

OFFICIAL REPORTER'S MINUTES

CASE NO. PUC-2007-00108

COMMONWEALTH OF VIRGINIA STATE CORPORATION COMMISSION

PETITION OF

SPRINT NEXTEL

CASE NO. PUC-2007-00108

For reductions in the
intrastate carrier access
rates of Central Telephone
Company of Virginia and
United Telephone-Southeast, Inc.

TESTIMONY OF CHRISTIAN DIPPON

- Hearing Examiner -

DATE TAKEN

September 29, 2008

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

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VOLUME I

The complete transcript of the testimony
and other incidents in the above-captioned matter when
heard on September 29, 2008, before the Honorable
Alexander F. Skirpan, Jr., Hearing Examiner for the
State Corporation Commission, Richmond, Virginia.

Reported and transcribed by:

Heidi L. Jeffreys, RDR, CRR

1 THE HEARING EXAMINER: Any objections to
2 its admission?

3 MR. PAGE: No objection.

4 (The exhibit was admitted into evidence.)

5 CHRISTIAN DIPPON, called as a witness by
6 Embarq, having been first duly sworn, was examined and
7 testified as follows:

8 DIRECT EXAMINATION

9 BY MR. PAGE:

10 Q. Please identify yourself, Mr. Dippon.

11 A. Yes. My name is Christian Dippon. The
12 last name is spelled D-I-P-P-O-N. I'm an economist
13 and vice president at National Economics Research
14 Associates. It's an international consulting firm.
15 My offices are based in San Francisco, California.

16 Q. Mr. Dippon, did you cause to be prefiled
17 in this proceeding direct testimony consisting of 44
18 pages of questions and answers and two attachments?

19 A. Yes, I did.

20 Q. And was this testimony prepared by you or
21 under your direct supervision and control?

22 A. Yes, it was.

23 Q. Now, subsequent to the prefiling of that
24 direct testimony did you cause to be prefiled in this
25 proceeding two errata pages substituting pages 40 and

1 41 of your prefiled testimony?

2 A. Yes, I did.

3 Q. And were those pages substituted by a
4 submission to the Commission made on August 27, 2008?

5 A. That is correct.

6 MR. PAGE: Your Honor, rather than pass
7 out those documents, which have already been passed to
8 the record, we'd like those pages to substitute, if we
9 could.

10 THE HEARING EXAMINER: Okay.

11 MR. PAGE: Thank you.

12 THE HEARING EXAMINER: We will do that.

13 BY MR. PAGE:

14 Q. And, Mr. Dippon, did you cause to be
15 prefiled in this proceeding rebuttal testimony
16 consisting of 36 pages of questions and answers and
17 one attachment?

18 A. Yes, I did.

19 Q. Do you have any further corrections to
20 either your direct or rebuttal testimony, as amended
21 by the substituted pages?

22 A. No, I don't have any corrections.
23 There's one clarification I'd like to add.

24 I noticed the white paper, which is
25 attached to my direct testimony as CMD-2, did not have

1 a date on it. The date should be August 1, 2008.

2 Q. Thank you. If I were to ask you the same
3 questions today in your rebuttal and direct testimony
4 as you've revised it, would your answers be the same?

5 A. Yes, they would.

6 MR. PAGE: Your Honor, I move that
7 Mr. Dippon's prefiled testimony -- I presume his
8 direct -- well, I'll let you go through the scenario.

9 THE HEARING EXAMINER: All right. I'll
10 mark his public direct testimony as Exhibit
11 Number 15 --

12 (The exhibit was admitted in evidence.)

13 THE HEARING EXAMINER: -- his
14 confidential direct testimony as Exhibit 16-C --

15 (The exhibit was admitted into evidence.)

16 THE HEARING EXAMINER: -- his rebuttal
17 public testimony as Exhibit 17 --

18 (The exhibit was admitted into evidence.)

19 THE HEARING EXAMINER: -- and the
20 confidential version of his rebuttal testimony as
21 18-C.

22 (The exhibit was admitted into evidence.)

23 THE HEARING EXAMINER: And they're all in
24 subject to cross-examination.

25 MR. PAGE: Thank you.

1 BY MR. PAGE:

2 Q. Mr. Dippon, Mr. Nurse, on page 3 of his
3 rebuttal testimony, states that, quote, "All the
4 parties, even Embarq, agree that Embarq's intrastate
5 switched access rates have been inflated by
6 significant implicit subsidies," end quote.

7 Do you agree with that statement?

8 A. I'm not quite sure I would characterize
9 it as inflated and significant, but I do agree that
10 Embarq's intrastate switched access rates contain a
11 subsidy element.

12 Q. And what is the objective of this
13 subsidy?

14 A. The objective is to keep prices for local
15 telephone service in Virginia, and particularly in
16 rural Virginia, affordable. And for that Embarq is
17 the carrier of last resort, so it's obligated to
18 provide services in high-cost areas, in areas where
19 thus far competitive carriers have decided not to
20 enter.

21 Embarq has to serve those areas, and what
22 that means is Embarq cannot charge prices according to
23 cost but according to regulated tariffs, and that
24 leads to Embarq charging prices below its cost.

25 Q. Is switched access revenue a significant

1 part of Embarq's earnings?

2 A. Embarq is largely a rural phone company,
3 and, hence, that subsidy is significant. I think the
4 Staff report confirms that.

5 Q. So, getting back to Mr. Nurse's
6 testimony, would you say that switched access rates
7 have been, quote, "inflated," end quote, by the
8 implicit subsidies?

9 A. Again, "inflated" has sort of a negative
10 aspect to it -- the word "inflated" has. We agree --
11 I certainly agree that it's a subsidy, but the subsidy
12 has been designed for a very particular purpose, and
13 that is to allow Embarq to recover the losses in
14 high-cost areas.

15 So it's not a rate that Embarq sets at
16 free will, it's a heavily -- a regulated rate and has
17 been under regulated scrutiny for a long time.

18 Q. What do you mean that the subsidy has
19 been under regulatory scrutiny, Mr. Dippon?

20 A. Well, this Commission has long regulated
21 as aspects of basic service rates, and the rest of the
22 rate structure is designed to promote universal
23 service, and that includes the current intrastate
24 switched access rates.

25 Q. Let's move on to Mr. Appleby's rebuttal

1 testimony. He states that -- and it's on page 3 of
2 his rebuttal testimony -- that, quote, "Embarq's dire
3 predictions will not occur if access rates are reduced
4 to costs or to interstate rate levels," end quote.

5 Do you agree with that statement?

6 A. No, I don't. And it's interesting that
7 Mr. Appleby says it's dire predictions, because all
8 I'm doing is presenting economic evidence in my
9 report. It's perceived as a dire prediction, and
10 maybe it should so, because I think the consequences
11 of granting Sprint's motion will be significant,
12 particularly for rural Virginia.

13 So, that said, I don't agree with
14 Mr. Appleby's statement, because holding everything
15 constant, if Sprint's proposal to reduce access
16 charges is adopted, Embarq will be worse off relative
17 to the status quo. Embarq as a firm will need to
18 respond to that access loss. There's no other way
19 about it.

20 Q. Mr. Dippon, let's talk a little bit about
21 Mr. Appleby's rebuttal on pages 3 and 4 where he gives
22 his four major considerations that he claims must be
23 reviewed in order to completely understand the
24 financial ramifications to Embarq of the proposed
25 access revenue reductions.

1 Do you agree with those four major
2 considerations?

3 A. No. From an economic point of view, I do
4 not agree with them. None of these four
5 considerations will allow Embarq to respond to the
6 access revenue loss.

7 Q. All right. Let's talk about the first
8 consideration of Mr. Appleby.

9 Do you believe that pricing flexibility
10 will allow Embarq to make up for revenue losses?

11 A. No. And that's a recurring theme I've
12 read many times, not only in Mr. Appleby's testimony
13 but also other testimonies, and it goes something like
14 this:

15 It's, "Well," you know, "Commission,
16 don't worry about it. There will be some access loss,
17 access revenue loss, but Embarq now has surprising
18 flexibility so let them set those prices and things
19 will be all good; they can recover that loss." And
20 that's just simply not true.

