**BEFORE THE**
**WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

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| VERIZON SELECT SERVICES INC.; MCIMETRO ACCESS TRANSMISSION SERVICES LLC; MCI COMMUNICATIONS SERVICES INC.; TELECONNECT LONG DISTANCE SERVICES AND SYSTEMS CO. D/B/A TELECOM USA; AND TTI NATIONAL INC., | ) | Docket No. UT-081393 |
| Complainants, | ) | |
| v. | ) | |
| UNITED TELEPHONE COMPANY OF THE NORTHWEST, | ) | |
| Respondent. | ) | |

**SURREBUTTAL TESTIMONY OF**

**CHRISTIAN M. DIPPON**

**ON BEHALF OF**

**UNITED TELEPHONE COMPANY OF THE NORTHWEST**

**d/b/a**

**EMBARQ**

**June 30, 2009**

## Contents

# I. QUALIFICATIONS AND SUMMARY

**Q.** ***Please state your name, occupation, and business address.***

**A.** My name is Christian Michael Dippon. I am a Vice President at the San Francisco office of NERA Economic Consulting (NERA) where I am an economist in the Communications practice. NERA provides expert economic and financial analysis for firms and government bodies on a wide variety of issues. My business address is 1 Front Street, Suite 2600, San Francisco, CA 94111. I filed responsive testimony on behalf of United Telephone Company of the Northwest (herein "United") in this proceeding on April 17, 2009.

**Q.** ***What is the purpose of this surrebuttal testimony?***

**A.** The purpose of my surrebuttal testimony is to respond to the:

- Rebuttal Testimony of Lawrence J. Bax on behalf of AT&T Communications of the Pacific Northwest, Inc., TCG Oregon, Inc., and TCG Seattle, Inc. (collectively AT&T)[1]
- Rebuttal Testimony of Dr. Kent A. Currie on behalf of AT&T[2]

[1] Before The Washington Utilities and Transportation Commission, Verizon Select Services, Inc.; MCIMetro Access Transmission Services, LLC; MCI Communications Services, Inc.; Teleconnect Long Distance Services and Systems Co. d/b/a Telecom USA; and TTI National Inc., *Complainants v. United Telephone Company of The Northwest*, Respondent, Docket No. UT-081393, Rebuttal Testimony of Lawrence J. Bax, on behalf of AT&T Communications of the Pacific Northwest, Inc., TCG Oregon, Inc., and TCG Seattle, Inc., June 5, 2009 (Bax Rebuttal).
[2] Before The Washington Utilities and Transportation Commission, Verizon Select Services, Inc.; MCIMetro Access Transmission Services, LLC; MCI Communications Services, Inc.; Teleconnect Long Distance Services and Systems Co. d/b/a Telecom USA; and TTI National Inc., *Complainants v. United Telephone Company of The*

– Rebuttal Testimony of Paul B. Vasington on behalf of Verizon Select Services Inc., MCIMetro Access Transmission Services LLC, MCI Communications Services Inc., Teleconnect Long Distance Services and Systems Co. d/b/a Telecom USA, and TTI National, Inc. (collectively Verizon)[3]

– Testimony of Glenn Blackmon on behalf of the Staff of Washington Utilities and Transportation Commission[4]

Specifically, I respond to the claims put forth by the witnesses for the other carriers in their rebuttal testimonies that the theoretical and empirical evidence put forth by United in this case is not defensible (Bax at 3), insufficient (Bax at 33), flawed (Currie at 78), and "unsupported and unsupportable" (Vasington at 18).[5] This is just some of the nomenclature used by AT&T's and Verizon's witnesses in their attempts to discredit the evidence presented by United and me in this case—evidence that does not support their employers' attempts to get a free pass on contributing to a universal service program in the State of Washington. I also respond to Dr Blackmon's testimony on behalf of the Staff of Washington Utilities and Transportation Commission (the Staff).

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*Northwest*, Respondent, Docket No. UT-081393, Rebuttal Testimony of Dr. Kent A. Currie, on behalf of AT&T Communications of the Pacific Northwest, Inc., TCG Oregon, Inc., and TCG Seattle, Inc., June 5, 2009 (Currie Rebuttal).

[3] Before The Washington Utilities and Transportation Commission, Verizon Select Services, Inc.; MCIMetro Access Transmission Services, LLC; MCI Communications Services, Inc.; Teleconnect Long Distance Services and Systems Co. d/b/a Telecom USA; and TTI National Inc., *Complainants v. United Telephone Company of The Northwest*, Respondent, Docket No. UT-081393, Rebuttal Testimony of Paul B. Vasington on Behalf of Verizon, June 5, 2009 (Vasington Rebuttal).

[4] Before The Washington Utilities and Transportation Commission, Verizon Select Services, Inc.; MCIMetro Access Transmission Services, LLC; MCI Communications Services, Inc.; Teleconnect Long Distance Services and Systems Co. d/b/a Telecom USA; and TTI National Inc., *Complainants v. United Telephone Company of The Northwest*, Respondent, Docket No. UT-081393, Testimony of Glenn Blackmon, Staff of Washington Utilities and Transportation Commission, June 5, 2009 (Blackmon Testimony).

[5] Unless otherwise stated, all references are to the rebuttal testimonies of Mr. Bax, Dr. Currie, and Mr. Vasington and to the testimony of Dr. Blackmon.

**Q.** ***Please summarize your assessment of the rebuttal testimonies submitted in this proceeding.***

**A.** In general, the witnesses' testimonies that I respond to are based on a misunderstanding of my position and/or the issue before the Commission in this proceeding. More specifically, they fail to utilize any United-specific information to support their proposals and choose to rely on other carriers' data that do not reflect the operating characteristics of United's service area and resulting cost structure. They also do not sufficiently take into account that a proposed reduction in access charges would pressure United to raise local rates. In areas where competition exists, this would increase the likelihood that United would lose access lines to intermodal competitors. In rural, high-cost and low-income communities, increases may not be sustainable and may be contrary to universal service policy goals, as I explain later.

In essence, AT&T and Verizon seek a reduction in intrastate switched access rates, which would improve *their* financial bottom line, but would be of little benefit to Washington consumers. If the Commission decides that access charge reform is appropriate, then it should do so as part of a balanced process that phases in over time greater pricing flexibility and an adequate universal service funding mechanism to allow United to meet its service obligations and to promote universal service throughout the company's service area.

## II. MR. BAX'S REBUTTAL ATTEMPT IS MISGUIDED

***Q. Please summarize Mr. Bax's rebuttal testimony.***

**A.** Mr. Bax testifies that no defensible arguments have been offered demonstrating that United's access rates should not be reduced and also characterizes (at 9) my testimony as saying that public policy goals cannot be met without implicit subsidies from access rates. This is wrong. Mr. Bax then attempts to revive his argument that United's intrastate switched access rates somehow are anticompetitive. Again, this is wrong. In fact, his explanation ignores that there is a subsidy element in intrastate switched access rates. The subsidy element can only have an anticompetitive impact if it provides United an unlawful advantage in competing for Washington subscribers. The only way this could happen is for United to engage in a price squeeze. However, as I explained in my responsive testimony (at 68), the opportunity cost of doing so makes this risk of a price squeeze virtually nonexistent. Mr. Bax continues (at 15) by claiming that affordability is not an issue, as competition would limit the sustainability of price increases. Mr. Bax also says (at 16) that competition is intense and increasing in the telecom industry. Thus, it would seem that Mr. Bax confirms my point that competitive forces would limit United's attempts to recover lost access revenue from all of its access lines, and the company would have to focus on subscribers in areas with limited competition—subscribers in rural, high-cost, and low-income communities.

Mr. Bax repeatedly cites from a paper that I coauthored.[6] In doing so, he attempts to show that my arguments in the paper are inconsistent with what I have argued in this proceeding and even I cannot justify maintaining the existing access rate levels and structure. Mr. Bax entirely misses the point and the quotes Mr. Bax uses were taken out of context. In short, the paper demonstrates that regulatory reform is imperative given the changes in the telecommunications sector and in competition for communications services. The paper shows that regulatory intervention of any type (e.g., cross subsidies) is inefficient *relative to a world without regulation*. Mr. Bax seems to have misunderstood this paper to say that regulatory intervention is inefficient *relative to his recommendation of reducing United's intrastate switched access rates to interstate levels.* Mr. Bax goes on and says (at 7) that intrastate switched access rates are priced higher than interstate rates as well as their underlying forward-looking incremental costs. My testimony in this case does not contradict this. Rather, it shows that, while the regulatory framework may be inefficient, excusing the IXCs from contributing to the social goals this Commission has established does not address the inefficiencies in the overall intercarrier compensation system—if anything, it makes the system worse. A comprehensive review and overhaul is needed, not a shortsighted and unbalanced quick fix.

Mr. Bax then goes on to reiterate the same arguments from his earlier testimony regarding the alleged benefits from reducing intrastate switched access rates. As before, however, he ignores the *costs* associated with the policy he proposes. As I have shown in

[6] As an aside, Mr. Bax obviously ignored the "Do Not Cite without Permission" stamp on this working paper as he

my testimony, while there might be minimal benefits, the costs far outweigh the benefits. Here also, Mr. Bax incorrectly claims that my testimony is inconsistent with the paper he cites. The parallels he attempts to draw between that paper and my testimony in this proceeding are wrong; thus, it follows that his criticism of my testimony is inaccurate.

***Q. Has United shown that its intrastate switched access rates are just, fair, and reasonable?***

**A.** Yes. Mr. Bax (at 3) claims to the contrary, but his claim is wrong. First, opposing parties have not demonstrated that United's existing intrastate access rates are unjust, unfair, and unreasonable as they allege. Moreover, when the Commission approved United's existing rates, it declared that they were just and reasonable. Further, I have presented substantial evidence addressing this point. See Section III of my responsive testimony, which is devoted to this subject.

