BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	Docket No. I-00040105

DIRECT TESTIMONY OF
RUSSELL R. GUTSHALL

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 1.0

Prefiled: December 10, 2008

INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

A. My name is Russell R. Gutshall. I am employed by Embarq Management Company as Senior Regulatory Affairs Manager - Regulatory and External Affairs. My business address is 240 North Third Street, Suite 201, Harrisburg, Pennsylvania, 17101.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on behalf of The United Telephone Company of Pennsylvania LLC d/b/a Embarq Pennsylvania ("Embarq PA" or "Company").

Q. BRIEFLY DESCRIBE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A. I earned an Associate Degree majoring in Business Management from the Harrisburg Area Community College, and have been employed in the telecommunications industry for forty-one years. My entire career has been at Embarq and its predecessors. I have held various positions of increasing responsibility including positions in Accounting, Finance, and Regulatory. In my current position as Senior Regulatory Affairs Manager, I have supervisory authority over various regulatory matters including, but not limited to, state regulatory policies impacting Embarq's operating entities in Pennsylvania and New Jersey, consumer complaints, and tariffs.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION AND ELSEWHERE?

A. Yes. I testified in this Commission's Formal Investigation to Examine and Establish Updated Universal Service Principles and Policies at Docket I-00940035, in October, 1997. Additionally, I have testified in a number of formal consumer complaint proceedings before this Commission and participated in several workshops. I have also testified before the New Jersey Board of Public Utilities.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN THIS PROCEEDING?

A. The purpose of my direct testimony is to respond to the issues identified in the Commission's Order entered April 24, 2008 instituting this proceeding and the Presiding Judge's June 18, 2008 scheduling order. Notably, but not exclusively, I will address the $18.00 cap on residential monthly service rates and the corresponding cap on business monthly service rates. I will also explain why an additional test – i.e., a "needs based test" – is unnecessary for determining receipts from the PA USF fund by existing USF fund recipients, including Embarq PA. Embarq PA's amended alternative regulation plan already addresses the revenue need for Embarq PA. An additional needs based test is contrary to incentive regulation. In doing so, I have formatted my testimony in accordance with the issues identified in the Commission's Orders.

IDENTIFIED ISSUES

I. ORDERING PARAGRAPHS 1(A) AND 2(E)

Q. WHAT IS THE FIRST ISSUE YOU WILL ADDRESS?

A. The first issue is very encompassing and was set forth in the April 24, 2008 Order and the Presiding Judge's June 18, 2008 scheduling order. This first issue directed the Office Administrate Law Judge to conduct appropriate proceedings to carry out the following:

> To address whether the cap of $18.00 on residential monthly service rates and any corresponding cap on business monthly service rates should be raised, whether funding "needs based" test (and applicable criteria) for rural ILEC support funding from the PaUSF in conjunction with the federal USF support payments that the rural ILECs receive should be established in order to determine which rural ILECs qualify for PaUSF funding as described in the body of the April 24, 2008 Order; (Scheduling Order, at 1.)

Q. CAN YOU PLEASE CONTINUE?

A. Yes. I would initially like to stress that the $18.00 monthly residential benchmark rate and the associated business monthly business rate are retail end user pricing caps. The Pennsylvania USF meanwhile is the mechanism and means by which this Commission historically ensured that pricing for Pennsylvania telephone consumers remain affordable. Embarq PA along with the other rural ILECs have been part of that history as recipients of PA USF funding.

Q. CAN YOU ADDRESS THE STATUS OF THE $18.00 MONTHLY RESIDENTIAL BENCHMARK AND THE ASSOCIATED BUSINESS MONTHLY SERVICE RATE FOR EMBARQ PA?

A. Yes, I can. In the Global proceeding and thereafter, Embarq PA, like the other rural ILECs, were authorized to abide by pricing caps, arising from a $16.00 monthly rate in the Global proceeding and then modified in 2003 to an $18.00 monthly residential cap. In both the Global Order and the 2003 settlement, the PA USF fund recipients, which included Embarq PA, were authorized to go to the state USF for revenues in excess of the applicable cap. In Embarq PA's 2005 price cap filing, Embarq PA finally moved to an $18.00 average basic local exchange rate for residential service and a $26.53 average basic local exchange rate for business service. In addition, for Embarq PA, the Commission's Order entered April 7, 2006 at Docket Nos. A-313200F0007 and A-311379F0002 approved a recommended decision seeking approval of a settlement in which Embarq PA, with limited exceptions, agreed not to implement any additional increase in the business and residential exchange rates contained in the Company's 2005 annual price cap filing. Furthermore, at Ordering paragraph 11 of the Order entered April 24, 2008 instituting this proceeding, the Commission stated: "That the current average benchmark caps on R-1 and corresponding business rate caps shall remain in effect pending the outcome of the ALJ hearing and final Commission determination."

Q. IS EMBARQ PA AT THIS TIME REQUESTING TO RAISE THE $18.00 MONTHLY RESIDENTIAL BENCHMARK AND THE ASSOCIATED BUSINESS MONTHLY SERVICE RATE?

A. No, not at this time. As I address below, if Embarq PA at the appropriate time seeks to pierce or increase the $18.00 monthly rate and the associated business monthly rate, then Embarq PA's amended alternative regulation plan, namely the Price Stability Mechanism ("PSM") within this plan defines the allowable revenue increase.

Q. CAN YOU ADDRESS THE ISSUE OF WHETHER THE PA USF FUND SHOULD BE MODIFIED TO INCLUDE AN ADDITIONAL "NEEDS BASED" TEST?

A. Yes, I can. The April 24, 2008 Order suggested that a "needs based" test may be appropriate to determine whether rural ILECs qualify for Pa USF funding if the $18 residential R-1 cap is pierced. Embarq PA disagrees with this approach.

An additional "needs based test" is contrary to Embarq PA's amended alternative regulation plan. Embarq PA's amended alternative regulation plan defines the process and the PSM within the Company's amended alternative regulation plan defines allowable revenues. Embarq PA's amended alternative regulation plan, therefore, defines the Company's "needs" as the Company's total revenue for noncompetitive services during the previous twelve month period, multiplied by a defined change in the Gross Domestic Product Price Index ("GDPPI"). The

Company's total non-competitive revenues are the product of actual demand multiplied by rates that have been determined by the Commission to be "just, reasonable, nondiscriminatory, and otherwise fully in compliance with All Pennsylvania laws." To the extent that year-over-year non-competitive revenue need grows, the Company can increase prices to satisfy the need for additional revenue for noncompetitive services. Thus, the revenue need is already defined and set forth in Embarq PA's amended alternative regulation plan. The implementation should be on a company-specific basis, therefore, but applied consistently among the PA USF recipients to achieve certain policy objectives, such as the important policy that rural ILECs continue to have the ability to sustain the reliability of their legacy networks and to provide broadband service to all their end-user customers by specific dates.

In addition, there is no current widespread request by rural ILECs to pierce the $18 cap for basic residential service or the equivalent benchmark for basic business service. The Commission does not need to modify the state USF to include an additional and unnecessary "needs based" test. Because Embarq PA recommends that a new "needs based" test should not be developed or implemented, I will not address the development of such a test per Ordering Paragraph 2(e) of the Commission's Order Entered April 24, 2008. I reserve the right to reply to any party's recommendations regarding the development and application of any "needs based" test and the interlinked areas identified in the Commission's ordering paragraphs, including Ordering Paragraph 2(e).

Finally, in November 2008, the Federal Communications Commission ("FCC") issued a Notice of Proposed Rulemaking ("NPRM") regarding, among other matters, the issue of broader intercarrier compensation reform. The FCC delayed action on broader intercarrier compensation reform until mid-December, at the earliest. Initial comments to the NPRM were due November 26, 2008 and reply comments were December 3, 2008 to allow for FCC action on December 18, 2008. On November 26, 2008, Embarq PA, through its parent, filed comments, along with many other carriers and interested parties. The Pennsylvania Commission also filed comments then. The FCC has granted an extension until December 22, 2008 for reply comments. Because the FCC continues to consider extensive reform of intercarrier compensation and Federal Universal Service Fund support and given the lack of any widespread effort by rural ILECs seeking to pierce the $18.00 residential cap or corresponding business monthly service rate, it is simply premature at this time to proceed.

Q. ARE BENCHMARKS AT ISSUE IN THE FCC PROCEEDING YOU REFERENCED?

A. Yes. For example, on September 19, 2008, the Independent Telephone and Telecommunications Alliance (ITTA) filed with the FCC a set of principles for intercarrier compensation reform. The ITTA describes its proposal as "reform that preserves the ability of carriers serving rural American to fulfill carrier-of-last-resort obligations and provide quality service to all their customers." Under the ITTA proposal, the relationship of a rural local exchange carrier's basic local service rate to the national benchmark would determine how much additional federal support for basic service is received by the local carrier.

Q. SHOULD THE COMMISSION IN THIS PROCEEDING CONTINUE TO REMAIN MINDFUL OF ACTION TAKEN AT THE FCC?

A. Yes. The Commission has already indicated a keen interest in FCC activities regarding intercarrier compensation reform. The Commission filed its own *Ex Parte* letter with the FCC and joined other regulators in *Ex Parte* communication with the FCC. Additionally, Chairman Cawley's letter of October 24, 2008 to the FCC expressed his concerns for any preemption of intrastate rate-making authority and the operation of intrastate universal service funds. I have attached copies of the Commission's letters to this testimony at Exhibit RRG-1. Ordering Paragraph 5 of the April 24, 2008 Order in this docket requires the Commission staff to continue to monitor the *FCC Unified Intercarrier Compensation* proceeding. And Ordering Paragraph 7 of that Order require that parties file status reports with the Commission if "at any time during this proceeding" the FCC releases an Order in the *Unified Carrier Compensation* proceeding. These actions show the Commission is very interested in any interplay between activity at the FCC and this proceeding.

Q. WHAT SHOULD THE COMMISSION DO NOW CONCERNING ANTICIPATED ACTIVITY AT THE FCC?

A. It is too early to tell with any reasonable degree of certainty what the FCC will do. At this juncture, predicting what the FCC may do would be too speculative. If greater certainty exists upon filing of rebuttal testimony on January 15, 2009 or thereafter, I will address those developments at the appropriate time.

Q. YOU PREVIOUSLY NOTED THAT THE FCC IS CONSIDERING BENCHMARK RATES AS PROPOSED BY PARTIES TO THE FCC PROCEEDING. WHY ARE PROPOSED BENCHMARK RATES AT THE FCC RELEVANT IN THIS PROCEEDING?

A. When and if the FCC decides on a benchmark rate, the benchmark may influence the policy decisions that this Commission makes regarding affordability standards and the size of the Pennsylvania USF. For example, if the national benchmark is significantly higher than Pennsylvania's current rate cap, the Pennsylvania Commission could adopt a policy that would discourage rural local exchange carriers from increasing their rates to the national benchmark. This Commission could do so by increasing the size of the state universal service fund and permit local carriers to receive additional support from the state fund rather than increase rates. In this way, all telecommunications users would help cover the costs of basic service in high cost areas, rather than just the end user customers of rural local exchange carriers.

Q. SHOULD THERE BE A "NEEDS BASED" TEST TO RE-DETERMINE IF RLECs QUALIFY FOR EXISTING PENNSYLVANIA USF FUNDS?

A. No. A need for PA USF support existed when the fund was created as a result of the Global Order and the subsequent Commission Orders and certainly exists today, especially when one considers the rural local exchange carriers' continued obligation to sustain the reliability of their legacy networks and to provide broadband service to all their end-user customers by specific dates. Also, as noted above, a "needs based" test is contrary to incentive regulation and Embarq PA's amended alternative regulation plan.