21 Embarq also serves nonrural areas. About
22 50 percent of its access lines are in nonrural areas,
23 and those nonrural areas, as I have explained in my
24 testimony -- and I think I haven't received any
25 rebuttal on that -- is that Embarq is facing

1 competition, strong competition. So under competition
2 you can't simply raise prices because you happen to
3 have some access revenue loss.

4 Embarq, like any other carrier, is a
5 price-taker in those markets; hence, a price increase
6 will be severely limited, if not impossible. It will
7 be disciplined by the competitive forces in the
8 market.

9 Now, that said, there are certain areas
10 that Embarq serves where other carriers have chosen
11 not to enter -- and I underline the word "chosen" --
12 have chosen not to enter, and in those areas Embarq
13 faces less competitive constraints. So there's a
14 possibility that the pricing flexibility will help,
15 but that is limited mainly to rural Virginia.

16 Q. Okay. Mr. Dippon, let's move on to
17 Mr. Appleby's second consideration.

18 Is it sensible in an economic sense to
19 include Mr. Appleby's consideration of Embarq's
20 further revenues from nonregulated services?

21 A. No. And I think I've seen this argument
22 in many other jurisdictions all the way back to 1997
23 in a proceeding before the FCC.

24 The point is that Embarq, nor any other
25 company, can be expected to subsidize the revenue from

1 nonregulated services -- to subsidize -- let me say
2 that again.

3 -- to subsidize nonregulated services --
4 I still got it wrong.

5 -- to subsidize regulated services with
6 the revenue from nonregulated services. Now I've got
7 it right.

8 In order for Embarq to be able to do
9 that, Embarq would have to earn some extra profit or
10 what I call super-competitive -- or has to be able to
11 charge super-competitive prices. There's no evidence
12 of that. There's no evidence that Embarq earns a huge
13 profit on these nonregulated services; hence, it's not
14 even in a position to make that proposed subsidy.

15 And, furthermore, what essentially would
16 happen is if Embarq would be obligated to subsidize
17 the regulated services with revenue from nonregulated
18 services Embarq will be unable to respond to changes
19 in competition as they incur on the nonregulated side.

20 Say, for example, DSL. Let's say Embarq
21 makes good money off the DSL today -- not more than
22 what anyone else can make, so it's not charging
23 super-competitive prices -- but what about if cable
24 came in tomorrow and undercut that price? Now,
25 Embarq -- if it had to use that revenue as a subsidy,

1 it could not respond to these competitive forces
2 anymore.

3 So, essentially, what Mr. Appleby's point
4 would be is that you ought to regulate the currently
5 nonregulated services.

6 Q. Let's talk about the third consideration,
7 Mr. Dippon.

8 Is it important to consider the access
9 cost savings that Embarq allegedly gains from the
10 revenue reduction?

11 A. Well, I think we went into that briefly
12 this morning with Mr. Schollmann. The argument that
13 Mr. Appleby brings forth here is correct in its own,
14 but he sort of misses the other part of it.

15 It's correct -- he's correct, there are,
16 strictly seen, cost savings that Embarq incurs by
17 having to pay less to Sprint, but don't forget it also
18 charges less to Sprint. So it's a wash, entirely a
19 wash.

20 To make matters worse, it is likely that
21 Embarq will have to pass on the cost savings to its
22 consumers, so at the end it's still worse off than it
23 was before. So at a minimum it's a wash. There are
24 no cost savings.

25 Q. Finally, on the fourth consideration do

1 you agree with Mr. Appleby's claims regarding Embarq's
2 existing financial strength?

3 A. No. I mean, I haven't looked into the
4 fact whether he is right that Embarq is financially
5 healthy, but even if it were, and assuming for a
6 moment that Embarq is, those are the results of
7 Embarq's commercial successes, particularly the
8 services it offers to its customers.

9 Again, it would be -- it would provide a
10 wrong incentive to force Embarq to use that commercial
11 success to pay for areas in which it loses money due
12 to its regulatory burden of being carrier of last
13 resort.

14 Q. So, Mr. Dippon, what are Embarq's
15 theoretical options that it has in responding to the
16 revenue loss, as proposed by the Staff and the parties
17 in this case?

18 A. Again, Embarq will need to have to
19 respond to the revenue loss, and there are a few
20 theoretical options.

21 So imagine if Embarq loses the money that
22 Sprint and AT&T proposes it loses. Embarq's
23 management will ask, "Well, how do we get this money
24 back?" And imagine there's a number of theoretical
25 options it has -- and, again, I underline

1 "theoretical."

2 It could do nothing and say, "Okay, fine,
3 we're not going to do anything about it." It could
4 say, "Well, let's try to increase prices in all of
5 Virginia," or it could say, "Well, let's increase
6 prices but not in all of Virginia; we're just going to
7 focus on the areas where we incur a loss."

8 It could try to do the same thing with
9 network expenses. It could try to lower network
10 expenses all throughout Virginia, or, again, just
11 lower network investments only in the areas where it
12 loses money.

13 It could try to do the same thing with
14 operating expenses; either reduce operating expenses
15 in all areas or reduce operating expenses in only the
16 areas where it loses money.

17 Then it could try to see whether there's
18 another fund it could get the money from, such like it
19 states a specific USF fund, or it could say, "We want
20 to pull out. We aren't going to serve those areas
21 anymore where we incur loss." Those are sort of the
22 theoretical options that Embarq's management would
23 face.

24 Q. Now, Mr. Dippon, are all these
25 theoretical options economically feasible?

1 A. No, they are not. Actually, when you go
2 through and study the economic forces that are
3 inherent in those options you will realize it boils
4 down to only a few options that are actually feasible.

5 Q. All right. Let's go through the options.
6 First of all, could Embarq do nothing?

7 A. Absolutely not. Embarq cannot afford to
8 serve an area where it loses money. Also, it has a
9 fiduciary duty to its shareholders not to do so. A
10 firm is profit-maximizing by theory. If a company
11 incurs losses what it will do is it will do something
12 about it; either pulling out or doing something else
13 about it.

14 Q. All right. Could Embarq increase prices
15 for local services in all the areas it serves in
16 Virginia?

17 A. No, it could not. As I've shown in my
18 testimonies, Embarq faces strong competition in its
19 nonrural areas, so even if you would try to increase
20 prices it will be severely limited. I can't say for
21 certain that it couldn't raise prices by a penny, but
22 it could not significantly increase prices due to the
23 competitive forces, because, very simply, another
24 carrier would come in and say, "Well, thank you very
25 much. Due to increased prices, I'm going to undercut

1 those prices and take away your customers." So that's
2 not an option.

3 Q. So let me ask you, are Mr. Nurse and
4 Mr. Appleby correct when they suggest that the pricing
5 flexibility is sufficient for Embarq to recover its
6 lost access revenue?

7 A. No. As I've said before, you can't shoe
8 this into price inflexibility and say, "Give up that
9 revenue; try to recover it; you're on your own."
10 Because, I'm telling you, in those nonrural areas they
11 will not be able to recover that revenue through
12 pricing flexibility because competitive forces will
13 come in and will not allow Embarq to do so.

14 Q. Could Embarq increase prices for local
15 service in areas where it charges rates below cost?

16 A. It possibly could, and simply based on
17 the fact that competitive carriers have chosen not to
18 enter, so there is little competition and sometimes no
19 competition -- or at least no direct competition -- in
20 those areas, the market forces are more limited.

21 And Embarq could try to raise rates.
22 Now, the question is going to be by how much, because
23 political forces will come in at some point, and
24 people will start to complain when they see
25 significant price increases in those rural areas.

1 Q. So the low-cost in rural areas. Is that
2 what you're talking about?

3 A. That is correct, that will be rural
4 areas.

5 Q. Could Embarq reduce network investments
6 throughout the areas it serves, or is this simply a
7 threat that's suggested by Mr. Appleby?

8 A. Well, again, I don't think I've ever used
9 the word "threat" myself. I just put out what I see
10 as an economist the options are.