***Q. Do carrier access charges priced above cost harm wireline toll consumers as claimed by Mr. Bax?***

**A.** No. Mr. Bax claims (at 3) that "the Embarq witnesses have not provided any evidence to show: … that these excessive rates [switched access] are not harming Washington wireline toll consumers.…" As I said in my responsive testimony (at 48), one could argue that any cost savings for long distance customers is a benefit, regardless of how small. However, any decrease in toll rates from a reduction in access charges would be

freely cites it.

insignificant when compared to the increases the consumers in United's operating areas would see if switched access rates were reduced.

**Q.** ***Mr. Bax alleges that you provide guidance as to why United's intrastate switched access rates should be reduced. Is this true?***

**A.** No. Mr. Bax states (at 4): "it seems indefensible that the implicit subsidies inherent in Embarq's intrastate switched access rates can be sustained." To support this statement, Mr. Bax inappropriately cites a working paper, coauthored by me, quoting passages from the paper entirely out of context and drawing parallels that are untenable. The paper addressed the following questions:

- Is regulation still necessary, redundant, or harmful?
- Where should regulation be directed, if at all?
- What form should it take—interventionist or passive?
- Who needs to be protected from whom?
- How can communications policy be used to improve social welfare

Generally, the paper explores how communications policy, and specifically intercarrier compensation, must evolve in order to adapt to changing industry circumstances. Thus, contrary to Mr. Bax's testimony, the paper did *not* address intrastate switched access rates, and it certainly did *not* address piecemeal reductions of intrastate switched access rates to interstate levels without any offsetting policy adjustments (as recommended by Mr. Bax). Consistent with the paper, my testimony in this case recommends holistic changes to Washington's intercarrier compensation system, rather than the piecemeal, self-serving approach recommended by AT&T and Verizon.

***Q. Are interstate access rates appropriate benchmarks for intrastate access rates?***

**A.** No. Mr. Bax continues making the same argument in his rebuttal testimony (at 6–7) that he tried to make in his direct testimony. That is, "Embarq's own interstate switched access rates are the most appropriate proxy as those rates can be demonstrated to be more than sufficient for the recovery of Embarq's access services costs.…"[7] As I have repeatedly explained, the FCC reduced interstate access charges in conjunction with the introduction of a federal universal service fund. Further, as I stated in my responsive testimony (Exhibit CMD-3 at 5): "The process of rebalancing interstate rates—that is, reducing interstate carrier access charges and increasing subscriber line charges—took place over more than two decades." I also explained (id. at 12) that state commissions can decide whether it is appropriate to fund universal service using carrier access charges and above-cost intrastate toll rates. That is, states can continue to use carrier switched access charges as a way of ensuring that providers of intrastate long distance services provide an equitable and nondiscriminatory contribution to fund universal service. The LECs in Washington contribute to universal service funding via subsidies implicit in their rates for toll and other services. It is important to note that the FCC during its access charge proceeding did not "attempt to identify state-level implicit universal service support …, nor did it try to convert such implicit mechanisms to explicit federal universal service

[7] Bax Rebuttal, p. 6.

support."[8] Contrary to what Mr. Bax appears to believe, the FCC did not reduce interstate access charges—the FCC created a universal service fund to make the subsidy element in *interstate* switched access rates explicit. Hence, only the combination of the *interstate* rate level with the *federal* fund is an appropriate benchmark.

***Q. Is it your contention that this Commission's policy goals cannot be met without the implicit subsidy flow from access charges?***

**A.** No. Mr. Bax claims (at 9) that I use Dr. Kahn's statements "as a means to support [my] contention that the Commission's public policy goals cannot be met without the implicit subsidies flows from access charges." This misconstrues my testimony. As I said in my responsive testimony (at 6), United's rates should remain in place until the Commission engages in a complete overhaul of the intrastate intercarrier compensation system, taking into consideration universal service requirements. Therefore, contrary to Mr. Bax's testimony, I have never claimed that the Commission's goals cannot be met without implicit subsidies.

***Q. Do you contend that Dr. Kahn supports the use of implicit, noncompetitively neutral cross subsidies?***

**A.** No, despite Mr. Bax saying (at 8–9) that this is what I imply, based on Dr. Kahn's writings, he does not seem to.

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[8] P.W. Huber, Michael K. Kellogg, and John Thorne, *Federal Telecommunications Law, Second Edition*, Aspen Law and Business, Gaithersburg, New York, 1999, p. 589.

**Q.** ***Do you support the use of implicit, noncompetitively neutral cross subsidies?***

**A.** No. Mr. Bax draws the conclusion (at 10) that "Dr. Kahn does not support implicit, non-competitively neutral cross-subsidies" and implies that I do. However, I do believe that if eliminated those subsidies must be replaced with explicit subsidies.

**Q.** ***Is it appropriate to cite Dr. Kahn to support the reduction of intrastate switched access rates to the interstate levels proposed by Mr. Bax?***

**A.** No. First, Dr. Kahn explains how access charges were set historically (and are set today, at least in those states that have not yet established a universal service fund):

> [T]he carrier access charge has always been directly regulated, explicitly set by utility commissions, including the FCC, at levels intented to be no higher than sufficient to afford the LECs a reasonable opportunity to recover their aggregate regulatorily determined revenue entitlements.[9]

Second, in discussing MCI's position that "the size of the markup in the access charge should be reduced to take into account the net revenues that the LECs may reasonably be expected to earn from such other offerings as vertical, video and, eventually, interLATA services,"[10] Dr. Kahn stated:

> The last of these suggestions is particularly incongruous—indeed, outrageously self-serving. It would clearly be inconsistent with efficient competition in the *unregulated* markets—specifically, it would handicap the LECs in that competition—if they alone had to continue to charge rates above competitive levels for those offerings because regulation was requiring them

[9] Alfred E. Kahn, Letting Go: Deregulating the Process of Deregulation, or: Temptation of the Kleptocrats and the Political Economy of Regulatory Disingenuousness, Institute of Public Utilities and Network Industries, The Eli Boroad Graduate School of Management, Michigan State University, East Lansing, Michigan, MSU Papers 1998, p. 106.
[10] Id, p. 113. Dr. Kahn summarizes an argument in MCI's comments in the FCC access reform proceedings.

> to rely on those contributions to recover the legitimate costs of regulated operations.[11]

Dr. Kahn also stated in connection with markups to retail services:

> Just as the access charges, both intra- and interstate, have been a means of continuing the necessary flow of contribution from long-distance services, so have the overpricing at the state level of vertical services and of dialtone to businesses, particularly in concentrated metropolitan areas.…
>
> The point of these mark-ups, it is worth re-emphasizing, is not merely to afford the ILECs an opportunity to recover their total costs and to continue the regulatorily-prescribed cross-subsidization. It is also, by imposing on their challengers the same proportionate burdens as they have themselves been forced by regulation to bear, to eliminate the invitation to inefficient competition in the provision of the overpriced services extended by the present distorted rate structures.[12]

Based on Dr. Kahn's above-cited previous statements, I do not think he could ever be cited to support the reduction of a subsidized service absent a replacement mechanism for the subsidy contribution portion.

**Q.** ***Please respond to Mr. Bax's attempt to explain why United's current access rate levels provide the company with a competitive advantage over IXCs.***

**A.** Mr. Bax again fails at his attempt (at 10–12) to restate his initial claim that United's current intrastate switched access rates give United a competitive advantage. While Mr. Bax now recognizes the need to define the market and identify the type of advantage where he alleges the advantage exists, this does not cure the original flaw in his

[11] Id., p. 114.
[12] Id., pp. 115–116.

reasoning. His price squeeze argument finds no support in economics, as shown in my responsive testimony at 68.

Moreover, I seriously doubt that the Washington Commission would have approved rates that embodied a subsidy if by doing so United would have been provided an opportunity to engage in a price squeeze because according to the Telecommunications Act of 1996 such subsidies are forbidden.[13]

**Q.** ***Could it ever be the case that the access rate reduction will be borne by all subscribers equally?***

**A.** Only if this Commission were to implement a state specific universal service fund that required all wireline subscribers to contribute an equal amount.

**Q.** ***Is it meaningful to compare United's local rates to Verizon's?***

**A.** No. Mr. Bax suggests (at 15) that, since United's average rates are below Verizon's average rates, there "is some opportunity to increase Embarq's end-user retail rates as a means to offset any revenue reduction resulting from intrastate switched access reform." As I stated above, I do not argue with Mr. Bax's position that there is "some opportunity" for United to sustain price increases in competitive areas. However, I disagree with Mr. Bax that Verizon's rates provide a meaningful benchmark. First, Verizon's operating areas in Washington are different from United's. Thus, it cannot simply be inferred that

[13] 47 U.S.C. § 254(k)

United's customers would react in the same way as Verizon's customers. Second, Mr. Bax did not examine whether Verizon's rates were sustainable. Verizon, like all other ILECs, is losing access lines, and Mr. Bax provides no evidence that the relatively higher prices did not cause Verizon to lose a disproportionate amount of lines. Third, as explained below, United's operating area characteristics, for example, population densities, are very different than those of Verizon; hence, its costs and the costs of meeting its COLR obligations are likely very different as well.

***Q. Do you agree with Mr. Bax that this Commission should not be concerned with price increases?***

**A.** No. Mr. Bax claims (at 15), "there is no need for intense regulatory concern with regard to local exchange service rates when competition exits." Essentially, Mr. Bax states that competition can limit price increases. First, this seems inconsistent with his previous claim that United can raise the prices on all of its lines. Second, Mr. Bax in effect confirms my previous testimony. That is, United would not be able to increase prices in areas that are competitive, and then it would be forced to seek price increases in noncompetitive areas.

***Q. Mr. Bax (at 16) says that competition is intense and increasing and exists in the form of cable operators, wireless carriers, and VoIP providers. What do you say to that?***

**A.** Mr. Bax simply confirms my testimony that the IXCs are losing revenue not because of the ILECs, but because of competition from cable, wireless, and VoIP providers. More importantly, reducing intrastate switched access rates likely would not significantly affect this trend because wireless operators offer "free" long distance as part of their service bundles.