Q. IF THE COMMISSION DOES NOT IMPLEMENT A NEEDS-BASED STATE USF, WHAT SHOULD BE THE BASIS FOR COMMISSION DECISIONS IF A RURAL CARRIER REQUESTS TO INCREASE BASIC LOCAL SERVICE RATES OR RECEIVE ADDITIONAL USF SUPPORT?

A. If a rural local exchange carrier were to seek permission to increase basic local service rates or receive additional state USF support, that rural ILEC would bear the burden of justifying the request. As has historically been done, this Commission would grant or deny such a request based on ILEC-specific evidence as balanced with regulatory policy objectives.

Q. IS THERE A NEED NOW TO DETERMINE WHAT AN AFFORDABLE BENCHMARK FOR BASIC LOCAL RESIDENTIAL SERVICE RATES AND AN ASSOCIATED RATE FOR BASIC BUSINESS SERVICE?

A. No there is not. The Commission can require a rural local exchange carrier seeking to increase basic local service rates or basic business rates to demonstrate that its proposed rates are affordable for its customers in its Pennsylvania exchanges.

Q. DOES THE COMMISSION NEED TO DECIDE NOW WHETHER TO INCREASE THE SIZE OF THE PENNSYLVANIA USF?

A. Not in my view. To my knowledge, there have been limited requests for additional funding from the Pennsylvania fund. The Pennsylvania Commission ruled on the requests based on the evidence presented by the requesting companies. And as I explained earlier in my testimony, entities such as the FCC, ITTA, and Embarq PA have proposed plans to reform intercarrier compensation that could influence this Commission's decisions regarding the size of the state universal service fund.

Q. SHOULD THE COMMISSION CONSIDER REDUCING THE SIZE OF THE FUND AT THIS TIME?

A. It should not. Historically, rates for local service have been priced below costs, and access and long distance rates have been priced above costs. In turn, revenues from access and long distance have been used to help cover the costs of basic local service. In this way, rates for basic local service in rural, high-cost areas of the state have been kept affordable. In September 1999, the Pennsylvania Commission ordered the creation of the Pennsylvania USF to enable rural local exchange carriers and Embarq PA (then known as Sprint/United) to reduce their intrastate access charges and intraLATA toll rates. The Commission's order described the Pennsylvania USF as "an exchange of revenue between telephone companies which attempts to equalize the revenue deficits occasioned by mandated decreases in their toll and access charges." I have no reason to believe that the need for the support is less today than it was in 1999.

Q. CAN THIS COMMISSION EXPAND THE PENNSYLVANIA UNIVERSAL SERVICE FUND?

A. Yes.

Q. HAS THE COMMISSION DONE THAT BEFORE?

A. Yes. During the Global proceeding, the Commission included Embarq PA (Sprint LTD, at that time) in the Small Company Plan by adding $9 million to the total fund size. It appears that the Commission has the authority to change the size of the fund. Further, during the early days of the fund, the Commission approved a settlement that included the Frontier companies in the fund (M-00001337, Order entered April 18, 2000). So, it is clear that the Commission can expand and change the universal service fund.

Q. HOW WOULD THE COMMISSION DO THAT?

A. The regulations governing the universal service fund (Section 63.164) call for the Commission to issue an order which "establishes the size of the fund" as well as a budget and assessment rate for contributing telecom providers and administrative guidelines. Further, Section 63.165 provides a calculation for an individual telecom provider's monthly contribution. The monthly contribution is developed using the increase in access lines, prior year's size of fund, uncollectibles, and administrative and audit expenses. The Commission can expand the fund by including the additional amount necessary for the next year in the calculation. The Commission would have to order the administrator to include the expanded amount in the size of the fund.

II. <u>ORDERING PARAGRAPH 2(A)</u>

Q. WHAT IS THE SECOND ISSUE YOU WILL ADDRESS?

A. The Commission's April 24 Order requested that this investigation address the following issue:

> Whether the Commission has the authority under Chapter 30 and other relevant provisions of the Public Utility Code to perform a just and reasonable rate analysis of the rural ILECs' residential rates for basic local exchange services when such rates exceed the appropriate residential rate benchmark.

Q. CAN THE COMMISSION "PERFORM A JUST AND REASONABLE RATE ANALYSIS" WHEN RATES IN THE FUTURE ARE CLAIMED TO EXCEED THE APPROPRIATE RESIDENTIAL RATE BENCHMARK?

A. Yes, but only as defined by Embarq PA's amended alternative regulation plan.

Q. CAN YOU PLEASE EXPLAIN?

A. Yes, I can. Embarq PA's amended alternative regulation plan provides that the Commission shall review tariff rate change proposals to determine whether those changes are designed to produce revenues so that the Service Price Index (SPI) is no greater than the PSI. If the Commission determines that the Company's rate proposals do not comply with this criterion, then the Commission may order the Company to modify. However, Embarq PA's amended alternative regulation plan provides that if the proposal complies with this criterion, then the Commission shall approve them subject to Part 3, Section F of the Company's Plan. Meanwhile, Part 3, Section F of Embarq PA's amended alternative regulation plan provides that the annual rate change limitation set forth in Embarq PA's Plan or any other Commission-approved annul rate change limitation shall remain applicable and shall be deemed just and reasonable. Any additional just and reasonable "analysis" over and above Embarq PA's amended alternative regulation plan is not allowed.

III. ORDERING PARAGRAPHS 2(B) AND 2(C)

Q. WHAT IS THE NEXT ISSUE YOU WILL ADDRESS?

A. I will simultaneously address two issues noted in the Commission's April 24 Order. First, the Commission's April 24 Order requested that this investigation address the following issue:

> The reopened investigation should address the appropriate benchmark for the rural ILEC residential rate for basic local exchange service taking into account the statutory requirements for maintaining and enhancing universal telecommunications services at affordable rates. Participating parties should be availed of the opportunity to submit appropriate studies and testimony, including economic cost studies, that can provide the necessary information for the establishment of the appropriate residential benchmark rate for maintaining and enhancing universal telephone service goals in Pennsylvania.

Second, the Commission's April 24 Order requested that this investigation also address the following issue:

> Whether Pa. USF funding support should be received by rural ILECs that incrementally pierce the appropriate residential rate benchmark because of the regular annual Chapter 30 revenue increases, and whether the Commission's Pa. USF regulations at 52 Pa. Code § 63.161 *et seq.* should be accordingly revised. The relevant inquiry should include the role of non-expired "banked revenues" that rural ILECs may have accumulated through the operation of their respective Chapter 30 modified alternative regulation plans and corresponding price stability mechanisms.

Q. SINCE EMBARQ PA IS NOT ASKING THE BENCHMARKS TO BE INCREASED, WAS THE PRODUCTION OF A COST STUDY FOR BASIC LOCAL SERVICE IN PENNSYLVANIA NECESSARY?

A. No. To the extent the direct testimony of other parties includes cost studies or other variations on "economic cost studies," Embarq PA reserves the right to address any such studies in its rebuttal testimony, including the right to submit, as appropriate, a responsive study.

Q. HAVE YOU CONDUCTED AN ECONOMIC STUDY TO DETERMINE AN AFFORDABLE RATE FOR BASIC LOCAL EXCHANGE SERVICE?

A. No. I have not conducted an economic study regarding affordable rate levels for basic service. Embarq PA sees no need to produce such a study until Embarq PA seeks permission to raise rates above the current $18 benchmark for residential service. If Embarq PA were to seek permission to pierce the benchmark, it would be incumbent on Embarq PA to support its proposal.

Q. BEFORE WE ADDRESS THE REMAINDER OF THE COMMISSION-IDENTIFIED ISSUES, CAN YOU EXPLAIN EMBARQ PA'S ALTERNATIVE REGULATION PLAN.

A. Embarq PA's original alternative regulation plan was approved in 1999 and was subsequently amended in 2005 because of statutory amendments to Chapter 30. In accordance with Act 183, Embarq PA's amended alternative regulation plan includes a plan for broadband deployment to 100% of the Company's access lines and the various mechanisms through which pricing flexibility and regulatory relief can be achieved. A copy of the Company's current amended alternative regulation plan is attached to my testimony at Exhibit RRG-2.

Q. WHAT CHANGED IN EMBARQ PA'S AMENDED PLAN?

A. There were several changes made to the original Plan, but the major change involved accelerating the Company's broadband commitment. Embarq PA chose to advance the deadline for broadband commitment from December 31, 2015 to December 31, 2013. And Act 183 laid out an intermediate broadband milestone to be met on the way to 2013. As a result, the Company committed to accelerate broadband availability to 80% of its customers by December 31, 2010. In exchange for the accelerated deployment, the Company's productivity offset was eliminated. In the original Plan the offset was 2%.

Q. EXPLAIN THE IMPORTANCE OF THE ELIMINATION OF THE INFLATION OFFSET.

A. The elimination of the 2% offset is a quid pro quo of Act 183. In exchange for a commitment to accelerate broadband availability and obtain additional pricing flexibility and offer a Bona Fide Retail Request program, the productivity offset was eliminated for Embarq PA. Rate changes in the Company's original plan and amended plan are based on the annual change in GDP-PI as measured by the U.S. Department of Commerce, Bureau of Economic Analysis. The original plan used the change in GDP-PI less the 2% offset. The resulting percentage was the percentage of allowed revenue-producing rate changes. If GDP-PI was 3%, the offset reduction would allow the company to make rate changes of 1% on noncompetitive revenues. Using the same example, with the elimination of the 2% offset, the amended plan would permit the Company to make rate changes of

3% on noncompetitive revenues. In certain years, the calculation resulted in required rate decreases.

Q. HOW MUCH HAS EMBARQ PA BEEN ABLE TO INCREASE RATES SINCE THE OFFSET WAS ELIMINATED?

A. Very little. Since we eliminated the offset in our 2005 filing, we have had the potential to increase rates by $12,510,000. But, we've actually increased rates by only $3,933,000 and we've banked $8,577,000. These figures cover the annual filings made from 2005 through 2008. In addition, from 2006 through June 30, 2009, Embarq PA is bound by an $18.00 residential rate and a $26.53 single line business rate as part of the Commission's approval of the separation settlement.

Q. YOU MENTIONED A BROADBAND COMMITMENT. IS EMBARQ PA ON TRACK TO MEET THE INTERMEDIATE MILESTONES?

A. Yes, in fact as part of the settlement reached with parties in its separation from Sprint-Nextel, Embarq PA agreed to accelerate its broadband deployment. As I mentioned previously, the Act 183 milestone for 2010 is 80% broadband availability. The separation commitments accelerated broadband availability to 80% by December 31, 2007 and to 85% by December 31, 2010. The Company met the first milestone commitment and is on track to meet the second milestone in 2010.

Q. HOW DOES ALL OF THIS – THE COMPANY'S AMENDED PLAN, THE PRICE STABILITY MECHANISM, THE OFFSET ELIMINATION, AND ACCELERATED BROADBAND COMMITMENT – RELATE TO THE ISSUES IDENTIFIED IN THIS PROCEEDING?

A. It proves that a needs based test is not necessary. As I have shown, Embarq PA's "need" is calculated using the price stability mechanism, and the other commitments and obligations support the "need." The Company's plan is working and has worked smoothly for several years to address the Company's total non-competitive revenues need. The process based on alternative regulation plan and PUC orders coupled with existing USF regulations is working today. The alternative regulation plan identifies the "need" and, given no outcry, this proceeding seems to be in search of a problem to resolve.