11 Reducing network investment in all areas
12 is not possible for the same reason as I stated; that
13 you cannot increase prices in all areas, as
14 competitive forces will severely limit that.

15 Q. Could Embarq reduce network investments
16 in areas where it charges rates below cost?

17 A. Yes, it could, for the same reason as I
18 stated; that it could actually try to increase prices
19 in the rural areas.

20 Q. Could Embarq reduce operating costs
21 throughout its territory?

22 A. No, very likely not.

23 There's two reasons for that. First of
24 all, it's competition again. But, second, Embarq has
25 been under price cap regulation for 13 years, so,

1 presumably, if it could have lowered operating
2 expenses they would have already done so, because that
3 would have translated directly into a profit.

4 Q. Could Embarq reduce operating costs in
5 areas where it charges rates below cost, Mr. Dippon?

6 A. Alone, probably not, because also in
7 those areas it has been under price cap regulation.

8 What it could probably do is it could
9 lower operating expenses, in addition to doing
10 something else; maybe lower service quality or lower
11 investments.

12 Q. And these are areas below cost. These
13 are rural areas, correct?

14 A. Predominantly rural areas, yes.

15 Q. Could Embarq seek compensation from a
16 state-specific Universal Service Fund?

17 A. No, there's no state-specific Universal
18 Service Fund.

19 Q. And, finally, could Embarq pull out of
20 areas where it cannot recover its costs?

21 A. No, it cannot. And I think that is the
22 most important point to consider in this proceeding;
23 is that the subsidy that Embarq receives is for the
24 regulatory burden of being carrier of last resort.

25 Competitive carriers do have the ability

1 to get into an area and pull out of the area if it
2 doesn't make money. Embarq does not have that
3 ability, so it cannot pull out of those areas.

4 Q. So what is the only feasible option to
5 Embarq, in your opinion?

6 A. Well, it boils down to very few options.
7 My recommendation would be to Embarq to say, "Well,
8 try to increase your prices in rural Virginia; maybe
9 try to reduce network investment in rural Virginia;
10 maybe you can try to do something with operating
11 expenses."

12 But the bottom line is it boils down to
13 the brunt; that the brunt of this access revenue --
14 proposed access revenue reduction will be felt in
15 rural Virginia.

16 Q. Would your answer change if this
17 Commission were to grant Embarq more pricing
18 flexibility?

19 A. No. It's been suggested that if the
20 current pricing flexibility is not enough there's a
21 procedure for Embarq to apply for more pricing
22 flexibility, but it really doesn't serve any good,
23 because it's the competitive forces that will tell
24 Embarq how much it can raise prices, if by any means
25 at all.

1 Q. Now, Mr. Dippon, in his rebuttal
2 testimony, at page 13, Mr. Appleby claims that it is
3 your belief that Embarq will not need to change its
4 VoIP bundle prices. Is that your testimony?

5 A. No, absolutely not. Mr. Appleby must
6 have misunderstood. What I said is two things about
7 bundles.

8 I said, first of all, the intrastate
9 switched access portion of the bundled cost is very
10 minor, so if you were to reduce that portion it likely
11 will not have an impact on bundled prices, or it will
12 have a small impact on bundled prices.

13 But I've also said -- and that's for all
14 carriers. I said bundled prices are set
15 competitively. So, actually, Embarq would like to
16 increase bundled prices, but it can't because they're
17 set nationwide, sometimes statewide, and they are
18 under competitive constraints.

19 So Embarq cannot increase bundled prices,
20 so it's quite the opposite, what I said.

21 Q. Is Mr. Appleby correct in claiming in his
22 rebuttal testimony, at page 16, that Embarq has a
23 competitive advantage due to local rates that are
24 subsidized by access charges?

25 A. No. Again -- and I've said this

1 before -- the subsidy does not come without cost. The
2 cost is that Embarq is carrier of last resort and is
3 obligated to provide service, even if that means it
4 incurs a loss. That's what the subsidy is for. The
5 subsidy is competitively neutral in that aspect.

6 Was it true -- Mr. Appleby's statement
7 could only be true if there was no obligation and that
8 subsidy would just be given out right, and that's not
9 the case.

10 Q. Now, on page 18 of his rebuttal testimony
11 Mr. Appleby claims that you explained that lower
12 levels of competition in rural areas are at least
13 partially the result of lower retail local service
14 rates.

15 Do you agree with this characterization
16 of your testimony?

17 A. I have to admit I had to read it a couple
18 of times to understand it. I'm not quite sure I'm
19 even getting it together right now.

20 But I believe Mr. Appleby's point was
21 that I somehow admit that the subsidy itself allows
22 Embarq to charge lower rates and those lower rates
23 prevent entrants, wireless, to come in and offer
24 service because those rates are so low. I entirely
25 disagree with that, particularly for wireless.

1 Wireless responds to different
2 competitive forces than wireline line, so a wireless
3 carrier can't go into an area and charge a higher
4 price. It offers an economically different product.

5 And, furthermore, wireless has entered in
6 areas where Embarq's intrastate switched access rates
7 are what they are and Embarq's basic local exchange
8 service rates are what they are.

9 Q. Why do you think Sprint has decided not
10 to enter certain rural areas in Virginia?

11 A. Well, I can't say for sure because, I
12 mean, I believe we would have to ask Sprint about
13 that, but typically it's the case if it makes no
14 financial sense to enter an area then they will not.
15 If there's a chance to make a return, a profit, in
16 areas, it would go in.

17 And, actually, if you look at maps of
18 Virginia you will see that wireless is available just
19 right down the highway or major streets, and as soon
20 as you go out a little bit from those areas you will
21 see there is no coverage. Now, there is no other
22 explanation. Sprint could serve those areas, but it
23 decided not to serve those areas, and most likely for
24 financial reasons.

25 MR. PAGE: Mr. Dippon is now available

1 for cross-examination.

2 THE HEARING EXAMINER: Thank you.

3 Any questions?

4 CROSS-EXAMINATION

5 BY MR. KEFFER:

6 Q. Good morning, Mr. Dippon. I'm Mark
7 Keffer with AT&T.

8 A. Good morning, Mr. Keffer.

9 Q. Let me make sure I understand the
10 testimony that you just gave in your oral surrebuttal.

11 If I boil it down, what I think you
12 said -- and you correct me if I'm wrong -- is that
13 Embarq has virtually no opportunities available to it
14 to raise prices for any of its customers.

15 A. No, I -- I mean, are you asking me
16 whether I agree with that? I should maybe wait --

17 Q. Is that what you just said? I mean,
18 I'm --

19 A. No. I mean, you summarized things, and
20 by summarizing you necessarily simplified what I said.
21 I would not agree with that characterization.

22 Q. It can raise prices for some customers?

23 A. It can try to raise prices in rural
24 Virginia, and it's more likely to succeed than if it
25 were to raise prices in nonrural Virginia.

1 Q. Okay. Let's talk about what you're
2 calling "rural Virginia."

3 And when you started you said that Embarq
4 really faces no competition in those areas, and I'm
5 wondering if we've got a chicken-and-egg issue going
6 on here.

7 Is the reason that Embarq faces no
8 competition in those areas, in your economist's view,
9 because its current prices are so low relative to what
10 you perceive its costs to be?

11 A. No, and I think after I address that
12 there's two reasons for it.

13 First of all, take, for instance, a
14 wireless carrier. A wireless carrier can enter with a
15 product that is more expensive than basic local
16 exchange service. That is because wireline customers
17 are not necessarily in the same economic market as
18 wireless customers, so they respond to different
19 market forces.

20 And just look at it. I mean, wireless
21 customers have entered in many areas where Embarq and
22 other carriers charge a regulated and subsidized lower
23 rate.

24 Q. So, if Embarq raised its prices in what
25 you're calling "rural Virginia," in your view that

1 would have no impact whatsoever on whether other firms
2 decided to enter the market?

3 A. If Embargo were to raise rates in those
4 areas -- it all depends. I could see that there's an
5 increase in competition, but the increase in
6 competition comes from the fact that carriers might
7 see there's some money to be made.

