Exhibit No. ___ THC (JMF-5THC)
Docket No. UT-081393
Witness: John M. Felz

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, d/b/a EMBARQ Respondent	DOCKET NO. UT-081393

SURREBUTTAL TESTIMONY OF
JOHN M. FELZ

ON BEHALF OF
UNITED TELEPHONE COMPANY OF THE NORTHWEST, d/b/a EMBARQ

June 30, 2009
Redacted – Public Version

Q. Please state your name, business address, employer and position.

A. My name is John M. Felz. My business address is 5454 West 110th Street, Overland Park, Kansas 66211. I am Director – State Regulatory for Embarq.

Q. Are you the same John M. Felz who filed responsive testimony in this case on April 17, 2009?

A. Yes.

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to address certain issues raised in the testimonies filed by Commission Staff witnesses Dr. Glen Blackmon, Ms. Jing Liu and Mr. Timothy Zawislak. In addition, my surrebuttal testimony addresses certain issues raised in the rebuttal testimonies filed by Lawrence J. Bax on behalf of AT&T Communications of the Pacific Northwest, Inc., TCG Oregon, Inc. and TCG Seattle, Inc (hereafter AT&T) and 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. (hereafter Verizon).

I. ISSUES RELATED TO UNITED'S COLR OBLIGATION, UNIVERSAL SERVICE AND STATUS AS A RURAL CARRIER.

Q. Dr. Blackmon claims that United has overstated its COLR obligations and misapplied it with respect to access charges (Blackmon testimony, page 12). How do you respond?

A. Dr. Blackmon's testimony on this topic focuses on just one aspect of United's COLR obligation – that being its obligation to extend facilities to new service addresses where no distribution plant exists. But United's COLR obligation includes more than just the requirement to extend facilities to new customers – it includes requirements to maintain its facilities including replacing or reinforcing network facilities where necessary and to comply with Commission service quality standards. While Dr. Blackmon points to the change in the Commission's line extension rule and the Commission's decision in a case where Verizon Northwest was not required to extend facilities to serve a location based on extraordinary costs, these factors do not change the underlying nature of United's serving territory – which is characterized by high cost to serve areas. As described in the responsive testimony of United witness Mr. Roth, United's service areas reflect higher costs to serve driven principally by lower density, longer distances to reach customers and economies of scale. These cost drivers are present and impact United's costs and need for universal service support, even if recent Commission changes have attempted to limit COLR obligations related to unreasonably costly line extensions.

Q. Dr. Blackmon also suggests that the presence of three wireless ETCs serves to minimize United's COLR obligation impacts (Blackmon testimony, page 16). Do you agree?

A. No. The designation of wireless carriers as ETCs in United's service territory may provide a more reasonable cost alternative than extending United's facilities to serve an isolated customer. However, the presence of ETCs does not diminish United's COLR obligation to provide service throughout its service area and to provide dependable service, consistent with Commission standards. Even if the obligation to provide service to an isolated customer were imposed on a wireless ETC, United is still required to maintain its network which in many cases is utilized by other carriers, including wireless carriers to transport traffic to/from the other carriers' network. Further, not only does the presence of ETCs do little to reduce United's costs, it serves to increase United's costs on a per customer basis as ETCs tend to serve lower than average cost customers. For these reasons, the presence of certified ETCs in United's service territory does little to reduce United's costs of meeting its COLR obligation.

Q. Dr. Blackmon states that the "terminating access rate is the only place in a company's access rate structure where universal service costs can be justified." (Blackmon testimony, page 16). Do you agree?

A. No. The Commission's rule WAC 480-120-540 allows recovery of loop costs through originating access rates. Specifically, the rule states that "nothing in this rule prohibits recovery of local loop costs through originating access charges. . ."[1] Dr.Blackmon also states in his testimony that ". . .it is reasonable to recover a portion of shared and common costs in originating access rates." While Staff believes their recommendation for reducing United's originating access rates provides sufficient recovery of such costs in originating access, United is not aware of any prohibition from recovering a portion of its loop costs through originating access as reflected in its current access rates.

Q. Commission Staff recommends a phase-down and eventual elimination of United's terminating universal service fund additive (Blackmon, pages 35-36). What concerns do you have with Staff's recommendation?