**Q.** ***Would customers who purchase wireline bundles not be affected by a rate increase?***

**A.** No. Mr. Bax states (at 18): "a large number of customers who currently purchase bundled telecommunication service packages likely will not be affected by any increase in the basic service rate because bundled packages are already subject to greater competition." However, Mr. Bax offers no evidence to support his claim. Moreover, his assertion does support the point I made in my responsive testimony (at 62)—not only would United need to focus its price increases on subscribers in high-cost rural areas (where there is less competition), but it would have to focus on subscribers that have stand-alone local exchange service. Hence, essentially Mr. Bax's own analyses confirm my findings that reducing intrastate switched access rates would benefit the IXCs at the cost of subscribers in high-cost rural areas and those with stand-alone local exchange service—the customers with few competitive alternatives. Interestingly, even though he seems to agree with my findings, Mr. Bax describes (at 32) these consequences as "bleak and grossly inaccurate."

**Q.** ***Does Mr. Bax identify how United is to recover the loss of access revenue?***

**A.** No. At first, it seems that Mr. Bax advocates (at 15) that the access revenue loss should be spread over all revenue producing access lines. Then he states (at 18) that the Commission should not be worried about price increases because "rebalancing by way of local retail rates does not necessarily mean that rates will automatically or immediately increase." This begs the question: How can United compensate for its loss of access revenue? In his direct testimony (at 25), Mr. Bax states that "Embarq should be permitted the opportunity to offset any reductions to its intrastate switched access services revenues by way of its end-user retail services, as was the opportunity availed to other providers, and to the extent necessary, with explicit and competitively neutral access replacement support." Now, it seems that Mr. Bax is saying that United cannot offset any reductions "by way of its end-user retail services." Therefore, one can only conclude that Mr. Bax is recommending to this Commission to allow United to offset the proposed reductions "with explicit and competitively neutral access replacement support."

***Q. Should United be allowed to offset the proposed reductions with explicit and competitively neutral support?***

**A.** Yes. As I stated in my responsive testimony (at 60–61), if this Commission supports the access rate reductions proposed by AT&T or Verizon, then it must establish a state-specific universal service fund.

***Q. Do you support maintaining the existing implicit, noncompetitively neutral cross subsidies?***

**A.** Not necessarily. I would prefer to see all implicit subsidies made explicit through a universal service fund and additional pricing flexibility. Mr. Bax grossly misrepresents (at 20) my testimony by claiming that "Embarq witness Dippon attempts to argue in support of maintaining the existing implicit, non-competitively neutral cross-subsidies." Mr. Bax is mistaken. I stress that I do not support the complex system of subsidies that my colleagues Dr. Ware, Dr. Taylor, and I describe in the white paper attached to my responsive testimony (see Exhibit CMD-3). I believe in a comprehensive, holistic approach to intercarrier compensation reform and the provision of universal service at affordable rates. Mr. Bax, however, offers no such solution. All he proposes is that the IXCs be excused from contributing to the universal service objectives, which are targeted for Washington consumers so they have a ubiquitous network at affordable rates. The self-serving solution offered by AT&T offers no remedy to the existing system. If anything, it makes matters worse. What I did say in my testimony relative to Mr. Bax's solution is that maintaining the current system produces a superior outcome than his solution.

***Q. Is it possible for this Commission to lower intrastate switched access rates without making matters worse?***

**A.** Yes, as long as a universal service fund is established and United is given additional pricing flexibility before a reductions are allowed to take effect. As detailed in my responsive testimony, this Commission could reduce United's intrastate switched access rates if, and only if, it provides the company with the "explicit and competitively neutral access replacement support" to which Mr. Bax alludes. Specifically, this Commission can reduce intrastate switched access rates as long as it *simultaneously* introduces a state-specific universal service fund. As stated, if the Commission finds that a price increase in high-cost rural areas of Washington is appropriate, it can also provide United with sufficient pricing flexibility that allows the company to raise its rates in these areas.

**Q.** ***Do the benefits of reducing intrastate switched access rates outweigh the costs?***

**A.** No. There is no evidence to suggest that Verizon and AT&T would voluntarily flow through any of the cost savings to their long distance customers. Even if they did, the effects would be negligible and would not nearly justify the costs of a reduction in switched access rates, as I explain later when I rebut Dr. Currie. I am rather curious as to how Mr. Bax plans to fund all the benefits he claims (at 29) will come in the long term to consumers. Essentially, he too argues for access charge reform; however, his idea is to immediately reduce intrastate switched access rates before the other aspects of access reform have been implemented. Genuine access reform means more than reducing one rate to satisfy one subset of service providers and requires that the benefits of access charge reductions be balanced against the costs.

**Q.** ***What costs do you mean?***

**A.** The reduction of switched access rates absent a means of recovering the lost revenue would jeopardize universal service policy goals and likely force the ILECs to make large price increases in high-cost rural areas and to low-income subscribers. I described these costs in detail in my responsive testimony (at 57–63).

***Q. Who does Mr. Bax propose should pay for these costs?***

**A.** Mr. Bax's testimony (at 15) recommends that United's subscribers should be solely responsible for funding any social programs. Mr. Bax contests (at 33) my argument that rural customers likely would be the ones to suffer the consequences of a reduction in switched access rates absent a mechanism to compensate United for the lost revenue. He says (id.) that "rural customers are not being asked to 'subsidize themselves.'" He continues by saying, "***all*** of Embarq's customers are being required to contribute equitably to the costs of their services." With this statement, Mr. Bax makes it clear that he thinks the IXCs no longer should be required to contribute to universal service programs. Rather, he thinks it is fair and equitable that all of United's customers should be required to pay for the costs of providing service to those subscribers in United's area that are the recipients of regulatory mandated social programs—programs that United was and is required to provide and for which the government up until now has ensured that United is compensated for providing. Moreover, Mr. Bax's argument seems at odds with Section 254(b)(4) of the 1996 Act where it was made quite clear that "[a]ll providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service."

***Q. Do you agree with Mr. Bax that AT&T's toll volume decreased?***

**A.** This is generally consistent with my prior testimony. Specifically, I stated in my responsive testimony (at 39–40) that the IXCs' toll volumes decreased, but not because of switched access charges. The decrease is largely due to increased fixed-to-mobile substitution as well as the increased availability of substitutes for wireline service, such as the "free" long distance calling offered by wireless, cable, and VoIP service providers.

**Q.** ***Do you believe that the IXCs' toll volumes will increase if access rates are reduced?***

**A.** While I do not have current own-price elasticities for the IXCs' toll services, I would not anticipate that a decrease in access rates would have a measurable impact on the declining trend found by both Mr. Bax and me. There are several reasons for this. First, while I understand that AT&T would be willing to eliminate its $1.40 monthly In-State Connection Fee to reflect material changes in statewide access unit costs,[14] such a price reduction is likely too small to compete with free long distance offered by the wireless carriers. Second, the wireless carriers attribute their success, at least partially, to the added convenience of mobility. IXCs (and ILECs) cannot offer that. Finally, to use Mr. Bax's words (at 29), wireless and other alternatives to wireline long distance are "convenient, feature rich, and have never been more affordable."

**Q.** ***Do you believe that jeopardies and arbitrage opportunities associated with implicit subsidies exist outside of this proceeding?***

**A.** Mr. Bax states (at 27) that I believe "[o]utside of this proceeding … Embarq witnesses believe there are jeopardies and arbitrage opportunities associated with implicit subsidies." Mr. Bax seems to imply that my opinions are different in this proceeding, which is not the case. Implicit subsidies do come with the risk of arbitrage, and that is a

[14] See AT&T's Responses to Embarq's Second Set of Discovery Requests, ATT 2-53.

well-known and documented fact. However, it does not imply that reducing intrastate switched access rates to interstate levels without providing United with an adequate recovery mechanism is a superior solution to this risk. In fact, it makes matters worse, as I detailed in my responsive testimony (at 83).

***Q.*** ***Are AT&T's retail rates reflective of Washington ILECs' intrastate switched access rates, as Mr. Bax argues (at 28)?***

**A.** No. While AT&T's retail rates may factor to a small degree into its intrastate rates in Washington, little if any of the difference in intrastate switched access rates appears to be reflected in AT&T's retail rates because—with the exception of certain surcharges—its rates do not change from state to state. This was explained in my responsive testimony (at 47 and Exhibit CMD-4).

***Q.*** ***Will the reduction of intrastate switched access rates ensure that consumers in high-cost rural areas have access to uninterrupted, high quality telecommunications services?***

**A.** No. Mr. Bax makes (at 29) the rather vague argument that lowering intrastate switched access rates will somehow benefit high-cost rural subscribers "over the longer term." This argument makes no sense. Essentially, Mr. Bax seems to argue that increasing local exchange rates in high-cost rural areas is beneficial because it increases the quality of toll service in these areas. This seems to be in direct conflict with previous policy goals that supported both the availability and affordability of local exchange service, not toll service. Not surprisingly, Mr. Bax offers no support for this rather odd claim.

**Q.** ***Do you agree with Mr. Bax that switched access demand will inexorably decline to a level close to zero?***

**A.** Not necessarily. Mr. Bax states (at 29): "switched access demand—and hence, the implicit subsidies contained in high intrastate switched access charges—will inexorably decline to a level close to zero." I am not sure that the downward trend will ever approach zero. However, Mr. Bax is correct that access demand will continue to decline. This is exactly why reducing intrastate switched access rates will not increase competition, nor will it benefit consumers. Second, if Mr. Bax is correct, this would mean that intrastate switched access rates must be *increased* as fewer people contribute (cross subsidize) to the costs of serving subsidized customers.