Q. SHOULD RURAL ILECs BE PERMITTED TO INCREASE RATES ABOVE THE CURRENT $18 RESIDENTIAL BENCHMARK IF THE PRICE STABILITY MECHANISM IN THE APPLICABLE ALTERNATIVE REGULATION PLAN ALLOWS THEM TO DO SO?

A. Yes. As a practical matter, competition will discipline a local exchange carrier's pricing decisions. However, if competitive conditions and affordability issues permit, I see no reason for rural local exchange carriers to forego increases allowed by the price stability mechanism. After all, the mechanism was designed to permit rural local exchange carriers to recover increases in costs driven by inflation and the costs of deploying advanced services to further the public interest.

Q. SHOULD THE ANNUAL FEDERAL UNIVERSAL SERVICE FUND SUPPORT THAT A RURAL LOCAL EXCHANGE CARRIER RECEIVES INFLUENCE HOW MUCH SUPPORT THE CARRIER RECEIVES FROM THE PENNSYLVNIA UNIVERSAL SERVICE FUND?

A. No, not as the current federal system of support is structured. Federal universal service fund support was also designed to replace local service subsidies that were once implicit in interstate switched access and long distance rates. In addition to universal service fund support, the FCC created other replacement mechanisms such as subscriber line charges. Both federal and state USF support should continue to be available to keep basic local service rates affordable in high cost areas of Pennsylvania.

Q. SHOULD THE OVERALL FINANCIAL HEALTH OF A RURAL LOCAL EXCHANGE CARRIER BE TAKEN INTO ACCOUNT IN DETERMINING HOW MUCH SUPPORT IT RECEIVES FROM THE PENNSYLVANIA UNIVERSAL SERVICE FUND?

A. No. The Pennsylvania USF was created to replace revenue lost to reductions in intrastate switched access and long distance rates. The support was and is needed to help keep rates for basic local service affordable in high cost areas of the state. There is no linkage between the creation of the state universal service fund and the move away from rate-base, rate-of-return regulation. In permitting alternative regulation plans, the General Assembly provided rural local exchange carriers incentives to be more efficient and to invest in their networks to produce new and innovative services. Considering the overall financial health of a rural local exchange carrier would punish it for achieving the goals that alternative regulation was intended to further and would also be tantamount to returning to rate-base, rate-of-return regulation.

Q. SHOULD RURAL LOCAL EXCHANGE CARRIERS BE PERMITTED TO RECOVER NON-EXPIRED "BANKED REVENUES" ACCUMULATED THROUGH THE OPERATION OF CHAPTER 30 PRICE STABILITY MECHANISMS?

A. Yes they should. Rural local exchange carriers like Embarq PA have committed to deploy 100% broadband availability by dates certain. These commitments were made pursuant to statutory revisions that offered rural local exchange carriers an incentive to more rapidly deploy broadband service in exchange for increased pricing flexibility. This flexibility was to be accomplished by reducing or eliminating the inflation offset in a local exchange carrier's price stability mechanism. The theory underlying the statutory revisions was that the additional upward pricing flexibility would be used to fund the broadband deployment commitment. Embarq PA committed to 100% broadband availability by December 31, 2013. The inflation offset in Embarq PA's price stability mechanism was eliminated.

Q. ARE THERE OTHER REASONS THAT SUPPORT THE NEED FOR THE UTILIZATION OF THESE 'BANKED REVENUES'?

A. Absolutely. In addition to the broadband commitment stated above, regulated ILECs such as Embarq PA have carrier of last resort obligations that many of its competitors do not have. This obligation, especially when coupled with strong and aggressive competitive challenges by competitors such as wireless and cable companies creates a huge and unfair imbalance. As Embarq PA's number of customers decline, so does its revenues. The banked revenues are deserved and are necessary for Embarq PA to carry out its commitment to provide quality service to the customers in its service territory.

Q. HOW COULD EMBARQ PA TAKE ADVANTAGE OF THIS UNUSED PRICING FLEXIBILITY TO HELP FUND ITS REMAINING BROADBAND DEPLOYMENT COMMITMENT?

A. Because the Commission has the authority to change the size of the fund, Embarq PA could seek to recover its unexpired banked revenues as additional support from the state USF, so long as doing so did not reduce the amount of support received by other rural local exchange carriers. Embarq PA currently has no plans to do so, but it is an option we will likely ask the Commission to consider as we move toward the 2013 deadline for 100% deployment of broadband availability.

IV. ORDERING PARAGRAPH 2(D)

Q. WHAT IS THE NEXT ISSUE YOU WILL ADDRESS?

A. I will address the following issue identified in the Commission's April 24 Order:

> The reopened investigation should address whether the potential availability of Pa. USF support distributions to those rural ILECs that pierce the appropriate residential benchmark rate because of their respective annual Chapter 30 annual revenue increases has any anti-competitive or other adverse effects, especially with respect to the currently established Pa. USF support contribution mechanism and its participating telecommunications utility carriers.

Q. SHOULD A RURAL ILEC RECEIVE PENNSYLVANIA UNIVERSAL SERVICE FUND SUPPORT IF THE CARRIER'S RATE FOR BASIC SERVICE PIERCES THE APPROPRIATE RATE BENCHMARK?

A. Yes it should. Support received from the state universal service fund simply replaced revenues lost to intrastate access and long distance rate decreases. As far as I know, no one has factually demonstrated that the need for the replacement support has diminished. In fact, my costing associates tell me that, generally speaking, the cost of providing service has likely increased since the state fund was created. A rural local exchange carrier may indeed realize a need to pierce the $18 residential benchmark in order to recover inflation driven cost increases or fund the deployment of advanced services the state considers to be in the public interest. Because of inflation, piercing the $18 residential benchmark would not diminish a rural local exchange carrier's need for state universal service fund support.

Q. ARE THERE ANTI-COMPETITIVE CONCERNS ASSOCIATED WITH A RURAL LOCAL EXCHANGE CARRIERS RECEIVING PENNSYLVANIA UNIVERSAL SERVICE FUND SUPPORT AND PIERCING THE BENCHMARK RATE FOR BASIC LOCAL SERVICE?

A. I do not think so. Competitors of rural local exchange carriers do not have carrier of last resort obligations, do not need to maintain the reliability of their legacy networks and are not required to provide broadband service to all their customers by specific dates. Rural local exchange carriers require sufficient pricing flexibility and universal service fund support to meet their obligations as carriers of last resort to and fund broadband deployment.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes it does.

COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

Exhibit R IN REPLY PLEASE REFER TO OUR FILE

October 27, 2008

EX PARTE

Ms. Marlene Dortch
Office of the Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re:	In the Matter of	)	
		)	
	Developing a Unified Intercarrier Compensation Regime	))	CC Docket No. 01-92
	In the Matter of Universal Service Contribution Methodology	))	WC Docket No. 06-122
	High Cost Universal Service Support	)	WC Docket No. 05-337
	Federal-State Joint Board On Universal Service	))	CC Docket No. 96-45

Dear Ms. Dortch:

Pursuant to Commission rules, please include the attached Ex Parte Comments of the Pennsylvania Public Utility Commission in the corresponding Docket numbers of the above-referenced proceedings.

Sincerely Yours,

Joseph K. Witmer

Joseph K. Witmer, Esq., Assistant Counsel
Pennsylvania Public Utility Commission

Enclosure
cc: Best Copy & Printing (via E-Mail)
FCC Chairman and Commissioners

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
Developing a Unified Intercarrier Compensation Regime	))	CC Docket No. 01-92
In the Matter of Universal Service Contribution Methodology	))	WC Docket No. 06-122
In the Matter of High Cost Universal Service Support	))	WC Docket No. 05-337
In the Matter of Federal-State Joint Board On Universal Service	))	CC Docket No. 96-45

EX PARTE COMMENTS OF
THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

The Pennsylvania Public Utility Commission (PaPUC), in addition to supporting the Ex Parte Comments the Five State Commissions ("Five State Commissions"),[1] is filing these supplemental Ex Parte Comments. The PaPUC already filed Comments and Reply Comments on intercarrier compensation reform, including the pending petitions in the Petition of AT&T in CC Docket No. 08-152 and the Petition of Embarq in CC Docket No. 08-160.

[1] The Delaware Public Service Commission, the Public Service Commission of the District of Columbia, the New Jersey Board of Public Utilities, the New York Public Service Commission, and the Pennsylvania Public Utility Commission.

These Ex Parte Comments repeat the concerns set out in those filings. Repetition is necessary given the recent concern that any pending decision may rely largely on Ex Parte reform proposals submitted *since* the closing of the public record in these cases.

The first concern is the FCC's legal authority to preempt state authority over intrastate rates either *de jure* or *de facto*. The Ex Parte filings of the New England Council of Utility Commissioners (NECPUC)[2] and the National Association of Regulatory Utility Commissioners (NARUC)[3] identify many legal infirmities. The PaPUC has set out similarly extensive legal considerations as well.[4]

The PaPUC repeats its observation that reform proposals which ostensibly claim they do not preempt the states begs the question of what happens if a state commission refuses to implement a federal mandate over a decision involving intrastate rates.[5] The PaPUC also repeats its earlier concern that federal benchmark rates for local service

[2] Ex Parte Letter of the New England Conference of Public Utilities Commissioners to Marlene H. Dortch, Secretary, Federal Communications Commission, *In Re: Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, (October 17, 2008).

[3] *In Re: Intercarrier Compensation*, CC Docket No. 01-92, *In the Matter of Petition of AT&T Inc. for Interim Declaratory Ruling and Limited Waivers Regarding Access Charges and the ESP Exemption*, CC Docket No. 08-152, In the Matter of IP-Enabled Services, WC Docket No. 04-36, *In the Matter of Universal Service Contribution Methodology*, WC Docket No. 06-122, *In the Matter of Petition for Declaratory Ruling Filed by CTIA*, WT Docket No. 05-194, *In the Matter of Jurisdictional Separations & Referral to the Federal-State Joint Board*, CC Docket No. 80-286, National Association of Regulatory Utility Commissioners (NARUC) Motion/Request for Public Comment on Recently Circulated "Report and Order," Order on Remand, and Further Notice of Proposed Rulemaking" on Universal Service and Intercarrier Compensation Reform, (October 21, 2008) (*NARUC Motion*).

[4] *Petition of AT&T for Interim Declaratory Ruling and Limited Waivers*, CC Docket No. 08-152, Comments of the PaPUC, p. 13 (*AT&T Petition*); *In Re: Intercarrier Compensation*, CC Docket No. 01-92, Reply Comments of the PaPUC (February 1, 2007), pp. 3-21.

[5] *AT&T Petition*, PaPUC Comments, p. 1 (*AT&T Petition*).

which exceed a state's benchmark, in Pennsylvania's case $18.00, could undermine universal service through local rate increases.[6] The PaPUC further reminds the FCC that prior federal reforms imposed rate increases with SLCs in Pennsylvania which produced penetration rate declines in Pennsylvania and the MACRUC Region during 2001-2008.[7]

The PaPUC particularly reminds the FCC that the current proposals do not address what happens in states with price cap regimes, including Pennsylvania, if those states have "exogenous events" or "change of law" provisions in their law.[8] There is a distinct possibility that states will be forced to increase rates to fund a "dollar for dollar" recovery of *all lost intrastate revenues arising from a federally mandated reform of intrastate rates*. This would be particularly egregious in states where the increases support access rate reductions and broadband deployment programs in other regions that have done little, if any, reform of their access rates and local rates to implement either rate reform or broadband deployment programs. To date, Pennsylvania's efforts alone have cost in excess of $1 Billion dollars.[9]

The PaPUC is concerned about the revenue impact from reform if those reforms reduce revenues available to competitive carriers in Pennsylvania. The PaPUC is equally

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[6] *AT&T Petition*, PaPUC Comments, p. 5.
[7] *AT&T Petition*, PaPUC Comments, p. 5, 12, 19-20.
[8] *AT&T Petition*, PaPUC Comments, p. 5 and 13; *Petition of Embarq Communications*, CC Docket No. 08-160, p. 8 (Embarq Comments).
[9] Embarq Comments, p. 7; *In re: Intercarrier Compensation Reform*, Docket No. 01-92, Comments of the Pennsylvania Public Utility Commission (October 25, 2006), pp. 3-4.

concerned if those same reforms reduce revenues to incumbent carriers that have undertaken extensive broadband deployment programs under state law. Pennsylvania has competitive carriers. Pennsylvania also has state laws that implemented rate reforms and local rate increases in order to fund broadband deployment. Carriers should not lose the intrastate revenues they need to compete nor should carriers lose the revenues they relied on to comply with state-law mandates on broadband deployment.