A. While there have been significant changes in the telecommunications market in the years since United's universal service fund additive was established, a fundamental fact that led to the Commission's approval of the charge has not changed. Specifically, United's service area is still characterized by areas of low population density which are reflected in the company's higher cost to provide service. This is supported by Mr. Roth's cost study results. In 1998, United's costs per line as determined in Docket UT-980311 were $44.17. In this proceeding, United's costs per line as supported by Mr. Roth are **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. Mr. Roth's surrebuttal testimony provides an analysis to demonstrate that even using the costs from Docket UT-980311, and comparing to United's revenue per line, the need for support still exists. To the extent the Commission found the need to support United's universal

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[1] WAC 480-120-540, paragraph 2.

service costs with a universal service fund access rate based on costs of $44.17 per line, it is clear that need still exists and the Staff recommendation to eliminate the charge as unnecessary or not needed is ignoring the Commission's original rationale for approving the charge.

Q. Commission Staff expresses concern that the universal service fund access rate mechanism does not provide sufficient and predictable support for universal service (Blackmon testimony, page 35 and Liu testimony, page 6). Is this a valid reason for eliminating the charge entirely?

A. No. When originally established, the universal service fund access rate element was established as an interim mechanism based on the premise that it would be replaced by an explicit state universal service fund. Although efforts to establish such a fund were unsuccessful, it should not be concluded that universal service support is unnecessary. Further, while United agrees that recovery of universal service support through an access charge mechanism necessarily carries with it some uncertainty, that should not be a reason for doing away with the charge. Instead, the Commission should again revisit the need for an explicit state universal service fund as the appropriate, sustainable mechanism for supporting universal service in Washington.

Q. Dr. Blackmon questions whether the concept of a universal service fund access rate element is still consistent with public policy, given the intervening time period since the mechanism was originally established (Blackmon testimony, page 33). Is this a valid reason for eliminating the charge for United in the context of this case?

A. No. Dr. Blackmon initially recognizes that "A universal service rate element may be justified if there is an excess between what it costs United to serve customers in high-cost locations and what United can recover directly from those customers through affordable and reasonably comparable retail rates." (Blackmon testimony, page 32). However, on the next page of his testimony, Dr. Blackmon expresses concerns that the rate element may not be consistent with public policy. If the Commission does not believe it is consistent with public policy to provide support for universal service through an access charge rate element, that debate and decision should take place in the context of a generic proceeding to adjust the Commission's policy as it applies to all ILECs. Commission Staff's recommendation in this case would serve to apply a significant policy change to a single company, United, and treat it differently than other companies which also recover universal service costs through a terminating universal service mechanism.

Q. Has the Commission previously indicated its intentions to comprehensively address the universal service fund rate?

A. Yes. In the Commission's Eleventh Supplemental Order in the Verizon Northwest access case (Docket No. UT-020406), the Commission indicated its expectations with regards to further consideration of issues associated with the interim terminating access charge (ITAC):

> "We have concerns about the ITAC in light of evolving competitive realities. It was contemplated as an interim measure, but appears to have acquired a longevity that was not anticipated. The nature of the revenue benchmark, the nature of the underlying cost study, the questions about continuing ability to require some support for costs from all customer classes in light of competitive realities, and the relationship with federal universal service support all deserve to be addressed in greater detail than appears on this record. Given the need to reduce access

> charges, the need for contribution to costs by all services, and the need for support in high-cost areas, we expect to address this issue again in the future[2]."

Q. Has the Commission initiated such a comprehensive review as indicated in Docket UT-020406?

A. No. Although the Commission did consider further changes to Verizon Northwest's ITAC in the context of a rate case proceeding in Docket UT-040788 as a result of a settlement in that case, the Commission has not initiated actions to consider the broad scope of issues as set forth in the statement outlined above. The Commission should not seek in this complaint case against a single ILEC, to make an important policy decision about Washington's universal service support that could set precedent for multiple ILECs. Rather, the Commission should open a generic proceeding to address the kind of comprehensive review of the issues that it has previously expressed its intention to complete. Such a review should provide the opportunity for all impacted carriers to provide input on the need for, and mechanism for funding state universal service support for Washington.