**Q.** ***Is it untenable to leave the current rates as they are, as Mr. Bax argues (at 30)?***

**A.** No. As I mentioned above and in Exhibit CMD-3 of my responsive testimony, the FCC left it up to the states to determine how to handle the issue of universal service—to the extent that a state commission decides that it is appropriate to fund universal service using carrier access charges and above-cost intrastate toll rates, it can do so. While outdated and in need of an overhaul, it is not untenable to leave the current intrastate switched rates as they are. It is, however, untenable to reduce access rates without first providing for recovery of the costs associated with providing the service. First, parties arguing for a rate reduction have not been able to prove that United's rates are unjust or unreasonable. Second, relative to the remedies offered by AT&T and Verizon, the current system of subsidies is superior. It is infinitely superior to AT&T's proposal to reduce intrastate switched access rates to the "interstate level and structure including elimination of the Carrier Common Line Charge and the Interim USF Additive." AT&T thinks that the Commission should allow "Embarq … the opportunity to offset reductions in revenues *by way of increases to its rates for local end-user revenue*," (Bax at 30; emphasis added). Mr. Bax continues (at 31) by saying that AT&T only wants to "direct the costs toward the cost causer … without regard to geography and/or income." This destroys the entire intercarrier compensation system, defeats the universal service policy goals, and is contrary to the intent of the 1996 Act.

***Q. Do you agree that a transition period needs to be considered if any action is taken, as Mr. Bax mentions (at 30)?***

**A.** Yes. This is crucial. Much like the FCC did at the federal level, any reduction in access rates must be simultaneously balanced with the introduction of a state universal service fund. Furthermore, to avoid rate shock, the reduction of switched access rates and the introduction of a state USF should be phased in.

**Q.** ***Do you think that additional pricing flexibility is a meaningful way to recover the proposed access rate reduction, as suggested by Mr. Bax (at 31–32)?***

**A.** Not by itself, but in conjunction with a state-specific universal service fund and sufficient time to implement such new programs it is a definite start in the right direction. Pricing flexibility and other parameters are complementary components of a state-specific USF. Thus, pricing flexibility should be determined along with the other parameters for the state USF. For instance, the Commission will need to decide on how to set up the fund, who contributes to the fund and how much, who draws from the fund and how much, what is the appropriate benchmark, and how should the benchmark be adjusted over time. In determining who draws and how much from the fund, the Commission will need to consider current rates and adjust those rates by sustainable pricing flexibility, if such should be granted in this context.

## III. DR. CURRIE PRESENTS A ONE-SIDED ANALYSIS

**Q.** ***Please summarize your view of Dr. Currie's rebuttal testimony.***

**A.** Because most of Dr. Currie's rebuttal testimony addresses testimony by other United witnesses, I speak to only the parts that address my testimony. To support his colleague Mr. Bax, Dr. Currie cites (at 71) to the economic literature that he alleges has found that access charge reductions "generally flow through to consumers in the form of decreased prices for long distance services." There are two problems with this assertion. First, most of the studies cited in Dr. Currie's literature review were written prior to the advent of wireless and VoIP providers as strong competitive forces in telecommunications markets. These types of carriers were not even in the picture when these studies were performed and often do not pay switched access charges. Hence, the effect of access charge reductions in the literature Dr. Currie cites overstates that effect today. Second, the access charge reductions in the studies cited by Dr. Currie were (with one exception) to *interstate* access charges and were applied by *all* local exchange carriers.[15] These reductions affected all long distance carriers in all states; their effect on the cost of an average interstate toll call was quite pronounced. In contrast, the effect of an intrastate carrier access charge reduction by one small carrier in one state on the cost of an average toll call is arithmetically negligible.

Dr. Currie also reports (at 76) a regression in which he examines the correlation between intrastate long distance average revenue per minute (ARPM) and intrastate access charges per minute of use as charged by the largest ILEC in the state. Taken literally, this regression merely demonstrates the uncontroversial fact that, in a competitive market, a nearly *market-wide* reduction in carrier access charges will lead to a reduction—not necessarily a full pass through—in toll prices. Economically, a reduction in the carrier access prices of the largest ILEC in each state would have a significant effect on the incremental cost of the average toll call in that state. However, in the current case, the carrier access charge reduction Dr. Currie proposes *will not be market-wide*: it will not apply to toll carriers that can avoid to a certain extent carrier access charges (wireless,

[15] Also, the FCC required that the IXCs pass through the access charge reductions in their interstate toll prices as part of the CALLS decision: Access Charge Reform, Sixth Report and Order, CC Docket No. 96-262 (released May 31, 2000).

VoIP) and it will *not* apply to the largest ILEC in any state. Hence, Dr. Currie's regression is not valid in the current context. In addition, his analysis fails to account for other variables that could affect toll rates—that is, he uses carrier access charges as the only independent variable, thereby omitting important determinants of toll prices and demand. In addition he uses only a partial representation of carrier access charges—one that omits transport and tandem switching elements. Finally, the measure of toll prices that he uses appears to be average revenue per minute (ARPM), which can be affected by many differences from one state to the next—for example, different mixes of residential and business customers, differences in whether AT&T is the predominant local carrier—which could affect the level of ARPM. Thus, his results, even if plausible as a matter of theory, cannot be used to estimate the impacts of a change in United's carrier access rates in Washington. Finally, Dr. Currie concludes by stating that there are benefits to access rate reductions and that excessive rates harm consumers. Much like Mr. Bax, Dr. Currie opts to examine only the purported benefits of an access rate reduction, completely ignoring the costs caused by such action. Hence, his analysis is at best incomplete.

***Q. Dr. Currie claims (at 71) that "reductions in access charges generally flow through to consumers in the form of decreased prices for long distance services." Do you agree with his claims on this issue?***

**A.** I disagree with Dr. Currie's claim (at 71) that "substantial evidence exists" demonstrating his point. The evidence he cites applies to market-wide access charge reductions, and that is not what is being proposed here. It may be true, as he states (at 73), that an "IXC can be expected to pass through at least some of any future access charge reductions." The economics imply that, in competitive markets, an IXC would pass through in the form of a lower price a portion of the reduction in the marginal cost of the average toll minute sold at that price. However, in contrast to the previous market-wide access charge reductions that Dr. Currie's citations examine, the proposed intrastate access charge reductions would not apply across the market, even for intrastate toll services. Calls that originate or terminate outside of United's service territory would not experience an originating or terminating access charge reduction. Thus, the average toll minute sold even by a wireline IXC would experience only a tiny reduction in its incremental cost.[16] Thus, the information and citations he provides do not establish that the IXCs will pass through most of the potential reductions in United's access charges, and the size of the potential reductions are unlikely to outweigh the costs to consumers of the unbalanced policy recommended by AT&T.

**Q.** ***What is your assessment of the literature on carrier access charges cited by Dr. Currie?***

**A.** Most of the papers he cites examine data from the 1980s and early 1990s. During that era, MCI and Sprint were seeking to capture market share from AT&T, and the FCC was changing the interstate carrier access charge regime. Thus, there were competitive and regulatory pressures on AT&T to pass through interstate carrier access charge reductions. The studies generally pertained to evidence prior to the advent of wireless and cable providers as a strong competitive force in the provision of local exchange services. In

[16] For three reasons. First, most intrastate toll calls in Washington originate or terminate outside of United's service territory. Second, many IXC toll services price toll minutes without regard to jurisdiction (i.e., intrastate or interstate), and a small reduction in the incremental cost of an intrastate toll minute would represent a much smaller

addition, most of the studies focus on interstate access and toll prices, and the changes in interstate access charges had a much more widespread impact on all carriers competing at the time of the studies. Therefore, there are too many variables for this evidence to be used to support any decision by the Commission in this case.[17]

***Q. Dr. Currie cites (at 71) a study by Lester Taylor and William Taylor. What did that study find?***

**A.** Taylor and Taylor found that there was less than one-for-one pass-through of access charge reductions—as indeed there would be even if long distance were a monopoly.[18] More to the point, the access charges that were reduced over the period studied by Taylor and Taylor were across-the-board interstate carrier access charge reductions—offset by FCC-mandated increases in the subscriber line charge—at a time when carriers sold interstate long distance service by the minute, which is no longer the case. Long distance is mostly supplied today in packages in which intrastate toll service is not priced separately from interstate toll service and is often not priced on a per minute basis. A large share of current toll service is also provided today by carriers that can avoid paying switched access charges and whose incremental costs—and prices—will be totally unaffected by a reduction in United's intrastate carrier access charges.

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reduction in the incremental cost of the average toll minute priced by the service. Third, wireless and VoIP carriers do not pay switched access charges.

[17] Dr. Currie cites four studies. Data in those studies range from 1984 to 1998: Taylor and Taylor: 1984–1992, Taylor and Zona: 1984–1995, Crandall and Waverman: 1987–1993, and Beard et al.: January 1997–July 1998.

[18] William E. Taylor and Lester D. Taylor, "Postdivestiture Long-Distance Competition in the United States," *American Economic Review* 83 (2), May 1993, p. 52.

**Q.** ***Do you agree with Dr. Currie's summary of the study by Drs. Taylor and Zona?***

**A.** Again, Dr. Currie recognizes: "This study found that AT&T's nominal toll prices for interstate services generally fell, *but not by as much as access charges fell*." (Currie at 72; emphasis added.) And, the interstate access charge reduction applied to all providers of interstate carrier access services, so that the access charge reduction led to a reduction in the incremental cost of the average interstate toll minute provided in the market. That result—that lower access charges lead to lower toll rates—does not apply in the case at hand because the incremental cost of the average toll minute supplied by toll carriers in Washington will be essentially unchanged by a reduction in United's access charges.