8 But I don't see that anywhere -- from a
9 wireless carrier certainly that's not the case, but
10 maybe from a cable provider that could be the case.

11 Q. So the answer to my question is, yes, if
12 the price goes up other firms may find it attractive
13 to enter those --

14 A. I admit it's a possibility, but there's
15 nothing that prevents them right now -- from entering
16 right now.

17 If you increase prices in those areas it
18 will not impact the -- or should not impact the
19 competition from wireless carriers. I can't be that
20 sure that it will not impact competition from cable
21 providers.

22 Q. Well, I mean, you're going in circles
23 here, so let me see if we can straighten out the line.

24 You said there's no competition from
25 wireless carriers in those rural areas today, and

1 there's no competition from cable companies in those
2 rural areas today. My question was if the price went
3 up would you expect to see more competition than there
4 is today?

5 A. You know, that's not what I said, and
6 that's why I'm not agreeing with you that I'm running
7 in a circle here.

8 First of all, I did say that there is
9 wireless competition in some of these areas,
10 regardless of the low price, and I said that if you
11 were to increase the prices it will not impact whether
12 wireless enters or does not enter.

13 What you have to understand is these are
14 different economic markets. That's what I'm trying to
15 get across, and I'm not sure I'm doing a good job in
16 getting that across.

17 Q. "These" being what markets? Tell me the
18 markets that you're differentiating here. Is it
19 wireless and wireline? Is it rural and nonrural?

20 A. Wireless and wireline. Wireless
21 subscribers are not necessarily in the same market as
22 wireline subscribers. They respond to different
23 market forces.

24 So whether you offer wireless in those
25 areas should not be impacted heavily -- I can't say

1 not at all, but it shouldn't be impacted heavily by
2 the price that Embarq charges -- or any ILEC charges
3 in those areas, because you're offering a different
4 product. You're offering a product that has more
5 mobility. It's an economically different product.

6 Q. So if they're different markets explain
7 to me how the price of wireless service constrains
8 Embarq's ability to raise its rates in rural areas.

9 A. Good point. Good point.

10 Wireline subscribers are in the same
11 market as wireless subscribers, but wireless
12 subscribers are not in the same market as wireline
13 subscribers.

14 I can understand that that's confusing to
15 non-economists, it's an econometric market definition,
16 but that's what it is. I can try to explain it, but
17 I'll ask you first -- or you tell me whether that was
18 sufficient of a response. I'll be happy to give an
19 example, if that's needed.

20 Q. Well, let's talk about the nonrural areas
21 that Embarq serves.

22 Now, you're aware Embarq has not raised
23 any of its prices in over 20 years.

24 A. I understand that's the case.

25 Q. Okay. And as an economist and someone

1 advising the company, that's of no concern to you?
2 That makes perfect sense?

3 A. Well, I'm not advising the company on
4 those aspects, so it has never come up.

5 Q. Okay. I'm asking you the question now.
6 If you were advising Embarq on its pricing decisions
7 and you learned that they had not changed their prices
8 in 20 years, as an economist would that be of concern
9 to you?

10 A. Not necessarily at face value. I mean, I
11 have to do my research and ask a whole bunch of
12 questions why and why is that the case. I can't just
13 sit here and look at a symptom and say, "Well, that's
14 a concern." I would have to find out first why that's
15 the case.

16 I mean, one thing I can think of is
17 regulation. Rates have been regulated. I would have
18 to see whether all or none of the price have changed.
19 So I don't think I can respond to that just sitting up
20 here and having this free dialogue.

21 Q. Okay. And thank you, because you took me
22 back to the point that I had forgotten to raise
23 earlier but that you reminded me of, and that's the
24 issue of regulation.

25 When you started your oral surrebuttal

1 you said that Embarq had not raised its rates in rural
2 areas because they had been heavily regulated. Now,
3 today Embarq has some pricing flexibility, right? So
4 the onerous regulation that you discussed is no longer
5 present in the way that it once was.

6 MR. PAGE: I'm going to object to the use
7 of the order "onerous." I don't think that's part of
8 the testimony, so --

9 BY MR. KEFFER:

10 Q. How would you describe rate-based rate of
11 return regulation from 1975?

12 A. I'm not sure how to describe that. You
13 know, certainly there are markets in which regulation
14 is justified, and if you go back to 1975 there
15 probably were good reasons to do so.

16 Regulation is still in place today.
17 Sometimes it's justified; sometimes it is not.

18 Q. When you started your oral surrebuttal
19 testimony you raised regulation as an issue, so what
20 did you have in mind when you were talking about
21 regulation?

22 A. Maybe you have to point me to the exact
23 place where I did it, but I'm telling you what I
24 recall on my surrebuttal.

25 I was talking about the subsidy itself.

1 The subsidy has been heavily regulated, and the
2 subsidy was designed to allow Embarq to recover its
3 costs in areas where it incurs a loss. So it makes it
4 financially whole. Or that, at least, is the
5 objective. The overall objective of society is that
6 we can keep local exchange rates in Virginia
7 affordable.

8 Q. Okay. Let's talk about that for a
9 second. We'll jump to that.

10 Affordable. Did you do any studies to
11 determine what an affordable local exchange rate is in
12 Virginia?

13 A. No. There's absolutely no need to do
14 one, not at the magnitude of numbers that you're
15 looking at.

16 I can't reveal them right now unless we
17 go on confidential record, but there's no -- there's
18 no need to do the study at all.

19 Q. Now, if Embarq raised its prices in areas
20 where it faces competition it's possible, is it not,
21 that its competitors might raise their prices, too?

22 A. I'm at a loss why they would do that.
23 Maybe you can explain that to me.

24 Q. Well, you buy gasoline at the corner gas
25 station, I assume, and when the station on one corner

1 raises its price sometimes the station on the opposite
2 corner raises its price, too.

3 Have you ever seen that?

4 A. I've seen it many times. My --

5 Q. And what would an economist call that
6 when firms in competing markets tend to observe one
7 another and --

8 A. There's really no one response. First of
9 all, just talking about your gas station analogy, what
10 those gas stations do -- they respond to changes in
11 cost, crude oil, okay? So if Embarq was to increase
12 its prices because its costs increased that does not
13 mean that other carriers will follow suit, because
14 their prices have not been increased. In fact, you
15 would expect the opposite.

16 Let's say your gas station, only one gas
17 station at that intersection, had an increase for
18 whatever reason, a cost increase. You would not
19 expect the other gas stations to raise its prices. In
20 fact, what you would expect -- if that one gas station
21 were to try to increase prices the other gas stations
22 might just stay at the same rate, because when you
23 pull up to the intersection you're not going to go to
24 the gas station with the highest price, you're going
25 to go to the one with the lowest.

1 Now, another way is unless you're
2 suggesting that the phone companies collude and say,
3 "Hey, we're going to be setting rates at the same
4 place starting tomorrow" -- that's illegal -- then I
5 can't see why they would increase the price along with
6 Embarq. It's a competitive environment; prices will
7 compete downwards.

8 Q. Let's go back to my question.

9 Have you ever seen a scenario where one
10 gas station raises its price and another gas station
11 does the same thing?

12 A. I believe I just answered that same
13 question. I told you that what's happening there is
14 they're responding to an increase in cost.

15 They all buy crude oil. If the price of
16 crude oil goes up, the price of gasoline goes up. So
17 they're not responding to each other. What they're
18 responding to is a change in the price of crude oil.

19 Q. We often hear that in competitive
20 markets -- and I think you defined, I think, nonrural
21 areas that Embarq is competing in as competitive
22 markets; that firms are price takers.

23 A. Is that a question?

24 Q. I'll make it one.

25 In my gas station example the first

1 station raises its price, and the station across the
2 street sees an opportunity to raise its price as well,
3 even though its cost of supply did not go up. Might
4 that happen? Do you see that happen? Would you
5 expect that to happen, as an economist?