Q. Staff witness Liu, AT&T witness Bax and Verizon witness Vasington make note that United does not receive federal high cost loop support. Should this impact United's eligibility for universal service support in Washington?

A. No. Ms. Liu concludes that since United does not qualify for federal high cost loop support that it should not be eligible for universal service support in Washington. (Liu testimony pages 8-10). Mr. Bax also indicates that none of the three ILECs (United,

[2] Eleventh Supplemental Order in Docket No. UT-020406, paragraph 148.

Qwest nor Verizon Northwest) receive high cost support other than federal Interstate Access Support (IAS). (Bax rebuttal testimony, page 5.) Mr. Vasington claims that United is not considered "rural" under the FCC's framework as it does not receive any of the universal service mechanisms "designated for rural carriers, such as High Cost Loop. . ." (Vasington rebuttal, page 13). While Ms. Liu, Mr. Bax and Mr. Vasington observe that United does not receive High Cost Loop support from the federal universal service fund, it does not follow that United should be ineligible for universal service support in Washington. As recognized by Ms. Liu, Mr. Bax and Mr. Vasington, United does receive Interstate Access Support (IAS) which is a component of the FCC's universal service fund. IAS was established in the FCC's interstate access reform initiative of 2000, and along with end user subscriber line charge increases, allowed ILECs like United (as well as Qwest and Verizon Northwest) to recover support that was previously recovered through interstate access charges. So while United does not receive high cost loop support, it does receive support from the federal universal service fund consistent with the rules that are in place for that fund. Similarly, United receives support in Washington through the universal service fund access rate element consistent with the rules established by the Commission for providing universal service support. The Commission should therefore not base its decision about United's need for universal service fund support in Washington on whether United receives specific forms of federal universal service support. The Commission previously recognized that federal and state universal service support were separable issues in their review of Verizon Northwest's access rates in Docket UT-020406 where the Commission Staff advocated that the Commission offset Verizon Northwest's Washington universal support requirements with

$21 million of federal universal service support. The Commission rejected the Staff recommendation, finding that ". . . it would be improper to credit the entire $21 million to total company universal service needs when it is by FCC definition limited to support for interstate universal service needs[3]" and concluding "This decision produces a fair and equitable allocation that is consistent with federal provisions that fully funds the state responsibility for universal service support.[4]"

Q. AT&T Witness Mr. Bax takes issue with your characterization of United as a high cost rural carrier that is significantly different from Qwest and Verizon Northwest. (Bax rebuttal testimony, pages 4 and 5). Are his criticisms valid?

A. No. While Mr. Bax correctly states that Qwest and Verizon Northwest have COLR obligations and quality of service standards, he ignores the underlying differences in the serving territories of United, Qwest and Verizon Northwest which translate to much different impacts in terms of meeting those COLR obligations and quality of service standards. As I explained in my responsive testimony, and as further described in the responsive testimony of Mr. Roth, the characteristics of United's serving territory with significantly lower customer density and economies of scale form the basis for the differences in costs between United, Qwest and Verizon Northwest. The fact that United, Qwest and Verizon Northwest all have similar obligations to provide service in their respective territories does not mean they all have the same costs and therefore should be treated the same when evaluating the need for universal service support.

[3] Eleventh Supplemental Order in Docket No. UT-020406, paragraph 134.
[4] Eleventh Supplemental Order in Docket No. UT-020406, paragraph 135.

Q. AT&T witness Mr. Bax and Verizon witness Mr. Vasington take issue with United's position in this proceeding that United's service territory has unique characteristics that render direct application of prior treatment of Qwest or Verizon Northwest access rates as inappropriate for United. Has this Commission recognized the unique challenges that United faces in its Washington service territory and implications for universal service?