**Q.** ***Does Dr. Currie omit caveats provided by Drs. Crandall and Waverman in their analysis of intrastate carrier access charges?***

**A.** Yes. Although Dr. Currie states (at 72): "Crandall and Waverman determined that reductions in intrastate switched access fees were associated with a reduction in AT&T's tariffed intrastate interLATA toll rates," he fails to mention that their results were not straightforward. They found that carrier access charge reductions for the higher mileage bands were passed through, and they concluded that the market was relatively competitive; however they also noted that:

> … between 1987 and 1991, the average inter-LATA rate net of access costs rose in the first three mileage bands, but declined in the longest seven mileage bands. Unfortunately, we do not have data on the number of minutes in each mileage band. Between 1991 and 1993, however, only the largest two mileage band evidenced a decline in gross margins (price net of access costs). This

> appears consistent with MacAvoy's observation that in the interstate jurisdiction AT&T's margin's have increases.[19]
>
> Unfortunately, there are no available data on the minutes of use by mileage band by state for the inter-LATA market. Without these data we cannot weigh prices by mileage band to arrive at an *average* price. We therefore cannot know the degree to which AT&T passed on access cost differences or decreases, on average across all mileage bands.[20]

In addition, the access price reductions in the study reduced the incremental cost of the average toll call, which the access price reductions under consideration here do not.

***Q. Please discuss how recent changes in competition have affected the relevance of the studies cited by Dr. Currie and the prospects that changes in United's carrier access charges will result in any meaningful toll price reductions.***

**A.** Dr. Currie's statement (at 75) that the "benefits of lower access rates through past access charge reform decisions at the federal level have already been documented" is correct, but those access charge reductions are different from the ones proposed here. Reducing United's intrastate access charges in today's environment does not necessarily mean that any toll price will fall. The literature Dr. Currie cites examines reductions in interstate carrier access charges by all local exchange carriers across the entire U.S. A reduction in intrastate carrier access charges for United would lower AT&T's or Verizon's average carrier access charge by an almost negligible amount because the proportion of AT&T (or Verizon) intrastate long distance calls that originate or terminate in United's Washington territory is very small.

[19] Robert W. Crandall and Leonard Waverman, *Talk is Cheap: The Promise of Regulatory Reform in North*

I agree with Dr. Currie (at 77–78) that toll is a comparatively price-elastic service and that economically efficient (Ramsey) prices would exceed their incremental costs to a lesser extent than for less price-elastic services. However, because carrier access charges are only a fraction (maybe 50 percent) of the incremental cost of long distance, the effect of a 10 percent decrease in the carrier access price *even for all calls* would be a smaller (maybe 5 percent) reduction in the incremental cost of long distance service. And, not all of that cost reduction would be passed through in the form of lower toll prices.[21] Thus, the reduction in demand for long distance services and the allocative inefficiency that Dr. Currie laments (at 77) is not as severe as he implies. Moreover, the fact that a reduction in United's Washington intrastate carrier access charges would have a negligible effect on the incremental cost of the average toll minute as sold in the market means that the proposed access charge reductions would lead to a negligible gain in economic efficiency. Finally, there is no evidence that demonstrates, even if a nominal increase in long distances prices were warranted, that AT&T or Verizon would raise prices at all in Washington.

***Q. Will consumers make more toll calls if United's switched access rates are reduced?***

**A.** I cannot say for certain with the data available, but I doubt that the effect would be large. Dr. Currie is concerned only with wireline IXCs, in particular with AT&T's decreasing call volumes. Contrary to Dr. Currie's argument (at 77), in today's environment, the

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*American Telecommunications*, Washington DC: The Brookings Institution, 1995, p. 153.
[20] Id., p. 161.

intrastate carrier access charge reductions proposed by AT&T are not likely to stimulate toll demand (or the derived demand for carrier access) by very much because:

1. As explained above, access charges are only a portion of the cost of toll and only a portion of the reduction in cost might possibly be passed through to end users in the form of lower toll prices.

2. Carriers price their toll within a broader market than the subset of intrastate toll calls affected by United's carrier access charges. That is, they factor in the access prices of other carriers because they set their toll prices over a larger area than that to which United's access prices apply, and they sell packages that mix at least various types of toll usage in bundles with fixed prices or uniform prices per minute.

3. Wireless firms, which carry a large share of toll traffic today, would not see any meaningful reduction in their input costs; thus, there would be less pressure on the IXCs to reduce their toll prices than there would be if all toll carriers saw lower access costs.

So, a modest decline in United's carrier access charges will have less of an impact on toll call demand than in the studies cited by Dr. Currie because the relevant toll market is much larger than the relatively small set of calls affected by changes in United's intrastate access charges.

[21] I agree with Dr. Currie (at 73) that "[a]n IXC can be expected to pass through *at least some* of any future access reductions.…" (Emphasis added.) However, it is far from certain that they will pass through all or even most of those (proposed) reductions.

**Q.** ***Does Dr. Currie's efficiency argument factor in all of the relevant changes in price and impacts on customers?***

**A.** No. Dr. Currie's allocative efficiency argument (at 77) ignores the need to balance the potential (and likely small) gains from reducing toll rates against social welfare considerations like universal service and COLR and against the allocative efficiency losses that would be likely if the Commission implements a piecemeal approach like that recommended by AT&T. I agree that allocative efficiency requires that users pay rates based on the true cost of the resources they use and producers match supply and demand at the margin. Prices in a fully competitive market with no other considerations would be controlled by market forces that promote allocative efficiency. In addition, there may be losses of allocative efficiency in a market where some prices are deliberately set above cost (switched access) and others (basic local) are set below cost to meet social goals. If the underpricing of local service increases consumer surplus because of the increased network size, then the overall effect of the pricing plan (including local exchange, carrier access, and toll prices) may be to enhance allocative efficiency. In other words, if the larger network expands the number of calls by expanding the number of lines on the network, the efficiency gains from additional calling may outweigh the allocative efficiency losses associated with higher toll prices.

And, as discussed above, a modest decline in United's intrastate carrier access charges would have less of an impact on toll call demand than it would have if the relevant market were confined to the relatively small set of calls affected by United's intrastate access charges.

**Q.** ***Dr Currie suggests that your regression somehow suggests that United has monopoly power. Is his argument correct?***

**A.** No. According to Dr. Currie (at 79), my regression results merely reflect the "unique circumstances that characterize switched access." He appears to claim that my regression shows no correlation between access charges and access usage for United because IXCs need to use LEC networks to reach a customer that uses the LEC's local service and that there are "constraints [that] make it unlikely for the IXCs to pass through access charges on [a] LEC-specific basis" to their long distance customers. However, those circumstances have nothing to do with my "no correlation" regression result.

My regression results showed that across Embarq's 21 operating companies, the demand for Embarq intrastate switched access minutes is unrelated to the prices charged for switched access. The fact that higher switched access charges (in the sample) were not associated with lower switched access demand means that users of switched access (IXCs) in Embarq's service territories did not substitute away from IXC toll services in response to higher carrier access charges. Dr. Currie does not dispute this finding. Rather, he explains it on the grounds that differences in Embarq's carrier access prices across its operating territories have little impact on the final toll price because the toll price paid by consumers "averages and blends the impact of access rates assessed by all LECs, not just Embarq." To which list he could add the fact that the toll price paid by consumers also averages and blends interstate toll prices as well as toll prices charged by competitors that do not pay carrier access charges. Thus, as Dr. Currie acknowledges (id.), "it comes as no surprise that Mr. Dippon finds no correlation between the switched access minutes sold by Embarq and Embarq access rates."

Irrespective of why United's switched access minutes are unaffected by United's switched access rates, the fact that they are uncorrelated—a fact with which Dr. Currie apparently agrees—tells us that a reduction in United's intrastate carrier access charges will not stimulate demand for United's intrastate carrier access minutes and thus for the IXCs intrastate toll service that originates or terminates in United's service territory. There will be no gains in economic efficiency for United customers from lower toll prices or expanded toll usage stemming from the proposed reduction in United's intrastate switched access rates. Moreover, as Dr. Currie tells us (at 79), there would be little effect on economic efficiency outside of Embarq's service territory because:

> The actual price signal that the IXC's consumers get is from the toll price which averages and blends the impact of access rates assessed by all LECs, not just Embarq.

And, the toll price in question involves interstate as well as intrastate calls and is affected by carriers that do not pay switched access charges.

In weighing the costs and benefits of the proposed reduction in United's intrastate switched access charges, the costs—described below—fall on telephone subscribers (and potential subscribers) in United's service territory in Washington. However, my regression results imply—and there appears to be agreement—that those subscribers do not receive the putative benefits from United's reduction in intrastate carrier access charges. Indeed, because the effect of those lower carrier access charges is a negligible reduction in the incremental cost of an average toll minute, there would be negligible efficiency gains from lower toll prices throughout the toll market.

***Q. Does Dr. Currie's discussion of the likely small impact of a reduction in United's carrier access charges on toll demand refute your regression analysis?***

**A.** No. The point of my regression was to test whether there was a statistically significant relationship between higher intrastate access rates and lower levels of toll usage by customers, and I did so by seeing if there was a statistically significant relationship between carrier access minutes—which provide a reasonable proxy for toll minutes—and carrier access prices, holding other relevant variables constant. If there were a relationship, one would expect that lower toll prices would lead to greater usage by customers. However, my analysis shows that there was not a statistically significant relationship between those two variables, and claims that lower toll prices and expanded toll demand would lead to efficiency gains are incorrect.

## IV. MR. VASINGTON OFFERS NO NEW EVIDENCE

***Q. Please summarize your view of Mr. Vasington's rebuttal testimony.***

**A.** Mr. Vasington offers no new arguments in his rebuttal testimony. Rather, he takes this opportunity to disagree, almost point-by-point, with all the testimonies submitted by United's witnesses. Mr. Vasington's assertions are either wrong or one-sided. In addition, his analyses are incomplete and do not establish his claims that United's access charges are excessive or anticompetitive. While he complains that my criticisms of the conceptual flaws in his analysis are too theoretical, Mr. Vasington offers no empirical evidence disproving the accuracy of the allegedly too theoretical arguments.