6 A. You asked me three questions, and the
7 answer to every single one is a "No."

8 Q. All right. In your testimony I think you
9 say that Embarq needs the subsidy, relative to
10 Verizon, because Embarq is different than Verizon; it
11 serves a more rural territory, it has higher costs.

12 Is that a fair characterization of your
13 testimony?

14 A. I just want to make sure that what I said
15 is Embarq is different. I want to warn this
16 Commission not to rubber stamp and just say, "Well, we
17 did one thing with Verizon; we're going to be doing
18 the same thing with Embarq."

19 What I highlighted in my testimony is the
20 fact that Embarq is different. I did not say that
21 Verizon did not need the subsidy. I was not in the
22 Verizon case, and I wouldn't want to make that
23 assessment without having looked at specific numbers.

24 Q. Well, did this Commission reduce the
25 level of subsidy that Verizon receives? Your

1 testimony is it should not do the same thing for
2 Embarq because Embarq serves a different type of
3 territory that's more rural and high-cost. Is that --

4 A. I think that is a fair characterization,
5 yes.

6 Q. Okay. Now, would you agree with me that
7 the largest area that Embarq serves, the largest
8 municipality that Embarq serves in its territory, is
9 Charlottesville?

10 A. Subject to check. I don't know it.

11 Q. Okay. And would you agree, subject to
12 check, that Charlottesville had a population,
13 according to the U.S. Census in 2007, of 41,228?

14 A. I'll take your word for it.

15 Q. Now, Mr. Dippon, have you ever been to
16 West Virginia?

17 A. Unfortunately, I've not, no.

18 Q. Okay. Do you have any idea what the
19 largest city in West Virginia is?

20 A. No, I don't.

21 Q. Do you know anything at all about West
22 Virginia? Would it be a rural area, mountainous,
23 rugged terrain, high-cost, similar to the area that
24 Embarq serves in Virginia?

25 MR. PAGE: You know, I'm going to object

1 to what I perceive to be the line of questions.

2 Obviously, Mr. Dippon did not testify
3 about what's happening in West Virginia or what's not
4 happening in West Virginia. He testified about
5 Virginia. Whether there are rural areas in West
6 Virginia that are comparable to Charlottesville I
7 think is totally irrelevant to this case, and, so, I
8 object.

9 THE HEARING EXAMINER: Do you want to
10 explain the relevance?

11 MR. KEFFER: Sure, Your Honor.

12 His testimony is that Embarq needs a
13 subsidy because it serves a rural, high-cost area
14 that's most different than Verizon's territory in
15 Virginia. But what I'm going to try to get him to run
16 through is a comparison that says in West Virginia,
17 which has similar cost characteristics, similar rural
18 nature, a city -- the largest city is comparable in
19 size to Charlottesville -- that in West Virginia,
20 where all those cost characteristics exist, that
21 Verizon-West Virginia has a 1FR rate, \$29, and it has
22 access charges that are going to interstate by the end
23 of 2010.

24 MR. PAGE: Well, it's still irrelevant,
25 Your Honor.

1 I'm sorry. Are you done?

2 It is irrelevant. And, in fact, you
3 know, unless Mr. Keffer is going to be able to show
4 the witness the entire regulatory scheme in West
5 Virginia it will be an apples-to-oranges comparison,
6 and it really won't help this proceeding.

7 And this is the kind of testimony,
8 frankly -- and, in addition, Mr. Dippon said he's
9 never been to West Virginia, and we presume he's not
10 testified about West Virginia. So this is all
11 relevant to his testimony, his claims about what's
12 happening in Virginia, rural versus nonrural.

13 THE HEARING EXAMINER: I think I've heard
14 his testimony to be that the unique nature of Embarq
15 is the reason that they need the access charge, and I
16 believe the witness will be able to deal with any of
17 the questions that the attorney may ask about that,
18 and I'm going to overrule the objection.

19 BY MR. KEFFER:

20 Q. Well, Mr. Dippon, now that you know where
21 I'm going, this is probably going to be even more fun
22 than I've been having up until now.

23 Do you want to venture a guess as to the
24 largest city in West Virginia?

25 A. You know, as a professional expert, I

1 won't venture any guesses.

2 Q. All right. Would you accept, subject to
3 check, that it's Charleston?

4 A. Subject to check.

5 Q. And would you accept, subject to check,
6 that the population of Charleston is 50,478, according
7 to the U.S. Census Bureau, as of 2007?

8 A. Sure, subject to check.

9 Q. And would you agree that certainly
10 relative to New York City or San Francisco or
11 Los Angeles that Charlottesville and Charleston,
12 West Virginia, would be comparable in size?

13 A. In absolute population, yes.

14 Q. All right. Now, are you familiar with
15 the territory that Embarq serves in Virginia? Did you
16 spend any time looking at the characteristics of the
17 area, the terrain, the population densities? Was that
18 of any concern to you?

19 A. Well, it partially is.

20 And to answer your question, yes, I've
21 spent some time. I haven't driven around there to
22 look at the areas, but I have spoken to several
23 individuals at Embarq about their territory; where
24 they incur high costs, why they incur high costs, I've
25 looked at service territories where wireless carriers

1 go. And I think Dr. Staihr has some of that in his
2 testimony.

3 So the answer is, yes, I have spent some
4 time on that.

5 Q. Okay. And if you look at the map you
6 would see that some of Embarq's service territory
7 bends around into Southwest Virginia along the border
8 with West Virginia.

9 A. That's what I recall to be correct, yes.

10 Q. And assuming that you took geography at
11 some point in your younger days, do you know anything
12 about the geography of West Virginia?

13 A. Unfortunately, the geography that I took
14 in my early days were basically based on European
15 geography. You might have detected that from my
16 accent. It did not include West Virginia,
17 unfortunately.

18 Q. And what do you know about the geography
19 of West Virginia, if anything?

20 MR. PAGE: You know, I'm going to object.

21 THE HEARING EXAMINER: I'll sustain that
22 one.

23 MR. PAGE: But I love West Virginia.

24 (Laughter.)

25 BY MR. KEFFER:

1 Q. Would you accept, subject to check, that
2 West Virginia has the same sort of rugged, mountainous
3 terrain that is present in much of Embargo's service
4 territory?

5 A. I would probably accept that, subject to
6 check, yes.

7 Q. Do you know who the largest incumbent
8 local exchange carrier is in West Virginia?

9 A. No, I don't.

10 Q. Would you accept, subject to check, that
11 it's Verizon?

12 A. Subject to check. And can you please
13 tell me how you define "largest"? Number of lines?
14 Service territory? Anything else?

15 Q. Service territory, number of subscribers,
16 number of lines served.

17 A. Okay.

18 Q. Would you accept, subject to check, that
19 in West Virginia Verizon has a 1FR rate of \$29 a
20 month?

21 MR. PAGE: Your Honor, I have to say I
22 object.

23 This is irrelevant to the question of
24 what should be Embargo's access charges in Virginia.
25 We heard a lot of objections in discovery when it was

1 perceived we were going afield -- far afield -- and
2 the comparison of West Virginia Verizon rates to, I
3 presume, Verizon's Virginia rates -- I guess that is
4 where we're going -- really is irrelevant to this
5 case, and I'm going to object to all these questions.

6 MR. KEFFER: Well, it absolutely is
7 relevant, Your Honor.

8 His testimony is -- in fact, Embarq's
9 testimony is -- that Embarq just could not possibly
10 continue serving its territory and -- could not
11 continue serving its territory if it increased its
12 residential, business, basic local exchange rates, by
13 any amount whatsoever. What I'm trying to get at
14 through this line of testimony is in a neighboring
15 state with the same basic geography, a lot of the same
16 cost characteristics, an environment where you've got
17 cities of comparable size, that Verizon has
18 established a \$29 rate for flat-rated residential
19 local service, they're reducing their access charges
20 to interstate levels, and -- I didn't mention this
21 before, but they're doing it voluntarily. So --

22 MR. PAGE: You know, I understand we're
23 arguing here, but we're introducing evidence that's
24 not in the record and that this witness has testified
25 he can't enter into the record. So, you know, when

1 you say that what Verizon is doing -- when Mr. Keffer
2 says what Verizon is doing, that is outside the record
3 and really has absolutely no relevance to this
4 proceeding.