The PaPUC has very real problems with any interim or final decision or result that takes revenues away from carriers in states with broadband deployment commitments in order to further federal efforts at broadband deployment or reform in other regions where similar efforts are not in place. This concern is aggravated in situations where the same carriers with broadband deployment programs face intermodal constraints from competitive carriers. Reform should not prevent competitive carriers' from continuing to operate. Reform should not deprive incumbent carriers of the intrastate revenue stream they relied upon to finance their major long-term capital programs, specifically broadband deployment. Given the conditions in the current capital and credit markets, the FCC is ill-advised to rush headlong into decisions that harm competition or undermine an incumbent carrier's access to the capital needed to fund broadband deployment, particularly rural carriers.

These impacts and issues cannot be comprehensively considered in brief Ex Parte Comments let alone a federal interim or final order which justifies rates using selective references to incomplete or outdated Ex Parte filings. For that reason, the PaPUC implores the FCC to tailor any pending decision to the narrow requirements of the pending Core Remand decision.[10] The issues set out in the latest plethora of Ex Parte reform proposals should be set out for public comment. Those issues have been pending for several years. There is no need to make hasty decisions in the current environment.

For these reasons, the PaPUC supports the alternative proposed in the October 21, 2008 filing of the National Association of Regulatory Utility Commissioners' filing.[11]

/s/ James W. Cawley,
Chairman

/s/ Tyrone J. Christy,
Vice Chairman

/s/ Robert F. Powelson,
Commissioner

/s/ Kim Pizzingrilli,
Commissioner

/s/ Wayne E. Gardner,
Commissioner

Dated: October 27, 2008

[10] *In re: Core Communications, Inc.* 531 F.3d 849 (D.C. Cir. 2008).
[11] NARUC Motion/Request, (October 21, 2008), p. 1.

COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

Exhibit RRC-1

IN REPLY PLEASE REFER TO OUR FILE

October 24, 2008

EX PARTE

Ms. Marlene Dortch
Office of the Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re:	In the Matter of	)	
		)	
	Developing a Unified Intercarrier	)	CC Docket No. 01-92
	Compensation Regime	)	
	In the Matter of Universal Service	)	
	Contribution Methodology	)	WC Docket No. 06-122
	High Cost Universal Service Support	)	WC Docket No. 05-337
	Federal-State Joint Board	)	CC Docket No. 96-45
	On Universal Service	)	

Dear Ms. Dortch:

Pursuant to Commission rules, please include the attached Ex Parte Letter of James H. Cawley, Chairman of the Pennsylvania Public Utility Commission, in the corresponding Docket numbers of the above-referenced proceedings.

Sincerely Yours,

Joseph K. Witmer

Joseph K. Witmer, Esq., Assistant Counsel
Pennsylvania Public Utility Commission

Enclosure
cc: Best Copy & Printing (via E-Mail)

Exhibit RRG-1

PENNSYLVANIA PUBLIC UTILITY COMMISSION
COMMONWEALTH OF PENNSYLVANIA
HARRISBURG, PENNSYLVANIA

JAMES H. CAWLEY
CHAIRMAN

October 24, 2008

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

RE: Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92; Universal Service Contribution Methodology, WC Docket No. 06-122; In the Matter of High Cost Universal Service Support Methodology, WC Docket No. 05-337; In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45.

EX PARTE SUBMISSION

VIA ELECTRONIC FILING

Dear Secretary Dortch:

I feel compelled to communicate to you a number of serious concerns that involve contemplated Federal Communications Commission actions on various subjects relating to intercarrier compensation reform that potentially will take place on or about November 4, 2008. According to various press reports and a flurry of *ex parte* filings, these FCC actions have the potential to greatly hinder the ability of the states to regulate and oversee intrastate carrier access rates and intrastate retail rates, as well as the operation of intrastate universal service funds (USFs), and broadband deployment. The FCC should separately address the mandate from the U.S. Court of Appeals for the District of Columbia Circuit in the *Core* case, and issue a new comprehensive proposed rulemaking on the wider range of intercarrier compensation reform.[1]

As Chairman of the Pennsylvania Public Utility Commission, I am gravely concerned about the potential FCC *de jure* or *de facto* federal preemption of intrastate rate making authority that involves carrier access charges. As the Pa. PUC has repeatedly and formally commented to the FCC, such federal preemption is legally impermissible, and it is certain to cause harmful rate effects in Pennsylvania. We have undertaken considerable intrastate carrier access charge reforms in Pennsylvania with parallel increases in basic local exchange rates for both major and rural incumbent local exchange carriers (ILECs). During the 1997-2005 time frame the Pa. PUC

[1] *In re Core Communications, Inc.*, No. 07-1446 (D.C. Cir. July 8, 2008)

cumulatively reduced intrastate carrier access rates by approximately $795.39 million.[2] We have also instituted a Pennsylvania-specific USF that has been in operation since 2001-2002. The local exchange rates for certain of the rural ILECs operating in Pennsylvania are at or approaching a state-specific benchmark of $18 per month (this figure *is exclusive of* applicable federal subscriber line charges or SLCs, 911 fees, telecommunications relay service or TRS fees, etc.). In Pennsylvania the total intrastate access rate reforms and Pa. USF outlays amount to no less than one billion dollars during the 1997-2005 time period alone.[3] Pennsylvania is also a *net contributor* state to the federal USF. Pennsylvania's annual net contribution to the federal USF exceeds $130 million.[4] Most of the major and rural ILECs in Pennsylvania operate under a price cap regime of regulation and have undertaken broadband deployment commitments that are mandated by state law. *See generally* 66 Pa. C.S. § 3011 *et seq.*

The exercise of the Pa. PUC's jurisdiction over regulated telecommunications utilities is based both on Pennsylvania *and* federal law. Legally impermissible *de jure* or *de facto* federal preemption of the Pa. PUC's ability to manage further intrastate carrier access charge reforms within Pennsylvania will lead to undesirable results for the end-user consumers of regulated telecommunications services. The Pa. PUC is obliged by Pennsylvania statute to make further intrastate carrier access charge reductions only on a "revenue-neutral basis." 66 Pa. C.S. § 3017(a). Federal preemption of intrastate carrier access rate making authority will create regulatory uncertainty, may have almost automatic and negative impacts for basic local exchange service rates, and – on top of the contemplated substantial increases in the federal SLCs – can have adverse effects on the availability of universal telephone service, especially for end-user consumers in the lower income brackets.

This situation will be further aggravated if the FCC were to proceed with preemption *and* the imposition of intrastate *interim* carrier access rates. Since this action will have *interlinked* effects with local exchange rates in Pennsylvania, the Pa. PUC will be left with the unfunded federal mandate to literally unscramble a complex regulatory "omelet" if and when such interim rates may be modified, e.g., after a successful court appeal. Further and significant regulatory uncertainty will ensue since there will not be a clear premise on whether Pennsylvania or federal law will govern the imposition of these interim rates and their subsequent modification.

These matters should not be deliberated and decided by the FCC on the basis of streaming *ex parte* submissions. I am aware of the mandate from the United States Court of Appeals for the District of Columbia Circuit in the *Core* case that obliges the FCC to act by November 5, 2008 on issues relating to intercarrier compensation for information service provider traffic. The FCC can act in response to the Court's mandate while proceeding to resolve the broader range of issues on intercarrier compensation in a more deliberate and transparent fashion through a new notice of proposed rulemaking. This will provide adequate

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[2] *In re Developing a Unified Intercarrier Compensation Regime*, Docket No. CC 01-02, *Missoula Intercarrier Compensation Reform Plan*, FCC DA 06-150, The Comments of the Pennsylvania Public Utility Commission, Exhibit 2.
[3] *Id.*, Comments at 4.
[4] *In re High-Cost Universal Service Support*, Docket No. WC 05-337, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, The Comments of the Pennsylvania Public Utility Commission.

opportunity for all interested parties to provide well reasoned and documented comments. I stand ready to answer any questions that you may have in this matter.

Sincerely,

James H Cawley

James H. Cawley

cc: Chairman Kevin J. Martin, FCC, via electronic mail
Commissioner Michael J. Copps, FCC, via electronic mail
Commissioner Jonathan S. Adelstein, FCC, via electronic mail
Commissioner Deborah Taylor Tate, FCC, via electronic mail
Commissioner Robert M. McDowell, FCC, via electronic mail

Exhibit RBG-2

NON-REDLINED FINAL
AS FILED MARCH 15, 2005
AND FURTHER REVISED JUNE 9, 2005

IN THE COMMONWEALTH OF PENNSYLVANIA
BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PETITION OF THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA FOR APPROVAL UNDER CHAPTER 30 AND ACT 183 OF THE PUBLIC UTILITY CODE OF AN ALTERNATIVE REGULATION AND NETWORK MODERNIZATION PLAN	:	Docket No. P-00981410

<u>AMENDED</u>
ALTERNATIVE REGULATION PLAN
OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA, DOING BUSINESS AS "SPRINT"

Revised March 15, 2005
And Further Revised June 9, 2005

Dated: Amended March 15, 2005 (Revised Per Commission Order Entered July 16, 1999; Amended Pursuant to Act 183 of 2004, as filed on March 15, 2005 and Further Revised June 9, 2005.)

TABLE OF CONTENTS

EXECUTIVE SUMMARY

This Amended Alternative Regulation Plan ("Plan") introduces a state-of-the-art telecommunications network in the service territory of The United Telephone Company of Pennsylvania d/b/a Sprint ("Sprint" or "the Company") and also provides a new regulatory framework for the Company.[1] It is designed to replace entirely rate base/rate of return regulation and procedures. Sprint will operate under a regulatory framework that will allow the Company to meet its customers' telecommunications needs in a more efficient way, while continuing to provide adequate consumer and competitive safeguards.

The Plan has five principal components: (1) a Network Modernization Plan ("NMP"); (2) a Competitive Services Deregulation Plan ("CSP"); (3) a Price Stability Plan ("PSP") for noncompetitive services; (4) commitments regarding quality, safety, adequacy and reliability of service; and (5) commitments arising as a result of Act 183. [2] These five parts of the Plan are interrelated and dependent upon one another.

Part 1 of the Plan is the Network Modernization Plan, which describes the Company's commitment to provide accelerated broadband availability to at least 80% of its total retail access lines in its distribution network by December 31, 2010 and 100% of its total retail access lines in its distribution network by December 31, 2013.

Part 2 of the Plan is the Competitive Services Deregulation Plan, which allows for the deregulation of the rates and earnings of competitive services, but preserves Commission authority over the quality of these services consistent with Act 183. In addition, the CSP

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[1] Sprint is a "Rural Telecommunications Carrier" as defined in Section 3 of the Telecommunications Act of 1996 (Public Law 104-104, 110 Stat.56) and for the purposes of Act 183, 66 Pa.C.S. §3011 *et seq*.