His first line of rebuttal is to claim (at 5) that United's contribution analysis is "fundamentally flawed." I offered no testimony that directly addressed the "contribution analysis," as Mr. Vasington describes United's loop cost allocation method; nevertheless, he claims that I contradict Mr. Roth's testimony. His claims are wrong. Mr. Vasington then dedicates an entire section (Section III) of his testimony explaining why I allegedly failed "to engage Verizon's evidence about the unreasonable and anticompetitive nature of Embarq's switched access rates." It is unclear why I would need to "engage" in such review, particularly as my own analysis shows that this evidence is flawed and that United's access rates are not unreasonable or anticompetitive. Mr. Vasington then claims (at 25) that I "undercut the well-established fact that reasonable access rates benefit competition and consumers." While I have serious reservations about Mr. Vasington's purported benefits, he completely ignores the costs at which those benefits come. Contrary to Mr. Vasington's characterization of my testimony, I have not said that there would be no benefits from reducing intrastate switched access rates in the context of this proceeding. Rather, I have said that the benefits would be minimal and would be far outweighed by the costs. Mr. Vasington does not engage in a balanced cost-benefit analysis, but instead focuses on the benefits that supposedly flow from Verizon's proposal. He then recommends (at 43) that the Commission should "reject Mr. Dippon's scare tactics." I simply portray what I expect would happen if the Commission granted Verizon's proposal and took no other action. Mr. Vasington concludes his testimony by recommending (at 47) that the Commission should "place the onus on Embarq to initiate a formal rate proceeding if Embarq seeks to demonstrate the need for rebalancing." Mr. Vasington has not demonstrated that the self-serving access rate reduction proposed by Verizon improves the outdated system of access charges. As I have shown previously, United's customers will be better served by a balanced approach that looks at the entire structure of access cost recovery, not the piecemeal approach recommended by Mr. Vasington.

***Q. What is the nature of the contradiction between your testimony and Mr. Roth's that Mr. Vasington alleges?***

**A.** Mr. Vasington alleges (at 7) that the white paper (Exhibit CMD-3) attached to my responsive testimony: (1) acknowledges that subscriber line costs are non-traffic sensitive (NTS) costs; (2) refers to the recovery of NTS costs, including loop costs, via access charges as "subsidizing basic rates"; and (3) directly contradicts Mr. Roth's characterization of such recovery as an appropriate allocation of loop costs to access. Mr. Vasington also alleges (at 8): "Mr. Roth is trying to provide a justification for loop cost allocation to switched access service." However, Mr. Vasington evidently misunderstood the nature of Mr. Roth's calculation. As Mr. Roth explains in his surrebuttal testimony in Section V, he agrees that loop costs are not traffic sensitive; however, the Commission-approved carrier access charges in Washington include carrier common line charges on originating traffic and the interim USF rate on terminating traffic—that is, charges to recover part of the local loop costs. Thus, he determined how much of the loop cost to recover from these elements in the aggregate based on the percent of network usage accounted for by intrastate carrier access.

**Q.** ***Do you agree with Mr. Vasington (at 8) that there is no valid economic basis for recovering part of the NTS costs from carrier access charges?***

**A.** No. Contrary to Mr. Vasington's assertion, local loop (NTS) costs are actual, forward-looking costs, and ILECs like United have had regulatory constraints imposed on the prices they can charge for local service. Prices charged by successful firms in unregulated markets would have to cover these costs somewhere across all the services they provide. However, the prices of some of United's services are regulated, so it cannot mark up the price of just any service it chooses to cover the fixed (and allocated) intrastate loop cost per line. In choosing which service prices to mark up, regulators have focused on toll and carrier access rather than local service to encourage universal service. Thus, a component of the per-minute price of carrier access—the carrier common line charge—exceeds the incremental cost of carrier access. While loop cost "allocations" are not part of the (incremental) cost of carrier access, loop costs are part of the cost of providing telephone service; and, carriers have recovered these costs on a per-minute basis because regulators have chosen to allow markups above incremental cost for carrier access services and toll services. The same is true of many of United's retail services and for the same reasons, because its basic local rates have been constrained by regulation and because it must find ways to recover its total costs.

***Q. Mr. Vasington claims: "it is incorrect for Mr. Dippon to assert that a more efficient rate structure will not have consumer benefits." Have you made such an assertion?***

**A.** No. Mr. Vasington does recognize (at 8) "that the historical practice of recovering loop costs in access rates is the result of a policy decision." Then, he states that it is not economically efficient to recover NTS costs in switched access rates. First, as I explained above, I am in favor of a more efficient rate structure; however, the policy changes recommended by Verizon and AT&T are likely to harm competition and thus reduce efficiency because they would put a more disproportionate burden on United for the cost of the state's universal service and COLR policies than it bears today. The problem is that there are tradeoffs between "efficient" cost recovery and the inefficiencies imposed by COLR obligations and keeping local rates below market levels. If efficiency were the only goal, then we would need an entirely different policy; we would need a policy that moved away from the current pricing of local service and drastically reduced the ILECs' COLR obligations. However, it is clear that the Commission is balancing efficiency against other goals because it has chosen to keep basic rates below cost-based levels.

***Q. Does Mr. Vasington present new evidence in his rebuttal testimony to demonstrate that United's intrastate access charges are unreasonable and anticompetitive?***

**A.** No. Mr. Vasington has not shown that United's intrastate switched access rates are anticompetitive or unreasonably high. For example, in his rebuttal testimony (at 29–30), Mr. Vasington simply restates his argument that United's rates are unreasonably high and anticompetitive relative to United's average intrastate toll price per minute. However, the comparison he repeats in his rebuttal testimony—between United's average intrastate carrier access charges and its average retail price—remains incomplete and still does not show that United's access charges are anticompetitive or unreasonably high. As I show below, despite Mr. Vasington's attempt to confine the analysis to what he calls (at 28) "simple facts," it is necessary to look at the data in light of the proper economic principles. Doing so reveals the flaws in his argument.

***Q. Why do you believe that Mr. Vasington's comparison does not prove that United's access prices have an "anticompetitive impact," as he claims (at 29)?***

**A.** According to Mr. Vasington (at 29–30), United's intrastate access charges are anticompetitive because the average intrastate access charges faced by an IXC for originating and terminating a toll call within Embarq's service area—that is, charges incurred when United is the local carrier at both ends of a call—are "*twice* as high as the *average retail* price Embarq charges its own long distance customers when they make intrastate toll calls."[22] However, prices can only be anticompetitive in the context of a relevant market in which firms actually compete. Thus, the example Mr. Vasington provides is misleading for the following reasons.

First, carriers like Verizon and United compete *at a minimum* to provide all toll calls to customers in their areas—not just intrastate toll calls that originate and terminate within

[22] Vasington Rebuttal, p. 30 (emphasis in the original).

United's service area.[23] In contrast to this marketplace reality, Mr. Vasington's primary example of the alleged anticompetitive impact of United's access charges singles out one small component from the set of voice-only calls. The following list of the types of voice calls for which United competes illustrates just how incomplete Mr. Vasington's example actually is. That is, it shows that intrastate voice toll calls originating and terminating on United's local network are only one of many types of calls for which Verizon may purchase access in order to compete as an IXC in United's service area.

- Intrastate toll calls
  - Originating and terminating on United's local network
  - Originating on United's local network, but terminating outside its service area
  - Originating on United's network, but terminating on a competitive carrier's network in United's area
  - Originating on another network in the state, but terminating on United's network
  - Toll calls originating on a competitor's network in United's area terminating outside United's area
- Interstate toll calls
  - Originating on United's WA network
  - Originating on another carrier's facilities (including Verizon's) located in United's WA area
  - Terminating on United's WA network
  - Terminating on another carrier's facilities (including Verizon's) located in United's WA area
- Local Calls

Because United has far fewer lines in Washington than does either Verizon or Qwest and because cell phones account for a great deal of calling, the percentage of calls covered by Mr. Vasington's example is likely to be a small minority of all intrastate toll calls.

[23] Indeed, Mr. Vasington (at 29, n. 23) says he does "not disagree that competition takes place increasingly compete for a bundle of services…." He adds that this does not mean "the costs for intrastate access rates are irrelevant to the market."

Second, even the set of all calls that uses United's intrastate carrier access only accounts for a small part of the relevant market—which also includes *all* interstate wireline calls, wireless intrastate and interstate toll calls, and bundled communications services.

***Q. Mr. Vasington claims that you are ignoring the relevant facts. Is this true?***

**A.** No. Mr. Vasington claims (at 28) that I attempted "to change the subject from the relevant facts … into a complex discussion of antitrust doctrines and analyses by trying to fit [his] testimony into a framework of market definitions and a vertical price squeeze analysis." The concepts of market definition and vertical price squeeze are both highly relevant to this proceeding.

- The list of calls provided above for which United and Verizon compete demonstrates why the discussion in my responsive testimony (at 77–78) of the importance of using the relevant market is crucial to assessing the true competitive impact of United's pricing structure. Focusing on a small part of that market gives a misleading impression: a store that offers a "buy one, get one free" promotion is not pricing the second item anticompetitively.

- A price squeeze may be present when a vertically integrated firm that provides an essential wholesale input and charges competitors so much for the input that an equally efficient retail-stage competitor cannot operate profitably given the level of retail prices charged by the vertically integrated firm. Mr. Vasington claims (at 28): "Embarq charges too much for its bottleneck switched access service and too little for its competitive local exchange services." In the extreme, the vertically integrated firm engaging in a price squeeze might charge a price for the essential input that is higher than the full retail price of the service. This is what Mr. Vasington's comparison of United's access charges and average intrastate toll rates, which he presents in *both* his direct (at 4) and rebuttal (at 29–30) testimonies, purports to show. (As explained above his example is incomplete and misleading because it does not relate to an economically meaningful service.) Although Mr. Vasington avoids the use of this term, the concept of a price squeeze clearly applies to his allegations. Thus, whatever Mr. Vasington may call his discussion of the differences between United's wholesale (carrier access) charges and its retail (intrastate toll) charges, my responsive testimony is clearly relevant when explaining why such pricing is not in United's interest, and why Mr. Vasington's data do not show genuinely anticompetitive pricing practices.