5 Mr. Dippon did not testify that Embarq
6 would be unable to serve rural customers if access
7 charges are increased. What he testified to was that
8 it would make it very difficult, that it would create
9 difficult choices for Embarq to make if you lower
10 access charges to the extent recommended by the
11 parties in the case. That's his testimony. He ran
12 through several possible scenarios, and, yes, one of
13 them was, pull out of the service territory. He said
14 that was not possible because of our obligation to
15 serve universally.

16 So, this is -- you know, what Verizon has
17 done in West Virginia is totally irrelevant and
18 probably should have been something that AT&T
19 presented in its testimony. Mr. Dippon is not going
20 to be able to testify about this. He's already said
21 he's not been to West Virginia. He doesn't know
22 anything about West Virginia.

23 So I'm going to object to this line of
24 questioning.

25 MR. KEFFER: I'll tell you what, Your

1 Honor. Rather than continue this with Mr. Dippon,
2 I'll just take it up with Mr. Nurse when he takes the
3 stand.

4 THE HEARING EXAMINER: That's fine.

5 MR. KEFFER: That might move it along a
6 little more quickly. I have a feeling he'll be a
7 little more cooperative.

8 Not that you haven't been a fount of
9 knowledge, Mr. Dippon.

10 (Laughter.)

11 THE WITNESS: Thank you.

12 THE HEARING EXAMINER: That's fine.

13 BY MR. KEFFER:

14 Q. Let's see. You didn't do a price
15 elasticity of demand study in the case, did you?

16 A. I think I answered that question before.
17 There's no need to do that with the order of magnitude
18 that we're talking about here.

19 Q. Okay. Now, the subsidies that we're
20 talking about here that Embarq is receiving -- where
21 do those come from?

22 A. You're referring to the CCL? Are you
23 asking where they come from?

24 Q. Where does the money come from?

25 A. Well, it comes --

1 Q. Who is paying them?

2 A. All depends which witness you believe.
3 One witness says -- and I'm not sure whether it's
4 Mr. Appleby or Mr. Nurse; we'll have to go back.

5 One says it's only IXEs -- so that will
6 be Mr. Nurse -- and Mr. Appleby says it comes from all
7 the carriers. And we can all argue about where it
8 comes from, but it comes mainly from IXEs and
9 sometimes also from other carriers.

10 Q. And where do the IXEs get the money?

11 A. They recover it from their customers.
12 I'm not sure how, exactly, they do that. That's their
13 pricing strategy, which is confidential. But I
14 obviously also can state the switched access fee that
15 both AT&T and Sprint charge to its long distance
16 customers, so I would think it comes from there.

17 Q. Well, to short circuit it, would you
18 agree with me -- I doubt it, but I'll ask -- that
19 consumers in the remainder of Virginia are paying long
20 distance prices that are providing this subsidy to
21 Embarq to cover its costs of providing local exchange
22 service in its territory?

23 A. Well, somebody is paying for it, and it
24 is the long distance subscribers, if -- that is
25 assuming that if you, as a company, pass on all these

1 costs to your subscribers. I would agree with that.

2 Q. All right. So, in your view it's
3 important that consumers in Virginia do that to make
4 local telephone service affordable in Embargo's
5 territory.

6 A. I don't think I said that it's important.
7 That's one way that that has been done for many years,
8 so that's one way of meeting this social goal of
9 making telephone service available and affordable in
10 all of Virginia.

11 So that's just one way it has been done.
12 I have never said that that's important. I never said
13 that that's the only way of doing it.

14 MR. KEFFER: All right. Those are all my
15 questions.

16 THE HEARING EXAMINER: Any questions?

17 MR. NELSON: Your Honor, I just have a
18 few.

19 BY MR. NELSON:

20 Q. Mr. Dippon, a hypothetical:

21 Could one reason a wireless carrier
22 decides not to serve a particular region of Virginia
23 be due to it not having spectrum in that part of
24 Virginia in order to provide service?

25 A. Certainly, if they don't have spectrum

1 they cannot provide their service, yes.

2 Q. Thank you. Another hypothetical:

3 An Embarq customer who has basic local
4 exchange telephone service experiences a rate increase
5 in that BLETs. Is it possible that at some point that
6 customer will switch to an Embarq bundled service
7 product?

8 A. So let me go through there. So you're
9 asking me that question for rural areas, right?

10 Q. Well, we can start with whichever you'd
11 like.

12 A. Okay. Well, because I'm thinking
13 nonrural areas, a price increase in just basic local
14 exchange service is less possible. So if we were to
15 look at rural areas, what you're saying is what
16 happens if just stand-alone BLETs were to be
17 increased.

18 Bundled service would not be increased.
19 There would be a point where that customers says,
20 "Hey, for a little bit more" -- or maybe even less --
21 "I can get a bundled service and get a superior
22 product." I think that's not a crazy idea to assume
23 that that substitution is a possibility.

24 Q. Thank you very much.

25 MR. NELSON: That's all I have, Your

1 Honor.

2 THE HEARING EXAMINER: Thank you.

3 MS. MACKO: I don't have any questions,

4 Your Honor.

5 THE HEARING EXAMINER: Mr. Gillespie?

6 BY MR. GILLESPIE:

7 Q. Good afternoon, Dr. Dippon.

8 One thing I would initially like to clear
9 up -- this involves Verizon again but within the State
10 of Virginia -- are you familiar with the regulatory
11 pricing scheme that Verizon now operates in Virginia
12 with?

13 A. I'm sorry. Can you speak up a bit? I
14 just have a hard time hearing you all the way up here.

15 Q. Are you familiar with the pricing scheme
16 that Verizon operates under in Virginia?

17 A. No. I have trouble understanding what
18 you mean by "pricing regime," with that a strategy,
19 but I wouldn't -- I'm not aware of that strategy or a
20 pricing regime, no. I don't know what they charge or
21 how they charge, if that's what you're asking.

22 Q. Okay. Are you aware that they recently
23 had a case in which they got competitive pricing in
24 for their local exchange services in a number of local
25 exchanges in Virginia?

1 A. I know that there was a case similar to
2 this one that Verizon went through. I'm not exactly
3 sure what they got and how much pricing flexibility
4 and where they were reclassified, if anywhere. So I'm
5 not sure of that.

6 Q. Okay. You wouldn't be prepared to
7 dispute that Verizon has, in fact, raised its prices
8 in some of those areas designated as competitive?

9 A. No, and I don't think that you can.
10 Understand prices -- Embarq can increase prices in
11 rural areas, but in competitive areas, even if Verizon
12 did it doesn't tell me anything at this point whether
13 they will be able to sustain the price increase. I
14 also don't know how large that price increase was.

15 So those are both things we would have to
16 look at.

17 Q. Can you tell me the name of any
18 competitor in Embarq's competitive areas in Virginia
19 that offers basic local exchange services outside of a
20 bundle?

21 A. Can you repeat that, please?

22 Q. Can you tell me the name of any
23 competitor in Embarq's competitive areas that offers
24 basic local exchange service that's not part of a
25 bundle?

1 A. No. You probably would have to ask
2 another witness on that.

3 Q. Okay. Let me ask you to go to page 31 of
4 your rebuttal testimony.

5 A. Did you say page 31?

6 Q. Page 31.

7 A. Yes, I'm there.

8 Q. At lines 8 through 19 you make a
9 statement regarding Embarq's new Alternative
10 Regulatory Plan adopted in Case No. PUC-2008-00008.
11 You state, and I quote, "What AT&T and Staff must
12 consider is that when the Commission and Embarq worked
13 out the details of the Alternative Regulation Plan
14 neither party took into consideration the effect of
15 switched access reductions."

16 Dr. Dippon, did you take part in working
17 out the details with the Commission and Embarq?

18 A. I'm sorry, just one clarification: I'm
19 Mr. Dippon, not Dr. Dippon.

20 Q. Okay.

21 A. But the answer to your question is, no,
22 the Alternative Regulation Plan was put into effect --
23 or the negotiations happened prior to Sprint's
24 petition, so I was not part of that negotiation, but
25 that is my understanding.