[2] In addition, Sprint's Plan includes several illustrative attachments, none of which have been modified due to Act 183.

contains safeguards to protect competitors from potential abuses and to mitigate the economic risk of competitive services upon basic ratepayers.

Part 3 of the Plan is the Price Stability Plan, which governs revenue changes for noncompetitive services for the duration of the Plan, as amended to be consistent with Act 183. The PSP also constrains noncompetitive service revenue changes, based on an independent inflation index and Commission review, and provides for interim rate adjustments, as amended to be consistent with Act 183.

Part 4 of the Plan describes Sprint's ongoing obligations and commitments regarding quality, safety, adequacy and reliability of telecommunications services and other business activities. It also describes the reports that the Company will continue to file with the Commission, as amended to be consistent with Act 183.

Finally, Part 5 of the Plan was added as a result of Act 183. Part 5 sets forth the various additional commitments Sprint will undertake pursuant to Act 183 and Sprint's election pursuant to Act 183 options for continuation of Sprint's Commission-approved alternative regulation and network modernization plan, including the implementation of a Bona Fide Retail Request Program (BFRR) and a Business Attraction or Retention Program (BARP).

A. Introduction

Sprint's Amended Network Modernization Plan ("NMP") establishes the Company's commitment to modernize its network infrastructure leading to 100% broadband availability by December 31, 2013. Under Act 183 of 2004, Sprint has elected in its NMP, to commit to accelerate 80% broadband availability by December 31, 2010 and 100% broadband availability by December 31, 2013. Among other commitments, Sprint shall be required to offer a Bona Fide Retail Request Program and a Business Attraction or Retention Program within the guidelines of Act 183.

Included in the NMP are details of the network facilities that the Company already has deployed or plans to deploy, descriptions of service capabilities, and examples of the services each network facility will support. The NMP portrays how the existing network infrastructure will evolve to support broadband availability.[3] The Company's network strategy for broadband implementation includes the continued deployment of technologies that will upgrade the existing switching, signaling, interoffice and exchange distribution network to support future, increased bandwidth requirements.

Sprint's NMP relies on digital switching, fiber optics and ADSL/DS1 technology; however, the Company projects that the existing copper distribution network, with the appropriate overlay electronics, will be able to support broadband availability to 100% of small business and residential customers by the year 2013. Sprint cannot predict future technological evolution with any degree of certainty. The NMP, therefore, does not commit the Company to deploying any specific technology for broadband implementation and broadband availability.

[3] For purposes of this Plan and NMP, "Broadband Availability" is defined as access to broadband service by a retail telephone customer of The United Telephone Company of Pennsylvania d/b/a Sprint. Moreover, "Broadband" is defined as a communication channel using any technology and having a bandwidth equal to or greater than 1.544 megabits per second (Mbps) in the downstream direction and equal to or greater than 128 kilobits per second (Kbps) in the upstream direction.

As future technologies are developed, the Company will modify its infrastructure plans accordingly. Such changes in deployment strategy will be included in periodic updates to the NMP that will be filed with the Commission. Sprint's commitment to Act 183, however, will not change, so long as Act 183 remains in effect.

This NMP outlines Sprint's commitment for broadband availability. It represents the Company's plan to conform to the intent of Act 183 for broadband availability to customers on a demand basis, predicated on standard service arrangements and terms as set forth in the Company's tariffs. As the existing network evolves to support broadband capabilities, customers will benefit from network capabilities as they are made available throughout the time period of the NMP, including services based on the digital network already in place.

The General Assembly in Act 183 found and declared that it was the policy of the Commonwealth to strike a balance between mandated deployment and market driven deployment of broadband facilities and advanced services and to continue alternative regulation. Act 183 requires that a Local Exchange Telecommunications Carrier "shall reasonably balance deployment of its broadband network between rural, urban and suburban areas within its service territory, as those areas are applicable..." 66 Pa.C.S. §3014(k). Sprint has classified each of its exchanges as rural.[4] See Attachment C.

The Company commits to biennial updates to the NMP in compliance with approved PUC filing requirements, with the first report due March 15, 2007 for the Plan Years 2005 and 2006. Absent exceptional circumstances[5], the Company will commit to meeting its deployment schedule.

Forecasting construction costs is difficult to determine in view of potential changes in technology, the economy and the financial condition of the Company. Thus, while the

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[4] See footnote 1, herein.

[5] Such exceptional circumstances shall be set forth in a petition to the Commission, with all Chapter 30 parties in this proceeding being given notice and the opportunity to respond, and shall be subject to Commission approval.

Company recognizes there will be significant capital required to meet the demands of the NMP, it emphasizes its right to make or change decisions regarding how to fund deployment or as to what technology or services should be used or offered to meet the broadband standard at any given point in time during the life of the NMP. Sprint will make broadband available, within 10 business days of a request, for 80% of its retail customers by December 31, 2010 and for 100% of its retail customers by December 31, 2013.

B. Digital Switching

The Company's first digital central office switch was deployed in 1978. The Company's analog switch replacement program continued over the years, culminating in 100% digital central office status in 1996. The Company will continue to modernize its central office plant, as evidenced by the fact that some first generation digital switches already have been replaced with newer technology. Other vintage digital network facilities will be identified for future replacement so that customers will continue to enjoy state-of-the-art digital services throughout the period of the NMP.

C. Integrated Services Digital Network ("ISDN")

1. Basic Rate ISDN ("BRI")

BRI service provides the capability for simultaneous transmission of voice and data over a single subscriber line. Each BRI line has two 64 kbps bearer ("B") channels and one 16 kbps data ("D") channel. A typical operation would provide for the simultaneous transmission of two voice calls and one data connection. Other options are possible, however. In addition to plain old telephone service ("POTS") calls, BRI can be used for services such as internet access, computer to computer dial-up data telecommunications and facsimile transmission. Basic Rate ISDN service is available for all of Sprint's retail customers in Pennsylvania.

2. Primary Rate ISDN ("PRI")

PRI provides the capability of dial-up voice and data calls on the public switched telephone network. Typically, a PRI line operates at 1.544 Mbps. The line is divided into twenty-four 64 kbps DS-0 channels and is arranged with 23 bearer ("B") channels and one data ("D") channel. There can be various combinations of voice and/or data calls on a PRI line at any given time. These combinations can be reconfigured dynamically by the customer, as needed. A PRI line requires a T-1 (DS-1 equivalent) carrier facility between the customer's location and the Company's PRI serving office. In addition to voice calls, PRI can be used for internet access, video conferencing, facsimile, computer to computer dial-up data communications and mainframe to mainframe computer applications. Primary Rate ISDN service is available to 100% of Sprint's retail customers in Pennsylvania.

3. Asynchronous Transfer Mode ("ATM")

The explosion in demand for new high bandwidth services, such as internet access, company intranets, telecommuting and remote local area network ("LAN") access, is a driving factor in the development of new transmission technology. One of these technologies is Asynchronous Transfer Mode ("ATM"). ATM is a networking technology developed by American National Standards Institute ("ANSI") and Consultative Committee for International Telephone and Telegraph ("CCITT") for a high speed, fixed cell-based network. The ATM network is capable of transporting different types of services--voice, data and video applications--multiplexed over the same bandwidth. With transmission speeds reaching from 1.5 Mbps to the Gigabit per second ("Gbps") range, ATM has the potential to become the universal transmission medium for many future applications. The Company has ATM switching nodes deployed within the existing network.

D. Signaling and Intelligent Network

1. Signaling System 7 ("SS7")

Another important element for migrating the Company's network to broadband capability is SS7. SS7 is a signaling system that overlays the traditional interoffice voice switching network and is an intelligent transport and switching platform that enables internodal features and services to work. The SS7 network requires hardware and software in digital host switches. The SS7 protocol is a 56 kbps packet data network that moves SS7 call management messages from one node to another. The main elements in the SS7 network are Service Switching Points ("SSP"), Signal Transfer Points ("STP") and Service Control Points ("SCP").

The Company's SS7 equipped central offices provide network features and services, such as interoffice trunk setup and teardown capabilities. The SS7 network also provides enhanced subscriber features and services such as Custom Local Area Signaling Services ("CLASS"). All of Sprint's central offices in Pennsylvania have access to and utilize SS7 signaling.

2. Intelligent Network ("IN")

The Intelligent Network uses the SS7 network as a platform to provide network functions in the traditional voice environment. IN is based on SS7 queries and data elements within SS7 messages. Enhanced 800 ("E800") and Line Information Database ("LIDB") services use SS7 to query data bases, (i.e., E800 service queries a database to determine the appropriate interexchange carrier ("IXC") for call routing, and LIDB queries a database to guarantee that billing information is legitimate). The IN also is used to complete data dips for CLASS services. The Company has E800 and LIDB service fully deployed in its network.

The Advanced Intelligent Network ("AIN") is an evolution of the Intelligent Network. Like the IN, AIN uses the capabilities of the SS7 network as a platform to provide network functions. AIN is based on switch trigger software that, when encountered, causes SS7 query messages to be sent to other nodes in the SS7 network. The Company has equipped AIN switch triggers to 100% of its central offices in Pennsylvania.

E. Interoffice Trunking

Another important part of the Company's universal broadband availability strategy is the deployment of fiber optic facilities in the interexchange ("IX") network. The Company has aggressively deployed fiber to 100% of its central offices in Pennsylvania. .

F. Public Schools, Administrative Offices, Industrial Parks and Healthcare Facilities

The Company has broadband available to all public schools, administrative offices supporting public schools, industrial parks and healthcare facilities[6] in its Pennsylvania service area.

G. Biennial Updates

The Company will provide biennial NMP reports on its provision of broadband availability as required by Act 183 and, absent exceptional circumstances, as set forth in footnote 5 above, will meet or exceed its 2010 and 2013 commitment schedules as addressed herein in Part 1, Section A. Biennial reports will be provided on March 15, 2007, March 15, 2009, March 15, 2011, March 15, 2013 and March 15, 2014 for the preceding year-end reporting period.

Such biennial reports shall be submitted in the form and detail required by the Commission as of July 1, 2004,[7] unless such reporting requirements are subsequently reduced

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[6] As used in this Plan, the term "Health Care Facility" shall have the same meaning given to it in the Act of July 19, 1979 (P.L.130, No.48) known as the Health Care Facilities Act.

[7] The reporting requirements are those specified in the "Reporting Guidelines" attached to the Commission's Order entered May 17, 1999 in *Re: Implementation of Chapter 30 of the Public Utility Code, Reporting*

by the Commission. The Commission may require the submission of further information to support the accuracy of or to seek an explanation of the biennial NMP reports filed by Sprint.

H. Failure to Provide Universal Broadband Availability

Utilizing the biennial NMP reports filed with the Commission by Sprint under Part I, Section G of this Plan, the Commission shall monitor and enforce Sprint's compliance with the interim (80%) and final (100%) commitments for broadband availability set forth in this Plan. In the event that Sprint is found by the Commission, after notice and evidentiary hearings held on an expedited basis, to have failed to meet such an interim or final commitment, then the Commission shall require Sprint to refund to customers in its next price stability filing an amount that is just and reasonable under the circumstances. Such amount shall not exceed an amount determined by multiplying the percentage shortfall of the broadband availability commitment on an access line basis required to be met during the period from the start of the amended plan or from the date of the last prior interim commitment, as applicable, times the increased revenue that was obtained by Sprint during this period as a result of eliminating the 2% productivity offset that was in effect prior to the amendment of this Plan under Act 183, plus interest calculated under 66 Pa.C.S §1308 (d)(relating to voluntary changes in rates). Any such refund shall be separate from and in addition to any civil or other penalties that the Commission may impose on a local exchange telecommunications company under Chapter 33 of the Public Utility Code (66 Pa.C.S §3301, et seq).