A. Yes. Although Mr. Bax suggests that United ". . .is more similar to Verizon and Qwest than it is to other rural carriers in the state," (Bax rebuttal, page 5) and Mr. Vasington claims that neither the Washington Commission or the FCC consider United as a "rural" carrier (Vasington rebuttal, page 13), the Washington Commission recognized the unique challenges United faces in meeting its universal service obligations in its comments to the FCC in the intercarrier compensation proceeding. The Commission stated:

> "The [Federal Communication] Commission's purpose fails to recognize that the individual operating characteristics of each rural market is determined by factors such as terrain, accessibility, distance, and customer density, not by the size or arbitrary classification of the incumbent carrier that serves it. In the case of rural "midsized" companies, the proposal's broadband build-out requirements, which are linked to access to continued universal service funding, could actually work to deter further broadband investment in rural areas by the mid-sized carriers that serve of the most rural areas of Washington State. In fact, large swaths of the state have extreme or difficult terrains that challenge provision of telecommunications and broadband services. Additionally, significant portions of Washington's rural service areas are served by two "midsize" carriers (CenturyTel and Embarq), which appear to be the carriers most adversely affected by the Commission's proposals. In Washington, CenturyTel and Embarq serve approximately 9 and 10 access lines per square mile, respectively, and together, these companies serve nearly 30 percent of the area of Washington state."[5]

[5] Comments of the Washington Utilities and Transportation Commission in the matter of *High-Cost Universal Service Support*, WC Docket No. 05"337; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *Lifeline and Link Up,* WC Docket No. 03-109; *Universal Service*

Q. AT&T witness Mr. Bax also mentions that the Commission granted United's petition for minimal regulation in Docket UT-071575. (Bax rebuttal testimony, page 5). Is that an important development as it relates to this proceeding?

A. No. While the Commission did grant United's petition for minimal regulation of bundled telecommunications services in Docket UT-071575, providing certain flexibilities to United for pricing and tariffing of its competitive bundled services, that proceeding provided no substantial capabilities for United to seek sustainable rate increases to mitigate the financial harms from potential access revenue reductions. United's bundled services are already set at competitive levels and the grant of pricing flexibility for bundles in the referenced case did not address United's restriction from increasing rates for non-bundled access line without a rate case or AFOR proceeding. Mr. Bax seemingly shares the perspective that bundled rates are already set at competitive levels in his discussion of rate rebalancing where he states:

> ". . . a large number of customers who currently purchase bundled telecommunications service packages likely will not be affected by any increase in the basic service rate because bundled packages are already subject to greater competition." (Bax rebuttal testimony, page 18).

Q. Staff witnesses Dr. Blackmon and Ms. Liu express concerns in their testimony that there are inadequate safeguards or accountability for the revenues generated from

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Contribution Methodology, WC Docket No. 06-122; *Numbering Resource Optimization,* CC Docket No.*99-200;1mplementation of the Local Competition provisions in the Telecommunications Act of* 1996, CC Docket No. 96-98; *Developing a Unified Intercarrier Compensation Regime,* CC Docket No. 01-92;*Intercarrier Compensation for ISP-Bound Traffic,* CC Docket No. 99-68; *IP-Enabled Services,* WC Docket No. 04-36, FCC 08-262 (released: November 5, 2008)., pages 5-6.

the universal service fund access rate element. Do you agree that there are inadequate safeguards or accountability for the funds generated by the charge?

A. No. The Commission has many tools available to ensure companies like United that receive revenues from the universal service fund rate element fulfill the requirement that the charge was designed to support. For example, United complies with Commission rule WAC 480-120-439 which requires detailed reporting of the companies performance in a variety of areas related to the company's universal service obligations established by Commission rules including:

480-120-105	Company performance standards for installation or activation of access lines
480-120-133	Response time for calls to business office or repair center
480-120-401	Network performance standards
480-120-411	Network maintenance
480-120-440	Repair standards for service interruptions and impairments

The detailed reports provide the Commission a timely view to the company's performance against established standards which help ensure the continued provision of universal service.

The Commission also has ability to review and evaluate United's overall financial position through quarterly and annual reports submitted in compliance with WAC 480-120-385. Coupled with the service quality and network measurements described above, the Commission's ability to assess United's financial situation provides the Commission the tools to ensure United is meeting its universal service and COLR obligations which ensure that the funds provided by the universal service fund access rate element are still needed for United to maintain financial viability.

II. ISSUES RELATED TO RATE REBALANCING

Q. Commission Staff recommends that United reduce its universal service fund access rate to zero over a three-year period beginning in 2011 and consider increasing its local service rates if it can demonstrate a need for the revenues. (Blackmon testimony, page 31; Zawislak testimony, pages 6-9). What is United's reaction to Staff's recommendation?