1 Q. Okay. Do you know who at Embarq worked
2 out the details with the Commission?

3 A. I don't know who worked out the details
4 with the Commission. You would have to ask somebody
5 else.

6 Q. Do you know who at the Commission worked
7 out the details of the Alternative Regulatory Plan?

8 A. Maybe Mr. Skirpan. I don't know.

9 THE HEARING EXAMINER: I can answer that.
10 No.

11 THE WITNESS: Okay. So it was not
12 Mr. Skirpan.

13 (Laughter.)

14 BY MR. GILLESPIE:

15 Q. Do you know if the Commission adopted the
16 Alternative Regulation Plan that was submitted by
17 Embarq originally in case 2008-00008?

18 A. No, I don't. Let me remind you what I'm
19 here for.

20 I'm here for to explain to the Commission
21 whether there's a need to reduce Embarq's intrastate
22 switch access rates and the consequences of it. So
23 I'm afraid if you're asking all those questions the
24 answer will be, "I don't know." That's definitely not
25 my assignment.

1 Q. Okay. So you're not in a position to
2 dispute that the Commission, in the final order,
3 modified what Embarq had submitted?

4 A. I can't hear that answer (sic). I'm
5 sorry. If you could speak up a bit that would help me
6 so much.

7 Q. Okay. You're not in a position to
8 dispute that the Commission modified the original
9 proposal of Embarq for an Alternative Regulatory Plan?

10 A. No, I believe that's right. I might have
11 heard that.

12 Q. Okay. And I believe Mr. Dippon has
13 acknowledged that neither party --

14 THE HEARING EXAMINER: Mr. Gillespie, if
15 you could please speak into the mike. If you would
16 just sort of move a little bit or --

17 MR. GILLESPIE: Okay. Is this better? I
18 could go to the podium, Your Honor.

19 THE HEARING EXAMINER: That would be
20 good.

21 MR. GILLESPIE: Okay.

22 BY MR. GILLESPIE:

23 Q. I believe, Mr. Dippon, you stated that
24 neither party, Embarq or the Commission, took into
25 consideration the effect of access -- of reducing the

1 prices of switched access.

2 A. What I said is -- I think my testimony
3 speaks for itself -- is the Commission has not
4 addressed at all whether the pricing flexibility
5 embedded in the Alternative Regulation Plan is
6 sufficient or can even cover the switched access
7 revenue reduction that is proposed by Sprint in its
8 motion.

9 MR. GILLESPIE: Your Honor, at this point
10 I'd like to pass out an affidavit of Steve Parrott
11 from the Alternative Regulatory Plan.

12 I think that, if need be, Ms. Cummings
13 could address what was contained in that document,
14 but --

15 MR. PAGE: Well, maybe before this is
16 done -- maybe this would help: To ask the witness if
17 he is familiar with it or if he has seen it, and then
18 if he says, "No" and maybe directs you to another
19 witness that would be helpful.

20 THE HEARING EXAMINER: Well, I'm troubled
21 by the fact that he put this in his testimony, what
22 the Alternative Regulatory Plan did or didn't cover,
23 and that's where these questions are going.

24 I mean, if he just wants to strike that
25 testimony, and then you could deal with it with

1 another witness, that would be fine.

2 MR. PAGE: Well, he has explained and can
3 continue to explain those sentences in his testimony
4 about the alt reg plan. I'm just concerned -- well,
5 not concerned. I mean, if we're going to pass out
6 something that -- an affidavit in another case and
7 Mr. Dippon said he was not involved in that case, I'm
8 just --

9 THE HEARING EXAMINER: Well, how can he
10 make the statement, though, what was considered and
11 isn't considered and now you're not going to let him
12 answer any questions on what was considered or not
13 considered? I mean, you can have it one way or the
14 other.

15 MR. PAGE: Mr. Dippon has testified that
16 he's obviously read the Alternative Regulatory Plan,
17 and he's talking about the effects of the plan on the
18 ability of Embarq to recover its possibly reduced
19 access charges. And he --

20 THE HEARING EXAMINER: That's not what it
21 says here, though. He says that, "When the Commission
22 and Embarq worked out the Alternative Regulatory Plan,
23 neither party took into consideration the effect of
24 switched access rate reductions."

25 I mean, that's saying what was taken into

1 consideration when the decision was made, and either
2 he testifies to that and answers the questions about
3 what was considered or he doesn't testify to it. This
4 is your choice.

5 MR. PAGE: He can answer the questions,
6 obviously, to the extent he can, so I'll sit down.

7 (There was a pause in the proceedings.)

8 THE HEARING EXAMINER: Do you wish this
9 marked?

10 MR. GILLESPIE: Your Honor, can we mark
11 this exhibit?

12 THE HEARING EXAMINER: Yes. I'll mark it
13 as Exhibit 19.

14 (The exhibit was marked for
15 identification.)

16 BY MR. GILLESPIE:

17 Q. Mr. Dippon, do you have before you what's
18 been marked for identification as Exhibit 19?

19 A. Yes, I do.

20 Q. Could you flip over to page 5 of that
21 affidavit of Mr. Parrott and read into the record
22 what's stated at item ten of his affidavit?

23 A. Item ten that starts on page 5? Is that
24 what you're --

25 Q. Correct.

1 A. It's under the heading "Rebalancing
2 Switched Access Rates." It says, "The new plan
3 includes a mechanism by which implicit subsidies in
4 Embarq's intrastate switched access rates can be
5 reduced without putting at risk Embarq's ability to
6 serve as a carrier of last resort. The new plan
7 allows Embarq to recover subsidies lost as the result
8 of access rate reductions by increasing rates for
9 basic local exchange service. The mechanism would
10 produce no increase in Embarq's net revenues but would
11 shift needed cost recovery from one service to
12 currently subsidized services. This mechanism is
13 often referred to as rate rebalancing."

14 MR. GILLESPIE: Your Honor, I would like
15 to move the entry of the entire exhibit.

16 THE HEARING EXAMINER: It's in.

17 (The exhibit was admitted into evidence.)

18 MR. NELSON: Your Honor, excuse me.

19 We were noticing that there doesn't seem
20 to be a date on this affidavit. Is there a date that
21 can be provided?

22 MR. GILLESPIE: We can provide that date.
23 I'm certain that there should be, since it is an
24 affidavit, a notary's acknowledgement that we can
25 furnish. But, if nothing else, this is the part of

1 the initial application that Centel and United filed
2 in Case No. 2008-00008.

3 THE HEARING EXAMINER: Okay. Thank you.
4 BY MR. GILLESPIE:

5 Q. Mr. Dippon, at page 28 in your rebuttal
6 question you were asked the question, "Would a
7 reduction in switched access revenues affect Embarq in
8 the same manner as it did Verizon?"

9 A. I'm sorry. You're on page 28? Can you
10 give me a line?

11 Q. Yes, let me...

12 (There was a pause in the proceedings.)

13 BY MR. GILLESPIE:

14 Q. Okay. I'm talking about, actually, the
15 bottom of page 28 and continuing on the top of
16 page 29.

17 "When Verizon began reducing its
18 \$52 million in carrier common revenue in 2005, Verizon
19 reported that it served approximately 3.2 million
20 access lines in Virginia. In contrast, Embarq serves
21 approximately 360,000 access lines in Virginia. A
22 \$23 million reduction in revenue due to the CCL being
23 eliminated for a company that serves 360,000 lines is
24 vastly different from a \$2 million revenue reduction
25 for a company with over three million access lines."

1 That's your testimony, isn't it, sir?

2 A. Yes, it is.

3 Q. Now, if we were to look at that reduction
4 that Verizon made beginning in 2005, wouldn't it be
5 fair to say, from their perspective, that Embarq has
6 avoided a similar reduction for an additional five
7 years?

8 A. Well, maybe relative to Verizon. I mean,
9 it's a fact that Verizon was being asked to reduce
10 intrastate switched access rate before this Commission
11 rules, so I think there's a time difference in that.
12 I'm not sure why that matters.