I. Construction

1. Sprint shall not be required to provide specific services or to deploy a specific technology to retail customers seeking broadband or advanced services.

2. Sprint shall be permitted to participate, should they choose to do so, in joint ventures with other entities in meeting advanced services and broadband deployment commitments under this Plan and NMP.

3. Under no circumstances shall Sprint be compelled to publicly release maps or other information describing the actual location of Sprint's facilities.

The Company's Competitive Services Deregulation Plan ("CSP") allows for the price and earnings deregulation of any services or locations that have been. or may be, found by the Commission to be competitive or declared by the Company to be competitive in accordance with Act 183. The Company may submit future requests to classify services as competitive in accordance with Act 183.

A. Competitive Services

1. The following services are currently competitive and shall continue to be classified as competitive under Chapter 30: Customer premises equipment, inside wire, billing and collection and voicemail. The following services were determined competitive pursuant to Chapter 30: Directory Assistance, Directory Assistance Call Completion and National Directory Assistance and IntraLATA Toll services. The following services were declared competitive by Sprint on February 23, 2005 pursuant to Act 183: directory listings, feature packages, and basic local service bundled with other services.

2. Services not deemed to be competitive under this Plan are classified as "noncompetitive" for purposes of the Price Stability Plan ("PSP").

3. The Commission may not fix or prescribe the rates, tolls. charges, rate structures, rate base, rate of return or earnings of competitive services or otherwise regulate competitive services except as set forth in Act 183.

4. Sprint may petition the Commission for a determination of whether a protected or retail noncompetitive service or other business activity in its service territory or a particular geographic area, exchange or group of exchanges, or density cell within its service territory is competitive based on the demonstrated availability of like or substitute services or other business activities provided or offered by alternative service providers. The Commission, after notice and hearing, shall enter an order granting or denying the petition within 60 days of the

filing date, or within 150 days of the filing date where a protest is timely filed, or the petition shall be deemed granted. Sprint shall serve a copy of its petition on the Office of Consumer Advocate, the Office of Small Business Advocate and each of the parties to the Commission's proceeding in which Sprint's Network Modernization Plan that was in effect on December 31, 2003 was approved by the Commission.

In making its determination, the Commission shall consider all relevant information submitted to it, including the availability of like or substitute services or other business activities, and shall limit its determination to the service territory or the particular geographic area, exchange or group of exchanges or density cell in which the service or other business activity has been proved to be competitive. The burden of proving that a protected or retail noncompetitive service or other business activity is competitive rests on the Company.

5. Notwithstanding the provisions of Part 2, Section A, paragraph 5 of this Plan, Sprint may declare any retail nonprotected service as competitive by filing a declaration with the Commission and serving it on the Office of Consumer Advocate, Office of Small Business Advocate and each of the parties to the Commission's proceeding in which Sprint's Network Modernization Plan that was in effect on December 31, 2003 was approved by the Commission, provided that Sprint may not use this declaration process for any service that the Commission previously has reclassified as noncompetitive under either Part 2, Section A, paragraph 6 of this Plan or prior law. A declaration of a retail nonprotected service as competitive shall be effective upon filing by Sprint with the Commission.

6. A party may petition the Commission for a determination of whether a service or other business activity previously determined or declared to be competitive is noncompetitive. The Commission, after notice and hearing, shall enter an order deciding the petition within 60 days of the filing date or 90 days of the filing date where a protest is timely filed, or the petition shall be approved. The petitioner shall serve a copy of the petition on

Sprint, the Office of Consumer Advocate, the Office of Small Business Advocate, and each of the parties to the Commission's proceeding in which Sprint's Network Modernization Plan that was in effect on December 31, 2003 was approved by the Commission. In making its determination, the Commission shall consider all relevant information submitted to it, including the availability of like or substitute services or other business activities, and shall limit its determination to the particular geographic area, exchange or density cell in which the service or other business activity has been proved to be noncompetitive. The burden of proving that a competitive service or other business activity should be reclassified as noncompetitive rests on the party seeking the reclassification. If the Commission reclassifies a service or other business activity as noncompetitive, the Commission shall determine a just and reasonable rate for the reclassified service or business activity in accordance with 66 Pa.C.S. §1301 (relating to rates to be just and reasonable).

B. Statutory Protections

1. Sprint shall not use revenues earned or expenses incurred in conjunction with noncompetitive services to subsidize competitive services.

2. By operation of the PSP, the revenues earned and expenses incurred for any noncompetitive service will not cross-subsidize or support any competitive service; therefore, this Plan is in compliance with the requirements of 66 Pa.C.S. §3016(d). This provision shall not be construed to prevent the marketing and billing of packages containing both noncompetitive and competitive services to customers.

3. The price that the Company charges for competitive services shall not be less than the costs to provide the services. Subject to the foregoing limitation, the Company may price competitive services at the Company's discretion. There is no cross-subsidy between services when the price charged for that service covers its incremental cost. Incremental cost

shall be defined as forward-looking costs directly attributable to the specified service. The price for each of the Company's services deemed to be competitive shall cover its incremental cost. Such cost documentation will be provided only under appropriate proprietary protection.

4. Sprint will perform its own cost studies in order to comply with competitive costing and pricing safeguards addressed herein, and will share those studies with intervenors, if challenged, under appropriate proprietary agreements.

5. Tariffs may not be required to be filed by the Company for ~~future~~ competitive services At its option, the Company may tariff its rates, subject to the rules and regulations applicable to the provision of competitive services. The Commission may require the Company to maintain prices lists with the Commission applicable to competitive services. Price changes that are filed in the Company's tariff for competitive services will go into effect on a one-day notice.

6. Formal challenges to the Company's compliance with the provisions of the CSP can be made only through separate complaint procedures. Any competitor or other party who believes the Company has violated any of the provisions of this CSP may file a complaint with the Commission. That party, however, bears the burden of proof under 66 Pa.C.S. §332(a). The Commission retains the right to institute proceedings on its own motion, and the Company shall have the burden of proof in those proceedings.

PART 3 - PRICE STABILITY PLAN FOR NONCOMPETITIVE SERVICES

The Company's Price Stability Plan ("PSP") sets forth the principles and procedures applicable to changes in the Company's rates.

The PSP will calculate the allowable change (increase or decrease) in rates for noncompetitive services, equal to the annual change in the Gross Domestic Product Price Index ("GDP-PI"), as calculated by the United States Department of Commerce and adjusted for any exogenous events. The PSI changes based upon this formula then are tracked cumulatively after 2001.

The PSP also addresses revenue neutral rate rebalancing/restructuring, the introduction of new services and the banking of price changes.

The PSP in the Plan is a complete replacement of rate base/rate of return regulation for the Company and is the exclusive basis upon which the Company's rates and services will be regulated, upon implementation of this Plan. All tariff filings for noncompetitive services are subject to review under the terms of this Plan. Noncompetitive services are defined as regulated services or business activities that have not been determined or declared to be competitive.

A. Modified Price Stability Mechanism ("PSM")

1. The Price Stability Index ("PSI") is based upon the Company's rates in effect on October 16, 1998, as a starting point. Those rates are just, reasonable, nondiscriminatory and otherwise fully in compliance with all Pennsylvania laws.

2. Annually the Company will calculate the PSI as follows:

$$PSI_t = PSI_{t-1} \times [1 + \%\Delta\ GDP\text{-}PI_{t-1} - 0.0\% \pm Z]$$

When:

PSI_t	=	The new maximum change in price for the noncompetitive service category for the current twelve month period.
PSI_{t-1}	=	The current maximum change in price for the noncompetitive service category for the previous twelve month period.[8]
$\%\Delta\ GDP\text{-}PI_{t-1}$	=	The percent change in the Gross Domestic Product Price Index based on the quarter ending six months prior to the effective date of the new annual tariff and the corresponding quarter of the previous year.
Z	=	The effect of any exogenous changes. Exogenous changes are positive or negative changes in the Company's revenues or expenses as defined in the Plan. In the calculation of the PSI, exogenous changes are expressed as a percentage of the Company's revenue received from intrastate, noncompetitive services.
0.0%	=	Inflation offset.

An example of how the Price Stability Mechanism will work is attached as Attachment B.

3. The PSI started at 100 upon Commission approval of this Plan in 1999. The PSI remained at 100 through the year 2001. Sprint's first calculation of the PSI was for the annual price cap filing in the year 2002.

4. The Service Price Index ("SPI") is the cumulative price change from current and prior years which tracks the actual total price changes for noncompetitive services. No Company proposed SPI may exceed, on a total intrastate basis, the PSI, except as otherwise

[8] The PSI relates to the sum of effective rates and units of demand which were realized during the previous twelve-month period. Growth in revenues that occurs as a result of growth in demand, customers, new services or any other source that is unrelated to the PSP formula rate changes already is reflected in the Price Stability Mechanism. Such growth in revenues is solely the productivity gain of the Company and may not be used for any other purpose.

expressly provided in this Plan (e.g., banking of decreases as set forth in Part 3, Section E, paragraph 1. herein).

5. The SPI shall be computed according to the following methodology:

$$SPI_t = SPI_{t-1} [\Sigma_i V_i (P_t/P_{t-1})]$$ [9]

When:

SPI_t	=	The proposed new SPI value.
SPI_{t-1}	=	The existing SPI value as of the last approved tariff filing.
P_t	=	The proposed price for rate element "i."
P_{t-1}	=	The existing price for rate element "i."
V_i	=	The current estimated revenue weight for rate element "i", calculated as the ratio of the base period demand for the rate element "i" priced at the existing rate, to the base period demand for all noncompetitive services priced at existing rates.

When a new service is incorporated into the index calculations, the demand for the new service during the base period must be included in determining the weights to be used in calculating the SPI.

6. On September 1st of each year (or the closest Commission working day to such date), beginning in 2000, the Company shall file with the Commission a PSI and SPI Report. Each such annual filing may be accompanied by tariffs to implement any required or authorized SPI.

7. The proposed tariffed rates will become effective subject to the Tariff Filing Process set forth below. The Commission shall review the tariff rate change proposals to determine whether they are designed to produce revenues so that the SPI is not greater than the PSI. If the Commission determines that the Company's rate proposals do not comply with this

[9] If the Department of Commerce should cease reporting the GDP-PI during the term of the Plan, then, subject to Commission approval, the Company will substitute an alternative index and make any adjustments to the formula necessary to replicate the current formula as closely as possible.

criterion, then the Commission may order the Company to modify them to produce an SPI value which is equal to the PSI. If the Company's proposals comply with this criterion, then the Commission shall approve them subject to the Consumer Protections in Part 3, Section F. herein.

8. The Company's annual PSP will be approved according to the following Tariff Filing Process. The Company will provide fifteen (15) days' advance notice of filing to the Commission and will generally describe the anticipated filing.[10] The Company will provide financial and cost data to the extent required by Act 183. Any and all interventions or complaints shall be due within ten (10) days of such filing. Twenty (20) days shall be reserved for Commission review of recommended decisions, if any, in this process. Responses to interrogatories would be due within ten (10) days of service. A Commission Order must be entered within one hundred five (105) days of the filing; otherwise, the tariff(s) shall become effective as filed, and shall be deemed to be approved. This procedure, as specified in this paragraph, is hereinafter referred to as the "Tariff Filing Process."