A. Commission Staff reaches a conclusion that United could offset the need for a universal service rate by increasing its local rates. Dr. Blackmon states: "If United were simply to charge all customers what it already charges customers in Poulsbo or what Verizon Northwest charges its customers, the additional revenue would offset most of the need for a universal service rate." Blackmon testimony, page 31. However, in reality, Staff's proposed solution is not a "simple" solution and even if feasible, would provide only partial offsets to the access reductions advocated by Commission Staff.

Q. Could you elaborate on some of the issues with the Commission Staff's proposed solution?

A. Yes. Staff's proposed solution is at best only a partial offset to the negative impacts that would result from Staff's recommended access reductions.

1. United is precluded from implementing a basic local rate increase without initiating a formal rate case or pursuing an alternative regulation plan. Such proceedings are complex and lengthy, with outcomes that are uncertain. United

would suffer financial harm to the extent access reductions were ordered to be implemented in advance of the company's ability to prosecute a local rate case or alternative regulation filing.

2. Staff's financial analysis as presented by Staff witness Zawislak assumes United can increase rates for all residential and basic business access lines, resulting in an overstatement of the real incremental revenue that could be expected if Staff's proposal were to be pursued. Specific concerns about Staff's analysis include:

   a. United's bundled rates are already competitive and at levels that are comparable to those of Verizon Northwest and Qwest. I have prepared Exhibit No. ___ JMF-6 that provides pricing for comparable bundles offered by Qwest, Verizon Northwest and United. While this is a single example, it demonstrates that United's bundled rates are at competitive levels, and the ability to increase rates for bundled services to offset any access reduction would not generate meaningful offsetting revenues. Dr. Blackmon seems to recognize this market dynamic with his comment at page 10 of his testimony that "An increase in local rates would narrow the difference between the price of standalone local service and the price of bundles – both United's bundles and those of its intermodal competitors." In spite of this position, Mr. Zawislak's analysis includes the impact of an increase for all of United's residential and basic business lines, including bundled and non-bundled lines.

   b. A revised analysis that updates Mr. Zawislak's analysis using only non-bundled access lines provided as Exhibit No. ___JMF-7HC reveals that a more realistic maximum opportunity from pursuing local rate increases for all exchanges to equal the local rates currently charged in Poulsbo is **[BEGIN HIGHLY CONFIDENTIAL]** $[redacted] **[END HIGHLY CONFIDENTIAL]**versus Staff's original calculation of **[BEGIN HIGHLY CONFIDENTIAL]** $[redacted] **[END HIGHLY CONFIDENTIAL]** .

c. The local rate increases for several individual exchanges would be significant under Staff's proposal (Stevenson – 90% increase from $8.90 to $16.90; Goldendale, Glenwood, Roosevelt, etc. – 55% increase from $10.90 to $16.90; Dallesport, Grandview, Prosser, etc. – 39% increase from $12.15 to $16.90). These would represent significant increases for customers and calls into question whether Staff's projected revenue impact can actually be realized.

Q. Dr. Blackmon comments that United's local rate structure is "upside down" (Blackmon testimony, page 29) and Mr. Zawislak recommends that United adopt a local rate structure that charges the same rates for all of its Washington exchanges and that United consider adjustments to its local calling areas (Zawislak testimony, pages 7-8). What is United's reaction to this proposal?

A. As explained above, this proceeding does not provide the opportunity for United to address its local rate structure or local calling scopes, so Staff's recommendation in this proceeding is misplaced. Nevertheless, United's current local rate structure is a product of the Commission's polices with regard to calling area expansions and mandatory EAS.

Ignoring EAS, United has only two rate groups, $8.90 and $9.40. Both Qwest and Verizon Northwest moved to an averaged state-wide rate in the context of rate cases and not through voluntary rate restructuring. Further, in regards to the suggestion that United consider local calling scope changes, the Commission's rule on EAS prohibits any additional EAS except those completed in compliance with Commission rule WAC 480-120-265. The Commission's own website states, "The UTC does not plan on conducting another review. The commission's policy going forward is to rely on competition and other options to meet individual customer calling needs. Larger calling areas will be mandated only under the most exceptional circumstances."