***Q. What does your discussion of the relevant market imply regarding Mr. Vasington's claim (at 3) that Verizon loses money when it terminates calls in United's service territory?***

**A.** This discussion also shows why this claim does not establish that United's access charges are anticompetitive. The relevant market includes at least all types of toll calls because carriers all provide and customers all demand at least the full set of toll calls from their carrier, and in fact most want a bundle of local and toll services. Mr. Vasington's comparison ignores these market facts (and the need to assess an economically relevant market) by focusing on a single type of call, which is one small aspect of the relevant market.

**Q.** ***Mr. Vasington (at 36) compares trends in FCC regulated interstate carrier access to United's intrastate carrier access charges in Washington. What lesson should the Commission draw from the FCC's carrier access policies?***

**A.** Interstate rates were reduced over a long time period as the FCC phased in and gradually increased SLCs, and it also phased in universal service funding. As I said in my responsive testimony (at 12–13):

> First, interstate carrier access charges were not simply lowered; the rates were rebalanced and restructured. That is, the FCC increased the interstate portion of basic monthly rates through SLCs to offset reductions in carrier access charges. In addition, universal service funding was introduced and expanded over time to give the ILECs the ability to replace the contribution to network costs that would have come from carrier access charges.

Further, as I said in my responsive testimony (at Exhibit-CMD-3, p. 5), "[t]he process of rebalancing interstate rates—that is, reducing interstate carrier access charges and increasing subscriber line charges—took place over more than two decades." Thus, the immediate access charge reductions recommended by Mr. Vasington (at 48) as well as his arguments against universal service funds are counter to the FCC's approach. I firmly believe as I said (at 88) in my responsive testimony that "[c]onsistent with the FCC's approach, the Commission should consider a phase in of any reductions in intrastate switch access rates in order to avoid rate shock."

**Q.** ***Does customer density affect switched access costs?***

**A.** Yes. Mr. Vasington argues (at 11) that customer density may affect loop costs, but "whether Embarq serves a territory with less customer density does not affect its costs for providing switched access services." As I explained above, if loop cost recovery is a component of intrastate switched access rates, then it follows that loop costs impact access rates.

***Q. Should Verizon NW's access prices serve as a benchmark for United?***

**A.** No. Mr. Vasington argues (at 12): "in competitive markets, higher cost firms are not rewarded for their higher costs with higher prices." According to Mr. Vasington (id.), regardless of the cost characteristics of United's service area, Verizon NW's intrastate access rates "should serve as a proxy for the 'competitive' rate that Embarq, like other market participants should be required to accept." This argument is fundamentally flawed. According to the efficiency principle cited by Mr. Vasington, prices should be set based on costs. Therefore, to the extent that United has higher costs because of its service area characteristics, it should charge higher prices for its access services. Moreover, because of the differences in serving areas and cost characteristics, reducing carrier access charges would have consequences that are more negative for United. Not surprisingly, Mr. Vasington cannot offer any convincing support for his use of this benchmark; rather, in his rebuttal testimony (at 12), he just refers back to his initial testimony. The argument, in his direct testimony (at 20), did not and does not make any economic sense. Simply because Verizon NW's "intrastate switched access rates have received scrutiny and have been determined to be just and reasonable" ***for Verizon*** does not imply that they are appropriate or just and reasonable ***for United***.

**Q.** ***Is Mr. Vasington's opinion (at 12) about whether United is "designated" as a "rural" carrier relevant?***

**A.** No. Mr. Vasington says (at 12) that United has not been officially designated a "rural" company in Washington. In my testimony, I simply use the FCC's definition of a rural wire center—making no comment on whether United is a rural or nonrural company. See also Mr. Felz's surrebuttal testimony (at 11) for a more detailed response to Mr. Vasington's allegations on this issue.

**Q.** ***Do you agree that United should be able to raise its local rates to the same levels as those charged by Verizon NW and Qwest?***

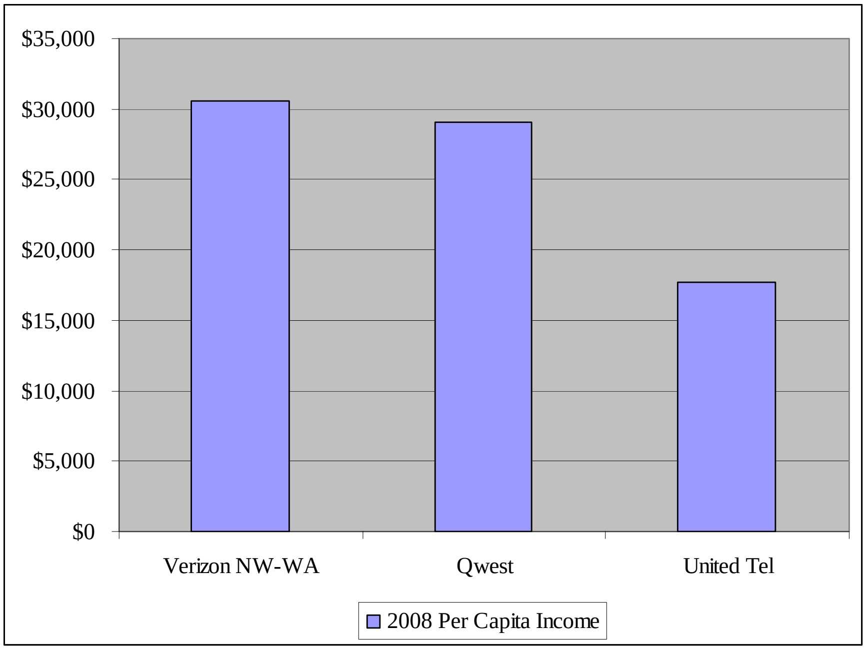
**A.** No, as I have explained above, doing so would not be advisable. In fact, this type of rate rebalancing would simply replace one type of subsidy contribution with another—from more competitive lower-cost areas to less-competitive, higher-cost areas, and it would make for an even less balanced approach—putting an even greater universal service and COLR responsibility on United than it already has.

**Q.** ***Has Mr. Vasington omitted any charges to end users in his discussion of affordability?***

Yes. Mr. Vasington states (at 18) that the "possibility of rebalancing would not raise any affordability concerns given that United's retail rates are quite low—only $8.90 or $9.40 per month for residential customers." However, these alleged rates omit the extended area service (EAS) adders that many of United's customers pay. As Mr. Felz shows (at Exhibit JMF-7HC in his surrebuttal testimony), when the EAS charges are included in basic rates, United's average residential charge comes to $13.25. This rate is $3.85 or $4.35 more than the United local exchange prices cited by Mr. Vasington.[24] It is approximately the same as the price Qwest charges today,[25] and only $3.65 less than Verizon's $16.90 average basic rate. His discussion (at 18) of basic rates also omits the SLC, which brings the effective monthly charge for basic service to about $19.75 per line per month. In addition, he omits the charges for many other retail services subscribed to by United's customers that add to their total bills and which could be increased if the Commission follows Mr. Vasington's proposal to require United to make up for the carrier access reduction by increasing its own retail rates without implementing a universal service fund.

[24] Vasington Rebuttal, p. 18.
[25] Qwest's local residential service rate is $13.50 with no extended area service charges. See Qwest Corporation Tariff WN U-40 - Exchange and Network Services Washington, Section 5, 2nd Revised Sheet 41 available at: http://tariffs.qwest.com:8000/idc/groups/public/documents/tariff/wa_e_t_s005p041.pdf#Page=1&PageMode=bookmarks.

**Figure 1**
**Per Capita Income in United's Wire Centers versus Verizon's or Qwest's in Washington**




**Q.** ***Do you agree with the timing of the rebalancing approach proposed by Mr. Vasington?***

**A.** No. Mr. Vasington admits that rebalancing is necessary:

> In both cases [New Jersey and Washington], Verizon supports more efficient recovery of costs, with end users picking up a greater portion of the costs that they have caused, if necessary. Verizon elsewhere has argued for full *revenue* recovery and has made the point that if a regulator decides that it is not appropriate to recover NTS costs in switched access rates, then it may be necessary for the regulator to provide for other cost recovery mechanisms, such as an increase in basic exchange rates, upon a showing that such revenue support is needed. That is entirely consistent with Verizon's advocacy in this case. Verizon does not claim that Embarq cannot recover loop costs that it currently recovers from intrastate switched access rates; it would simply be more appropriate and more economically efficient, and more conducive to the development of

> efficient competition, if these costs were recovered from end user customers.[26]

However, he asserts that rebalancing should be done in an inappropriate manner that would first reduce carrier access charges and only later consider policies to offset the resulting revenue losses.

> The Commission should approach this proceeding the same way it approached the complaint case that AT&T brought against Verizon Northwest in 2005: require Embarq to immediately reduce its intrastate switched access rates to levels that comply with Washington law, and separately permit Embarq to seek rebalancing in another forum.[27]

Ending the practice of recovering part of local loop costs in carrier access charges prior to rate rebalancing would be premature and harmful to the public interest.

**Q.** ***Did you explain the revenue harms faced by United in your responsive testimony in this proceeding?***

**A.** Yes. Contrary to Mr. Vasington's assertions (at 4, 23–25), I present a detailed explanation of the revenue harms to Embarq and its consumers from rate rebalancing. As I said in my responsive testimony (at 60–61):

> United would be forced to recover any lost switched access revenue from wherever it could. It could increase prices on its retail services, but these services are generally sold in more competitive areas; therefore, United would stand to lose those customers if its prices were raised above competitive levels. It could raise end user charges, but only where there was sufficient room to move prices to cover costs and still have reasonable rates. This would certainly exclude those customers in high-cost areas because any attempt to price basic local service at cost-based rates in these

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[26] Vasington Rebuttal, p. 20.
[27] Vasington Rebuttal, p. 48.

areas would make the price too high to be affordable. Finally, United could cut back on its investments and its service quality, which would be detrimental to consumers.