9. Notwithstanding any other limitations specified herein, the Company, or any other party, may request that the Commission make special revenue adjustments within the scope of the PSI to recognize significant exogenous events that are outside the Company's control as follows:

(a) Jurisdictional shifts in cost recovery when interstate revenues actually change;

(b) Subsequent state or federal regulatory and legislative changes which affect revenues or expenses, to the extent they are not captured in GDP-PI; and

[10] Notice may be provided to the public through newspaper advertisements, bill inserts or bill messages. Notice also will be served upon the OCA, OSBA, OTS and any other Chapter 30 party, as identified by the Commission's Secretary.

(c) Unique changes in the telephone industry that are not reflected in the overall inflation factor as measured by GDP-PI.

For example, the institution of a universal service fund in Pennsylvania, and any requirement that the Company participate as a contributor, shall be a qualifying exogenous event. Exogenous revenue changes shall be flowed through on a dollar-for-dollar basis, using the most recent per books revenue levels, without any investigation or review of earnings. Exogenous expense changes shall be flowed through, dollar-for-dollar, on the basis of review of that single expense item for which an exogenous change is sought, without any investigation or review of earnings, and using the most recent per books level of such expense. Results shall be adjusted to recognize the impact of gross receipts taxes. The Tariff Filing Process and Part 3, Section A, paragraph 8 herein shall apply to any such exogenous changes.

B. Rate Restructuring and Rebalancing

1. The Company restructured its rates during the first year of this Plan for residential and business customers and included touch tone charges as part of basic service rates, eliminated zone charges and multi-party service, consolidated its rate bands to three, and performed other local restructuring on a revenue neutral basis as provided for in Attachment A, attached hereto and incorporated herein by reference.

2. The Company shall be allowed to rebalance its rates in order to reduce Sprint's access rates, including the Carrier Charge,[11] in accordance with Act 183, subject to the following conditions:

(a) After December 31, 2003, the Company shall be permitted to increase residential local basic service rates above any weighted average rate cap ordered by the Commission if (1) the Commission requires the Company

[11] See footnote 16, *infra*

to charge a residential local basic service rate in excess of the rate cap in order to receive universal service funding, or (2) the Commission requires the Company to reduce its access rates and the Commission determines that it would be just, reasonable and affordable to increase residential basic service rates to fund all or a portion of such access reduction.

(b) The Company shall also have the opportunity to petition the Commission to increase or eliminate the aforementioned residential rate cap after December 31, 2003. All parties to the Company's Chapter 30 proceeding will have the opportunity to respond to such a petition.

(c) The rate rebalancing set forth under the subsections of this Plan was used to reduce the Company's access rates to an effective switched access rate of $.12 per minute of use. The Company received universal service funding as a result of the Global Telecommunications Settlement. Any other Settlement, or Commission Order, relative to the rate rebalancing set forth under Part 3, Section B. of this Plan was unaffected by such funding. Any universal service funding received by the Company shall be on a revenue neutral basis and shall be used to reduce access rates or to reduce other rates.

3. The Company may file tariffs proposing to rebalance and/or restructure its rates for noncompetitive services, either an increase or a decrease, upon the implementation date of the Plan, as authorized under Act 183. If a proposed tariff would not cause the Company's SPI to exceed the PSI as calculated in the most recent annual filing, then such tariff shall be approved, subject to Part 3, Section F. provided that:

(a) The SPI is not greater than the PSI except for the banking of decreases;

(b) Beginning in the year 2002, no other rate restructuring/rebalancing filing has become effective in the same calendar year which affects exchange service rates[12] exclusive of changes made pursuant to the PSI/SPI formula and exogenous events;

(c) The rates for those services which are established by the Commission as universal services do not exceed the level determined by the Commission to be affordable pursuant to the Universal Service proceeding or any successor docket; and

(d) In the event that an affordable rate is not established by the Commission, exchange service rates may not exceed the cost of providing such service.

4. The Company may also propose revenue neutral tariff rate changes to implement the results of Commission orders involving generic industry issues.

5. The Company may make rate decreases at any time.

6. The Commission shall review the tariff proposals to determine whether they are within the criteria listed in paragraph 3 above. If the Commission determines that the Company's rate proposals are not within these criteria, then the Commission may order the Company to modify them to produce a tariff which does not exceed these criteria. If the tariff proposals are within the criteria listed in paragraph 3. above, then the Commission shall approve them.

7. The Commission authorized process shall apply to all rate restructuring and rebalancing filings, and the Commission's standards at 66. Pa.C.S. §1308 would apply for any increase above the Commission approved weighted average rate cap for local residential service.

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[12] Exchange service, as defined in Sprint's tariffs, is the general telephone service rendered in accordance with individual Local Exchange Tariff and General Exchange Tariff provisions. <u>See</u>, Tariff Telephone Pa. P.U.C. No. 26, First Revised Page 13, attached hereto as Attachment D.

C. Modified Lifeline Service, Link Up Service and Universal Service

1. The Company provides Lifeline and Link Up programs for qualifying, low-income residential customers, which programs will remain in effect during the Plan. Lifeline service provides qualifying, residential service customers with the applicable residence local service monthly rate, minus the applicable discount in accordance with the approved tariff . The Link Up America program continues in accordance with the approved tariff discount.

2. Sprint also provides Optional Local Measured Service ("LMS") which allows measured calling to all points within the existing non-toll calling area. LMS is an economical way for customers to reduce their exchange service bills. LMS also will remain in effect during the Plan.

3. The Company also provides discounts or exemptions to disabled persons, which exemptions and percentage discounts will remain in effect during the Plan.

4. The Company shall be fully qualified to participate as a recipient of any universal service program instituted by the Commission. Nothing in this Plan, or the Company's regulation under Chapter 30, or its successor Act 183, shall disqualify it from full participation in any Pennsylvania or federal universal service programs.

5. All eligible telecommunications customers who subscribe to lifeline service shall be permitted to subscribe to any number of other eligible telecommunications carrier telecommunications services at the tariffed rates for such services; however, the Commission's regulations at 52 Pa. Code §64.01 et seq. relating to suspension and termination of residential telephone service shall continue to be applicable.

6. Whenever a prospective lifeline customer seeks to subscribe to local telecommunications service, the Company shall explicitly advise the customer of the availability of lifeline service and shall make reasonable efforts, where appropriate, to

determine whether the customer qualifies for such service and, if so, whether the customer wishes to subscribe to the service.

7. The Company shall inform existing customers of the availability of lifeline service twice annually by bill insert or message. The notice shall be conspicuous and shall provide appropriate eligibility, benefits and contact information for customers who wish to learn of the lifeline service subscription requirements.

8. The Company shall not be required to provide, after November 30, 2004, any new lifeline service discount that is not fully subsidized by the federal universal service fund.

D. New Services

1. The Company may introduce new services at any time.

2. If a new service is offered which falls within the definition of "protected services,"[13] then the Commission's existing regulations for tariff filing requirements at 52 Pa. Code §53.59 shall apply

3. Any new service which does not fall within the definition of "protected services" shall become effective upon a one day notice to the Commission.

4. Revenues from new noncompetitive services shall be included in the calculation of PSI and SPI, beginning with the first annual PSP filing after the new service has been in effect for one year.

5. Sprint may file special tariffs offering experimental treatment for new services, and such tariffs shall be effective when filed.

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[13] As used in this Plan, the term "Protected Service" shall refer to the following telecommunications services provided by Sprint, unless the Commission has determined the service to be competitive:

(1) Service provided to residential consumers or business consumers that is necessary to complete a local exchange call.
(2) Touch-tone service.
(3) Switched access service.
(4) Special access service.
(5) Ordering, installation, restoration and disconnection of these services.

E. Banking of Annual Price Decreases

1. After 2001, annual price decreases calculated under the PSI filed on September 1 of each year may be banked for application in future years, not to exceed four (4) consecutive years.[14] Such banking of decreases will be with interest at a rate set forth in 66 Pa. C.S. §1308.

2. The banked price changes must be implemented no more than four (4) years after the annual price change is applied.

3. If a decrease is greater than $500,000, the Company will implement the decrease immediately.

F. Consumer Protections

1. Nothing in this Plan shall be construed to limit the requirement of section 1301 (relating to rates to be just and reasonable) that rates shall be just and reasonable. The annual rate change limitations set forth in Sprint's Plan or any other Commission-approved annual rate change limitation shall remain applicable and shall be deemed just and reasonable under section 1301.

2. Financial and cost data, as authorized by Act 183, shall be provided for all rate increase proposals for protected services, except those provided under Section B, paragraph 2 above.

G. Other Act 183 Provisions

1. The Company, at its discretion, may offer and bill to customers on one bill bundled packages of services which include non-tariffed, competitive, noncompetitive or protected services, including services of an affiliate, in combinations and at a single price

[14] For annual price increases, the Company may apply them in future years, without limitation as to time.

selected by the Company. The Company may file an informational tariff for a bundled package effective on a one day notice.

2. When an alternative service provider is offering local exchange telecommunications services within an exchange of the Company, Sprint may reduce its prices on services offered within the exchange below the rates set forth in its otherwise applicable tariff in order to meet such competition. The Company may not offset revenue reductions resulting from such competitive pricing by increasing rates charged to other customers through its price stability mechanism or otherwise.

3. The Commission may not require Sprint to reduce access rates[15] except on a revenue-neutral basis to Sprint.

4. No person or entity may refuse to pay tariffed access charges for interexchange services provided by Sprint.

5. The Commission retains the authority to ensure that Sprint does not make or impose unreasonable preferences, discriminations or classifications for protected services and other noncompetitive services.

6. The Commission shall retain the power to review and revise quality of service standards contained in 52 Pa. Code (relating to public utilities) that address the safety, adequacy, reliability and privacy of telecommunications services and the ordering, installation, suspension, termination and restoration of any telecommunications service. Any review or revision shall take into consideration the emergence of new industry participants, technological advancements, service standards and consumer demand.

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[15] As used in this Plan, the terms "access rates," "access charges" and similar terms, unless the context requires otherwise, shall refer to special access service and switched access service. As used in this Plan, the term "special access service" shall mean service provided by the Company over dedicated, nonswitched facilities to interexchange telecommunications carriers or other large volume users that provides connection between an interexchange telecommunications carrier or private network and a customer's premises. As used in this Plan, the term "switched access service" shall mean service that provides for the use of common terminating, switching and trunking facilities of Sprint's public switched network. The term includes, but is not limited to, the rates for local switching, common and dedicated transport and the carrier charge.

PART 4 - ADDITIONAL COMPANY COMMITMENTS AND OTHER TERMS

A. Ongoing Regulatory Requirements

1. All services provided by the Company within the jurisdiction of the Commission are still subject to all provisions of 66 Pa. C.S. §1501, et seq., regarding safety, adequacy and reliability of telecommunications services. See, 66 Pa.C.S. §3019(b)(2).

2. The Company will continue to monitor service quality for noncompetitive services in compliance with Act 183. 66 Pa.C.S. §3019(b)(2).

3. The Company will comply with the Commission's Extended Area Service ("EAS") regulations, as revised by the Universal Service task force, on an interim basis. The Company may petition for waivers from those regulations as needed and can petition for an automatic waiver if a waiver is granted to a similarly situated company.

The Company will continue to provide EAS on required routes, will continue to regroup exchanges as appropriate and will be allowed to implement EAS-related rate increases, subject to restrictions in Section B, paragraph 2 above on Rate Rebalancing.

4. The Company will file affiliated interest agreements, in accordance with 66 Pa. C.S. §2101, et seq., unless such agreements involve services found or declared to be competitive in accordance with this Plan. The filings shall constitute notice to the Commission only and shall not require approval by the Commission. Review of the associated costs and benefits shall be deemed to be unnecessary. The Commission may seek information necessary to audit Sprint's accounting and reporting systems with affiliates pursuant to 66 Pa.C.S. §2101 et seq. (relating to relations with affiliated interests) and as set forth in Part 4, Section B, paragraph 2 of this Plan.