13 MR. GILLESPIE: Your Honor, that's all.

14 Thank you, Mr. Dippon.

15 THE HEARING EXAMINER: Any redirect?

16 MR. PAGE: Yes, a few questions. Thank
17 you, Judge.

18 REDIRECT EXAMINATION

19 BY MR. PAGE:

20 Q. Mr. Dippon, let's deal with the
21 Alternative Regulatory Plan first.

22 In answer to Mr. Gillespie's questions
23 you were asked to read an affidavit that was submitted
24 by Steve Parrott on behalf of Embarq. Is that
25 correct?

1 A. That's correct.

2 Q. Do you still have that in front of you?
3 I believe that's Exhibit 19.

4 A. Yes, I do. I have it open on page 5,
5 paragraph 10, that I just read into the record.

6 Q. Why don't you read into the record
7 paragraph 11, which is on page 6, please.

8 A. "Embarq is not proposing rate rebalancing
9 at this time. Reducing the implicit subsidies in
10 intrastate switched access charges is a public policy
11 consideration beyond the scope of Embarq's
12 application. The new plan's provision for rate
13 rebalancing does nothing more than recognize that the
14 implicit subsidies contained in intrastate access
15 charges are critical to sustaining the universal
16 service provision of affordable basic service, which
17 is the hallmark of both state and federal
18 telecommunications policy."

19 Q. Now, how does that relate to your
20 testimony on page 31, lines 8 through 12, when you
21 talk about that the Alternative Regulatory Plan
22 doesn't take into consideration the effect of switched
23 access reductions and is not designed to recover lost
24 revenue from a switched access rate reduction?

25 A. Well, essentially, it's pointing out

1 exactly what I just read into the record, and
2 particularly paragraph ten.

3 What I'm saying here is that the alt reg
4 plan has not looked into Embargo's ability to recover a
5 reduction. And I'm not talking just a little bit of a
6 reduction, I'm talking about the removal of the CCL.
7 It has not taken that into account.

8 If I'm looking at the affidavit that I
9 just read into the record, what it talks about there
10 is -- it talks about that, "The new plan includes a
11 mechanism by which implicit subsidies of Embargo's
12 intrastate switched access rates can be reduced." I
13 don't think I've ever said that no reduction could be
14 recovered. That would not be too strong of a
15 statement.

16 What I do say is that removing the CCL
17 has not been considered in the alt reg plan. It's not
18 inconsistent with what the affidavit that I've read
19 here. What Embargo seems to be asking for is the
20 opportunity to increase prices. It's a possibility.

21 THE HEARING EXAMINER: Let me ask a
22 question in follow-up.

23 I mean, is it your understanding that the
24 choice before the Commission is to either eliminate
25 the CCL or do nothing? What -- I mean, is that your

1 understanding of what this case is about?

2 THE WITNESS: No. The option, as
3 proposed by Sprint and AT&T --

4 THE HEARING EXAMINER: That -- okay. Go
5 ahead.

6 THE WITNESS: The way I understand it,
7 the options proposed by -- or the recommendations
8 proposed by AT&T and Sprint are either phase out the
9 CCL or go to the levels of interstate access charges.

10 THE HEARING EXAMINER: Well, what is your
11 idea of what this case is about? What am I doing
12 here? What am I supposed to do, I guess?

13 THE WITNESS: Well, see whether you want
14 to grant Sprint's petition or seek some resolution in
15 between.

16 THE HEARING EXAMINER: Okay. I mean,
17 it's my understanding that the Commission has asked me
18 to do an investigation and to come up with a
19 recommendation. I mean, from what I understand your
20 testimony, it sounds like I have only two choices;
21 nothing or there.

22 I mean, you've just testified that there
23 could be some reduction, but I don't see that
24 anywhere.

25 THE WITNESS: Well, Your Honor, I'm

1 actually -- I'm responding to, actually, three offers
2 on the table; one by AT&T, one by Sprint, and one by
3 Staff. And all these three offers, the way I've read
4 them, incorporate a drastic reduction of the
5 subsidies, basically; either phasing out or -- phasing
6 it out over time, if you were to look at Staff's
7 recommendation, getting rid of it right away -- I
8 think there's one witness, and, again, I've forgotten
9 whether it's Mr. Appleby or Mr. Nurse -- that says the
10 proposed plan by Staff is actually not aggressive
11 enough because it allows for that phase-out. And then
12 Sprint and AT&T, both -- what they propose are
13 removing the CCL or go to interstate mirroring; that
14 it be dropped to interstate access.

15 I don't think that those are your only
16 options, and I would urge you not to consider those as
17 the only options, because there are many options in
18 between.

19 THE HEARING EXAMINER: Well, the only one
20 that I've heard is not to do anything, or to make no
21 changes at all, which is Embarq's position.

22 So, I mean, I just wanted to make sure
23 that there was an understanding that there could be
24 something in between, which you had just mentioned;
25 that you acknowledge that there was some. And that's

1 the first I've heard it.

2 THE WITNESS: Yeah. No, absolutely. And
3 there is definitely many options in between.

4 One that I personally favor -- and I
5 brought that up in my testimonies -- is establishing a
6 state-specific universal service fund. You can make
7 those implicit subsidies explicit, but you do need
8 to -- well, at least in my opinion as an economist,
9 you do need to give Embarq the ability to recover that
10 revenue and a realistic ability to recover the
11 revenue. And pricing flexibility alone is really not
12 a realistic opportunity.

13 THE HEARING EXAMINER: Thank you.

14 MR. PAGE: And, Your Honor, if I may
15 point out, Mr. Appleby has another alternative in his
16 testimony, and Dr. Staihr, who is our last witness,
17 comments on that as a possibility in his rebuttal, and
18 we could probably talk about that today as well.

19 THE HEARING EXAMINER: Okay. Thank you.

20 MR. PAGE: We mean to be helpful.

21 BY MR. PAGE:

22 Q. So we're talking about the alt reg plan,
23 Mr. Dippon.

24 Are you aware that the affidavit that is
25 Exhibit 19 was attached to the original plan as

1 proposed by Embarq?

2 A. No, I was not aware of that.

3 Q. So are you aware that the plan that was
4 eventually ordered by the Commission differs from the
5 plan that was originally introduced by Embarq?

6 A. I -- that's my understanding, yes.

7 Q. Okay. Thank you.

8 In answer to one of Mr. Gillespie's
9 questions you talked about Verizon, and you -- about
10 Verizon raising prices in areas that are designated as
11 competitive. And you testified that while they may be
12 able to increase rates for basic local service in
13 those areas, they may not be able to sustain those
14 prices.

15 Do you remember that testimony?

16 A. Yes, I do.

17 Q. And is the same true for Embarq?

18 A. Absolutely.

19 Q. And why is that?

20 A. Well, because you have competitive
21 forces. If you were to increase prices -- it's
22 ultimately the market that decides whether you can
23 increase prices or not. You can try to increase
24 prices and maybe tomorrow will see a huge price
25 increase, but what will happen is consumers will

1 switch away from a carrier that increases prices if
2 there are competitive alternatives. Then, after a
3 while, the company will see that its price increase,
4 although getting revenue from some customers, really
5 is incurring a net loss because it loses subscribers
6 and loses their entire revenue.

7 So sustainability is very important in a
8 price increase. Just simply because one carrier
9 raises prices one day that doesn't mean it's
10 sustainable. They might just be trying the market.

11 Q. When you were talking with Mr. Keffer he
12 used the words "onerous regulation." You don't use
13 that in your testimony, do you?

14 A. No, I don't.

15 Q. Do you talk about the "regulatory
16 burden"?

17 A. Yes, I do.

18 Q. What is the regulatory burden that Embarq
19 has here?

20 A. Well, in this case the regulatory burden
21 is really being a carrier of last resort; having to
22 serve high-cost areas at below cost.

23 MR. PAGE: That's all the questions I
24 have, Your Honor.

25 THE HEARING EXAMINER: Thank you. You