**Q.** ***Does Mr. Vasington's rebuttal testimony (at 32–34) present a balanced view of Professor Kahn's discussion of carrier access reform?***

**A.** No. Like Mr. Bax, Mr. Vasington, picks out only those aspects of Professor Kahn's policy discussion that bolster Verizon's position. The result is a distorted, incomplete picture. I refer you to my discussion above where I rebut Mr. Bax's allegations that I misstated Dr. Kahn.

## V. DR. BLACKMON MISINTERPRETS MY STATEMENTS

**Q.** ***Please summarize the testimony of Dr. Blackmon.***

**A.** Dr. Blackmon's main point seems to be that United's switched access rates should mirror Verizon's. As I have said before and repeat here, United's operating area in the State of Washington is vastly different from either Verizon's or Qwest's. As I have shown above, the geographic characteristics—notably population density—and demographic characteristics—income per capita—of United's service area are vastly different from those of Verizon and Qwest. Thus, if the Commission does decide to reduce United's switched access rates, then it must do so based on United's particular circumstances—and establish a state-specific universal service fund along with additional pricing flexibility. I also disagree with Dr. Blackmon's assessment of the competitive effects of United's terminating access charges and of the potential for rate rebalancing. I believe he greatly overstates the harms of those charges and of the ability of United to charge local rates that are closer to the larger carriers in the state.

**Q.** ***How do you respond to Dr. Blackmon's claim (at 8) that you are in error when you say, "United cannot sustain an increase in local rates due to competition"?***

**A.** I do not agree with his description of my testimony on this issue or with his statement (at 9): "Mr. Dippon attributes United's price structure to 'the legacy of value of service pricing,' (p. 23) but he accepts this pricing structure as a given." I do not accept "this pricing structure as given." I recognize that adopting Verizon's proposal (or Dr. Blackmon's variation of that proposal) without universal service reform could lead to higher rates for more rural areas and/or lower service quality. I emphasize that the Commission must take note of the implications of lower access charges on rates in rural areas. As I said (at 25) in my responsive testimony, United faces competition in its more populated exchanges from various sources such as the CLECs and intermodal competitors, and this competition will only intensify. This puts pressure on United to keep its local rates in competitive exchanges sufficiently low so that it does not suffer additional line losses.

**Q.** ***Do you think Dr. Blackmon is correct when he implies that United should be treated the same as Verizon and Qwest?***

**A.** No. Dr. Blackmon says (at 9): "Mr. Dippon contends policies applied to Qwest and Verizon Northwest 'cannot simply be ported' to United, but this is no explanation for why United persists in an upside-down rate structure more than a decade after the Commission eliminated it for Qwest." It may be possible for United to raise rates in more rural areas, where there is less competition, but that does not mean the solution that worked for Qwest and Verizon would work for United. As I explained in my responsive testimony (at 23) and repeat here:

> [T]he large majority of United's wire centers are rural—with population densities below 100 people per square mile—and the majority of its access lines are in such areas.[28] I stress that even the wire centers that the FCC would classify as nonrural (Grandview, Poulsbo, and Wapato) are very sparsely populated and simply do not compare to rural areas such as the metropolitan area of Seattle. In contrast, Qwest and Verizon NW are more concentrated in urban and suburban areas of the State of Washington. The average population density of wire centers served by United is 27.96 people per square mile, only about 11 percent as large as that of Qwest and 18 percent as large as Verizon NW's. Finally, while about 73 percent of the lines served by United are residential lines, Qwest's and Verizon NW's residential lines make up about 66 and 69 percent, respectively, of total lines.

As I also said (id.), firms serving areas with low population densities like United incur greater average costs for basic local service customers; more rural areas usually have a lower ratio of business to residential lines, and the economics for providing advanced services, such as broadband and video, are less favorable in low population density areas. Factors such as these separate United from Qwest and Verizon NW. These factors also suggest that in the absence of the subsidy contribution from carrier access revenues, United may have more difficulty meeting its COLR obligations than the other carriers would.

[28] This is based on the FCC's definition of rural, which is not to say that it cannot be changed by the states based on circumstances.

**Q.** ***Do you agree with Dr. Blackmon's argument (at 10) that if United raised its local basic rates United's profits could increase because more of its customers would purchase bundles from United or just pay the higher local rates?***

**A.** No. As he recognizes, the increase would narrow the difference between basic rates and the bundled services of "both United's bundles and those of its intermodal competitors." Thus, his assertion is speculative at best because United has no way of ensuring that customers would shift to its bundled services. In fact, if they are motivated by United's price increase enough to shift to a bundle, they may well move to a competitor. Moreover, United's basic service customers who buy enough a la carte optional services could well opt for a $30 bundle from a competitor.[29] Thus, I disagree with Dr. Blackmon (at 9) that intermodal options do not compete with United's basic services because so-called "basic service customers" really should be considered a la carte customers whose combined expenditures on local access, optional calling features, and toll calling could easily cost them more than $30 per month.

**Q.** ***Do you agree with Dr. Blackmon that United's originating switched access rate should mirror Qwest's?***

**A.** No. On page 57 of my responsive testimony, I responded to Mr. Vasington's request to require United to mirror Verizon NW's rates. My response was, "Verizon NW's serving areas and its cost structure are entirely different from United. Therefore, there is no reason why United's rates should be set at the same level as Verizon NW's rates." I can

[29] Dr. Blackmon recognizes (at 9) that United's competitors market bundled services for $30 to $50 per month.

only repeat myself with regard to Verizon. Verizon's rates in no way reflect United's operating areas or its costs.

**Q.** ***What is your assessment of Dr. Blackmon's argument that United's originating carrier access charges allow it to export its costs to service areas other than its own?***

**A.** Dr. Blackmon argues (at 4): "United's originating access charges are higher than those of Verizon or Qwest"; thus, the company can "export costs of the United … local network to the customers of Qwest, Verizon Northwest, and/or the [IXCs]. . . ."[30] He continues (id.) his argument by saying that this occurs because carriers must average their toll rates throughout the state, and, thus, the "excess" rates charged for originating access result in higher rates for customers in other parts of the state who make intrastate toll calls. My analysis of Dr. Blackmon's proposal to bring United's originating access charges into line with Verizon's shows that the effects of United's carrier access charges on other areas are not sufficient to justify the policies he recommends. More specifically, the proposal by Dr. Blackmon (at 18) implies that United is receiving about $0.015 more per originating minute of access than Verizon for originating access.[31] However, based on the number of originating carrier access minutes United billed in 2008 and the number of wired access lines in Washington, I estimate that United received an average net inflow

[30] Dr. Blackmon repeats this allegation at 18.
[31] Dr. Blackmon recommends (at 18): "United should be required to reduce its originating access rates to the level charged by Verizon...." Adopting this proposal would reduce these rates from about $0.031 to about $0.0158. Dr. Blackmon would accomplish this: "by eliminating United's carrier common line charge, which is $0.01 per minute, and by lowering United's LS1 and LS2 originating premium access rate from $0.020740 per minute to $0.015817 per minute."

of only about $0.018 per month from wired lines in the state in 2008.[32] This amount of "excess" carrier charges as Dr. Blackmon refers to the difference between United's current charges and the charges he recommends is hardly significant in practice.

Moreover, the competitive implications differ from those that Dr. Blackmon suggests. Other carriers are not "squeezed by United's high access charges" as Dr. Blackmon alleges (at 12). To the contrary, because they serve all geographic areas, they have a competitive advantage competing for toll customers in United's territory. More specifically, United competes against IXCs in its territory and is concerned about meeting the toll prices of IXCs (e.g., Qwest and Verizon) that serve all of Washington. As a reseller of long distance services, United must reimburse the wholesale long distance provider for carrier access charges. Thus, United pays the same carrier access charges as those that would be paid by another firm with the same toll traffic. In setting its toll prices, United, therefore, must take into consideration the opportunity cost it incurs when it captures toll traffic—if it gets the toll customer, it loses the access charges that it would have had. As Dr. Blackmon points out, IXCs geographically average toll prices; and, since United's territory is small, IXC toll prices essentially do not reflect United's relatively higher carrier access charges. If anything, United must compete against IXCs that are possibly pricing below cost in United's territory. It is United that would be competitively harmed in the toll market—it makes more money selling access than

[32] I calculated this figure by: (1) taking the difference between United's originating revenues from carrier common line and local switching (LS1 + LS2) during 2008 and the amount of revenues United would have received had it charged the current Verizon tariff rate of $0.015817 for originating local switching minutes, according to Dr. Blackmon's testimony (at 18); (2) dividing the difference by the total number of LEC lines in Washington—

competing against the IXCs that (effectively) ignore United's access charges. High access charges do harm wireline carriers (including United) in their competition against wireless and other carriers that pay little or no access charges. However, the solution proposed by Dr. Blackmon would do more harm than good because it puts an even greater burden on United than it operates under today.

## VI. CONCLUSIONS

**Q.** ***Please summarize your testimony.***

**A.** None of the parties has presented additional evidence that causes me to change my mind. My recommendation stands—do not reduce intrastate switched access rates unless simultaneously providing a fair and reasonable opportunity for United to recover the costs of its regulatory burdens—a cost that is not part of a nonregulated firm. This must be done through a state-specific USF. Furthermore, United should be granted pricing flexibility to allow it an opportunity to price at competitive levels in an effort to compensate for the access rate reduction.

**Q.** ***Does this conclude your surrebuttal testimony?***

**A.** Yes, it does.

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3,070,965 lines according to the most recent FCC Local Competition Report, as of 12/30/07, Table 7; and (3) dividing the result by 12 to obtain the monthly amount.