Q. Verizon witness Vasington makes references to United's residential local rates being ". . .below what constitutes "affordable" local retail service." (Vasington rebuttal testimony, page 2) Is this an accurate conclusion?

A. No. While Mr. Vasington correctly quotes United's stand-alone local rates, he ignores the mandatory EAS charges which are applied to local access lines, including bundled lines, for all of United's exchanges except Stevenson. The practical impact of United's rate structure is that the average rate paid by a residential stand-alone customer for local service across all of United's exchanges is approximately $13.25. While this rate is below Verizon Northwest's equivalent local rates, it is consistent with rates charged by Qwest of $13.50. Mr. Vasington's conclusions that United's rates are too low and could be increased to offset the access reductions proposed by Verizon are based on an incorrect starting point. Thus, his conclusions overstate the true offsetting revenues

United could conceivably expect to achieve IF it were able to increase its stand-alone local service rate. Further, as I explained earlier in my testimony, and also discussed by United witness Mr. Dippon, competitive factors would further limit the offsetting revenue United could expect from a local rate increase. Finally, as explained further in Mr. Dippon's surrebuttal testimony, Mr. Vasington ignores the fact that per capita income is much higher in Verizon Northwest's service territory than United's which may affect a determination as to whether Verizon Northwest rates could be considered affordable in United's service territory.

Q. Does this incorrect starting point impact Mr. Vasington's conclusions about United's ability to offset the access revenue reductions advocated by Verizon with increases in local service rates?

A. Yes. Mr. Vasington suggests at page 44 of his rebuttal testimony that United could recover all of the revenue reduction from Verizon's proposed access reductions by increasing rates across all access lines by **[BEGIN HIGHLY CONFIDENTIAL]**[redacted] **[END HIGHLY CONFIDENTIAL]** per month, and that such an increase would result in local retail rates that ". . .would still be lower than Verizon Northwest's." (Vasington rebuttal, page 47). First, Mr. Vasington's calculation of a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**local rate increase as the amount necessary to offset Verizon's proposed access reduction ignores the reality that United's bundled rates are already at levels comparable to those of Verizon Northwest and Qwest and should not be considered in calculating potential rate rebalancing impacts.

Secondly, even if a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** increase across all access lines were sustainable (which United does not believe it is), when added to the correct starting point of $13.25, United's rate would be $19.25, which is $2.35 (nearly 14%) higher than Verizon Northwest's current local service rate of $16.90.

Q. Mr. Bax discusses United's ability to rebalance intrastate switched access revenue reductions with increases in the rates for basic local exchange rates and points out that United's average tariffed rates being below Verizon Northwest's provides such an opportunity. (Bax rebuttal testimony, page 15). Is Mr. Bax utilizing the correct starting point for evaluating United's current basic local rates?

A. Although Mr. Bax does not reference specific numbers on this point in his rebuttal testimony, it appears he is simply comparing a "simple average" of United's basic local service rates without considering the impact of EAS rate additives to get a complete picture of United's local service rates. While a simple average of United's two residential basic local service rates of $8.90 and $9.40 would be $9.15, as I explained earlier, when considering EAS additives, the weighted average rate for residential service is $13.25. This is the more appropriate rate for comparison with the rates charged by another Washington ILEC like Verizon Northwest.

Q. Have you estimated the local rate increases to non-bundled access lines that would be needed to offset the access reductions proposed by the parties in this proceeding?

A. Yes. Exhibit No. ___JMF-9HC summarizes the estimated impact of the access rate reductions proposed by Verizon, AT&T and Staff in this proceeding and calculates the monthly increase that would be needed for each non-bundled access line in order to offset the access revenue reductions. The impacts are summarized below **[BEGIN HIGHLY CONFIDENTIAL]**:

Party	Annual Proposed Access Revenue Reduction	Monthly Per Line Increase Needed on Non-Bundled Lines
AT&T	[redacted]	[redacted]
Verizon	[redacted]	[redacted]
Commission Staff	[redacted]	[redacted]

[END HIGHLY CONFIDENTIAL] This analysis demonstrates that the various rate rebalancing scenarios discussed by the parties to this proceeding cannot produce the revenue needed to offset their proposed access rate reductions and still maintain affordable basic local rates.

