington
17 reveal that currently some customers are paying higher rates than those proposed by
18 Verizon NW. Verizon NW also looked at the cost that Mr. Collins developed for
19 residential service in comparison to the proposed rates, which shows a Verizon NW
20 calculated cost of \$38.36. As can be seen, the proposed rate of \$22.80 plus the current
21 subscriber line charge of \$6.50 still does not cover Verizon NW's calculated cost of
22 providing residential service.

23

1 **Q. IN PREVIOUS DOCKETS, THE COMMISSION HAS HELD THAT LOOP**
2 **COSTS ARE NOT PART OF THE COST OF PROVIDING BASIC SERVICE**
3 **BUT INSTEAD ARE “COMMON COSTS.” IF THE COMMISSION WERE TO**
4 **APPLY THIS POSITION HERE, WOULD VERIZON NW’S PRICING**
5 **PROPOSALS CHANGE?**

6 A. No. Verizon NW’s cost studies, which are sponsored by Mr. Collins, reflect that loop
7 costs are part of the direct cost of providing basic service. Verizon NW does not agree
8 that such costs are common. But even if loop costs were treated as common costs, all
9 such costs must be allocated to (and thus recovered from) basic services. This is because
10 market forces will not allow Verizon NW to recover loop costs from other services.

11
12 Furthermore, until its decision in the AT&T Access Complaint case, UT-020406, the
13 Commission had a long-standing policy that required Verizon NW to recover a
14 significant portion of its loop costs through access charges. In this way, the Commission
15 was able to keep the price for basic services lower than they otherwise should have been.
16 Given the Commission’s decision that access charges should no longer recover a
17 significant portion of loop costs, Verizon NW’s basic service rates must increase.

18
19 **Q. WHAT IS VERIZON NW’S PROPOSAL REGARDING INCREASES TO**
20 **LIFELINE CUSTOMER RATES?**

21 A. Verizon NW is not proposing to increase Lifeline rates in this filing. Verizon NW
22 proposes that the Lifeline revenue not recovered, associated with the R1 increases, would

1 be drawn from the Washington Telephone Assistance Program (WTAP) Fund. Lifeline
2 customers would not see an increase to their bills.

3
4 **Q. WHAT ISSUES NEED TO BE ADDRESSED IN REGARD TO THE WTAP FUND**
5 **AND VERIZON NW'S PROPOSAL TO INCREASE RESIDENTIAL RATES?**

6 A. Verizon NW has learned in discussions with the WTAP Fund Administrator and the
7 Commission Staff that a potential funding issue exists with the WTAP Fund. These
8 funding issues may require changes to the mechanics of the WTAP Fund. (e.g., how it is
9 funded, the ceiling on Lifeline rates, etc.)

10
11 Verizon NW is currently working with the Fund Administrator and the Commission Staff
12 to assess these Fund issues and explore options that may resolve these issues.

13
14 **Q. IF A SOLUTION CANNOT BE FOUND FOR THE WTAP FUNDING ISSUES,**
15 **WHAT OTHER OPTIONS ARE AVAILABLE?**

16 A. One option would be to reprice the current residential and business basic rates to provide
17 the revenue that would have been received from the Fund. However, Verizon NW is not
18 proposing this option and will continue to work with the Fund Administrator and
19 Commission Staff to develop a potential solution for the WTAP Fund.

1 **Q. PLEASE PROVIDE VERIZON NW'S PROPOSAL TO INCREASE BASIC**
2 **BUSINESS RATES BY \$9.80?**

3 A. Today the business rates, with few exceptions, cover their associated cost. Verizon NW
4 is proposing increases to these rates that will provide additional contribution in order to
5 minimize the increase to residential rates.

6

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

8 A. Yes.