Q. On Page 22 of his rebuttal testimony, Verizon witness Mr. Vasington comments that Embarq has expressed concerns about the impact of low local service rates impeding competition, and he cites a specific Embarq filing in Ohio involving the Doylestown Telephone Company. Are his statements accurate?

A. His statements in this portion of his testimony are incomplete and misleading. The situation in that proceeding is not comparable to this proceeding. The state of Ohio has a rule that allows an ILEC to operate as a CLEC in other carriers' territories without actually being designated a CLEC. These pseudo-CLECs, such as Doylestown

Telephone Company, are given CLEC pricing flexibility, and they must cap their access rates at the ILEC's level. The reason they must cap their access rates is because access rates serve a specific function for an ILEC in the ILEC's own territory: they help to cover the costs of serving where the ILEC is obligated to serve. But they do not serve this same function outside-of-territory since there is no obligation. Specifically, the Ohio Commission wrote:

> "As we note in our Opinion and Order adopting the carrier-to-carrier rules, the current access rates in a small ILEC's incumbent territory were designed to achieve a particular purpose, that being to promote universal access to telephone service in rural markets at affordable rates. That same purpose does not exist when a small ILEC chooses to compete outside of its territory. For that reason, the Commission concluded that, as a matter of public policy, such out-of-territory operations should be treated just like any other competitor. To do otherwise would place at a competitive disadvantage the in-territory ILEC, against which the edge-out company is competing.[6]"

The Ohio Commission appropriately ruled that Doylestown should not be able to utilize its in-territory ILEC access rates which were designed to support universal service needs to its competitive advantage in out-of-territory operations where it has no obligation to serve.

Q. How would the access reductions recommended by the parties in this case impact the company's overall financial situation?

A. Commission Staff's proposal would result in an estimated access revenue reduction of approximately **[BEGIN HIGHLY CONFIDENTIAL]** $[redacted] **[END HIGHLY**

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[6] Commission Order in Case No. 08-117-TP-WVR, In the Matter of the Application of Doylestown Telephone Company for a Waiver of Edge-Out access Rate Reduction Requirements, paragraph 18.

CONFIDENTIAL] based on 2008 annual demand. To provide an illustration of the impact of such a revenue reduction on United's overall financial situation, I have provided as Exhibit No. ___JMF-8HC, an adjusted statement of operations for the 12 months ended March 2009 which calculates the company's intrastate rate of return. The exhibit demonstrates that United's intrastate return would be a **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**. Clearly, the proposed access reduction would have significant consequences for the company as it would effectively eliminate the company's intrastate operating income. The proposed access reductions of AT&T and Verizon would have even greater negative financial consequences. While Staff, AT&T and Verizon have all included testimony about the potential for offsetting revenues from local rate increases, there is absolutely no certainty about whether such increases would be authorized, and further uncertainties about the timing and sustainability of any local rate increases provides little to change the negative financial situation United would face if access charges were reduced as a result of this proceeding. This analysis clearly demonstrates that United has a definitive need for the revenues currently provided through its access rates to continue to meet its COLR obligations and universal service requirements, and that the Commission should carefully coordinate timing of any access rate reductions with a definitive ability to recover those revenues from other sources.

Q. Would a reduction of United's intrastate access rates without a simultaneously replacement for the lost revenue constitute single-issue ratemaking?

A. Yes. General ratemaking principles entitle regulated utilities to charge rates that are sufficient to allow them to recover a reasonable rate of return on their investment. According to United's first quarter 2009 statement of operations, it is currently earning a **[BEGIN HIGHLY CONFIDENTIAL]**[redacted] **[END HIGHLY CONFIDENTIAL]** intrastate rate of return. The parties' proposals to reduce United's access rates would drive its rate of return [**BEGIN HIGHLY CONFIDENTIAL]**[redacted] [**END HIGHLY CONFIDENTIAL]** as described above. It does not matter whether any reduction to United's return resulting from an access reduction, should the Commission order one, turned out to be on the high or low end of these figures; United is entitled a hearing before the Commission on all relevant ratemaking adjustments before any reduction to access charges is authorized. Anything less would be a reduction to United's rates on a single issue, without consideration of all adjustments required for the Commission to determine the rates United is entitled to charge to earn a reasonable return.

Q. Does this conclude your surrebuttal testimony?

A. Yes.

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