5. The Company shall continue to comply with Chapter 63 and 64 of the Commission's regulations as amended from time to time. The Company reserves the right to

petition for waivers of those regulations and to petition for an automatic waiver if it is granted to a similarly situated company.

6. Approval of this Plan shall not operate in any way to foreclose the Company from exercising any of its options, pursuant to the enactment of new state or federal legislation.

7. In the event that the Company effects a change either to its depreciation expense or depreciation reserve, Commission approval shall not be required; however, in the event of the reinstitution of any form of rate base/rate of return regulation of the Company, then the Company will request permission from the Commission to establish booked amounts for depreciation at that time.

8. In the event that Sprint applies to the Commission for the sale, merger, acquisition or other transaction required to be approved under 66 Pa.C.S. §1102(a)(3) of another local telecommunications company or any facilities used to provide telecommunications services, Sprint shall not propose to reduce the existing advanced service or broadband deployment obligations agreed to by the local exchange carrier that previously served the sold, merged or acquired property.

9. The terms of this Plan relating to access charges are subject to modifications resulting from the <u>Generic Access Charge Investigation</u> and the <u>Global</u> proceedings, Docket Nos. I-00960066, P-00991648 and P-00991649, as well as any other applicable final Commission order(s) entered, or to be entered, after the foregoing named proceedings.

10. The Company has complied, to the extent applicable to it, with the resolution of Docket Nos. L-00990141 and M-00960799, relating to imputation requirements for intraLATA toll services.

B. Reporting Requirements

1. The Commission's filing and audit requirements for Sprint shall be limited to the following:

(i) The Network Modernization Plan Report filed pursuant to Part 1 of this Plan.

(ii) An annual financial report consisting of a balance sheet and income statement.

(iii) An annual deaf, speech-impaired and hearing-impaired relay information report.

(iv) An annual service report.

(v) Universal service reports.

(vi) An annual access line report.

(vii) An annual statement of gross intrastate operating revenues for purposes of calculating assessments for regulatory expenses.

(viii) An annual State Tax Adjustment Surcharge ("STAS") computation for years in which a tax change has occurred, if applicable.[16]

(ix) A bona fide retail request report in the form determined by the Commission.

2. Notwithstanding any other provision of the Public Utility Code (Title 66), no report, statement, filing or other document or information, except as specified in Part 4, Section B, paragraph 1 of this Plan, shall be required of Sprint, unless the Commission, upon notice to

[16] This includes the State Tax Adjustment Surcharge (STAS) tariff filings pursuant to Commission STAS Guidelines (52 Pa.Code 69.51, et seq.), the State Tax Adjustment Surcharge Order and the Company's STAS tariff. STAS-related changes shall be excluded from the SPI calculation. The Company shall serve copies of its STAS filings on OCA, OSBA, and OTS, coincident with its submission of such filings to the Commission.

Sprint and an opportunity to be heard has first made specific written findings supporting conclusions in an entered order that: (i) it is necessary to ensure that Sprint is charging rates that are in compliance with Chapter 30 of the Public Utility Code (66 PA.C.S. §3011 et seq.) and their effective alternative form of regulation; and (ii) the benefits substantially outweigh the attendant expense and administrative time and effort required of Sprint to prepare it.

C. Term of the Plan

1. The legislation underlying the original Plan had a sunset date of December 31, 2003.. The amendments to this Plan are submitted pursuant to Act 183. Act 183 does not have a sunset date.

2. In the event of any appellate court reversal, remand, vacation, amendment or other modification of any Commission order approving or interpreting this Plan, or any aspect thereof, the Company retains the right to withdraw from the Plan.

3. No change may be made to this Plan without the express agreement of both the Commission and Sprint. Sprint may subsequently petition the Commission for approval of further modifications to this Plan, which the Commission may grant upon good cause shown.

4. The terms of Sprint's Plan and NMP shall govern the regulation of Sprint and, consistent with the provisions of Act 183, shall supersede any conflicting provisions of Title 66 or other laws of the Commonwealth and shall specifically supersede all provisions of Chapter 13 (relating to rates and rate making) other than §1301 (relating to rates to be just and reasonable), §1302 (relating to tariffs: filing and inspection), §1303 (relating to adherence to tariffs), §1304 (relating to discrimination in rates), §1305 (relating to advance payment of rates; interest on deposits), §1309 (relating to rates fixed on complaint; investigation of costs or production) and §1312 (relating to refunds).

D. Miscellaneous

1. Except as otherwise provided in 66 Pa.C.S. §3019(d), Sprint may not disclose to any person information relating to any customer's patterns of use, equipment and network information and any accumulated records about customers with the exception of name, address and telephone number. Sprint may disclose such information: (i) pursuant to court order or where otherwise required by federal or state law; (ii) to its affiliates, agents, contractors or vendors and other telecommunications carriers, as permitted by federal or state law; (iii) where the information consists of data which does not identify individual customers.

PART 5 - ADDITIONAL ACT 183 COMMITMENTS

A. Bona Fide Retail Request Program

No later than 90 days after the effective date of its amended Plan, the Company will implement a Bona Fide Retail Request ("BFRR") program in areas where it does not provide broadband. The Company's BFRR program will be implemented in accordance with the Company's written description of the program, to be filed with the Commission and provided to the Department of Community and Economic Development, not later than 30 days in advance of program implementation. The Company's BFRR filing, along with the applicable requirements set forth in Act 183, shall govern Sprint's implementation of a BFRR program.

B. Business Attraction or Retention Program

1. No later than 90 days after the effective date of its network modernization plan, Sprint shall establish a Business Attraction or Retention Program ("BARP") to permit the Department of Community and Economic Development ("DCED") to aggregate customer demand where necessary and facilitate the deployment of advanced or broadband services to

qualifying businesses which DCED seeks to attract to or retain in this Commonwealth and whose requests for such services are submitted by or through DCED.

2. The Company's participation in DCED's Business Attraction or Retention Program shall continue through December 31, 2015, or such earlier date as the Company achieves 100% broadband availability throughout its service territory.

C. Broadband Outreach and Aggregation Fund and Education Technology Program

1. The Company shall be assessed by the Commission for contribution to a Broadband Outreach and Aggregation Fund ("BOAF") and to the Education Technology Fund ("E-Fund") an amount of 20% of the first year's annual revenue effect of any rate increase permitted by the elimination or reduction of the offset under 66 Pa.C.S. §3015(a) and placed into effect. For purposes of this paragraph, the term "first year's annual revenue effect" means the projected or actual increased revenues received by the Company during the one-year period from the effective date of its rate increase. The Commission shall begin the assessments provided for in this paragraph on June 30, 2005, and thereafter shall make such assessments annually on June 30 until June 30, 2010, for assessments that include amounts for the BOAF and the E-Fund and until June 30, 2015, for assessments that include amounts for only the BOAF. Each assessment shall be based on the first year's annual revenue effect of any covered rate increase effective after the date of the last annual assessment.

2. An amount not to exceed 50% of such assessment shall be allocated to the BOAF. The remainder of the assessment shall be allocated to the E-Fund provided for under 66 Pa.C.S. §3015(d) until its termination on June 30, 2011. After the E-Fund termination, the maximum assessment percentage shall be reduced from 20% to 10%, and contributions shall be made only to the BOAF until the Company achieves 100% broadband availability.

Contributions of allocated amounts shall be paid to the BOAF and the E-Fund by the Company in equal quarterly installments.

3. In the event of overfunding in excess of the total BOAF amount, the overcollection shall be credited by DCED to the next year's contribution amount.

4. The BOAF shall continue until July 1, 2016, at which time the BOAF shall terminate, and DCED shall return any funds remaining in the BOAF, on a pro rata basis, to the local exchange telecommunications companies that contributed to the BOAF.

5. The E-Fund shall continue until June 30, 2011, at which time the E-Fund shall terminate and the Department of Education shall return any funds remaining therein, on a pro rata basis, to the local exchange telecommunications companies that contributed to the E-Fund.

D. Broadband School Discount

1. The Company shall offer school customers[17] in its service territory, that meet the eligibility standards described in 47 CFR §54.501 (relating to eligibility for services provided by telecommunications carriers) and that agree to enter into a minimum three-year contract with Sprint for telecommunications services, a 30% discount (or greater discount at the Company's discretion), in the otherwise applicable tariffed distance sensitive per-mile rate element and also will waive the associated nonrecurring charges for available intrastate broadband services where the telecommunications services are used for educational purposes and not for the provision of telecommunications services to the public for compensation. The discount or waiver shall not be required where application of it to a particular service would conflict with applicable law.

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[17] As used in Part 5, Section E, paragraph 1 of this Plan, the term "school entity" shall mean an intermediate unit, school district, joint school district, area vocational-technical school, independent school, licensed private academic school, accredited school and any other public or nonpublic school serving students in any grade from kindergarten through 12th grade.

2. The Company will assist school customers in applying for e-rate funding under 47 CFR § 54.505 (relating to discounts).

E. Assistance To Political Subdivisions

Sprint commits to make technical assistance available to political subdivisions[18] located in its service territory, in pursuing the deployment of additional telecommunications infrastructure or services provided by Sprint.

[18] "political subdivision" is defined as any county, city, borough, incorporated town, township, municipality, municipal authority, or county institution district.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rate of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	Docket No. I-00040105

REBUTTAL TESTIMONY OF
RUSSELL R. GUTSHALL

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 1.1

RECEIVED
MAR 26 2009
PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

Prefiled: January 15, 2009

Q. ARE YOU THE SAME RUSSELL R. GUTSHALL THAT FILED DIRECT TESTIMONY IN THIS PROCEEDING ON DECEMBER 10, 2008?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. I will specifically respond to certain statements made by Verizon (Price), OSBA (Buckalew), and AT&T (Nurse and Oyefusi), all of whom filed their respective Direct Testimonies in this proceeding on December 10, 2008.

Q. PLEASE PROVIDE A SUMMARY OF YOUR REBUTTAL TESTIMONY.

A. My rebuttal testimony explains how consumers continue to benefit from the state Universal Service Fund ("PA USF"), why the $18 rate cap is not arbitrary and the PA USF is not "contrary" to Legislative intent and policy, why an examination of RLEC costs is contrary to current law, why a generic price ceiling is unnecessary, and under what circumstances the state USF should be used to support the deployment of broadband service.

Q. ON PAGE 4 OF THE DIRECT TESTIMONY OF DON PRICE, HE STATES THAT THE PUC SHOULD REDUCE AND EVENTUALLY ELIMINATE THE PENNSYLVANIA USF. DO YOU AGREE?

A. Absolutely not. As I explained in my Direct Testimony, the PUC's Global Order described the Pennsylvania USF as "an exchange of revenue between telephone companies which attempts to equalize the revenue deficits occasioned by mandated decreases in their toll and access charges." That Order permitted RLECs, including Embarq Pennsylvania, to reduce their intrastate intraLATA toll and intrastate switched access rates and recover the lost revenue from the newly created state USF. Embarq PA's retail and wholesale customers continue to benefit from the lower switched access and long distance rates which resulted from the Global Order. As explained in more detail by Embarq PA witness Jeffrey Lindsey, Embarq Pennsylvania customers in rural, high cost areas of the state continue to benefit from rates that have been kept below cost and affordable by Embarq Pennsylvania's support from the state USF. No witness has offered evidence that these affordable, below-cost rates could be sustained without continued support from the Pennsylvania USF. The state USF support was and continues to be needed to help keep rates for basic local service affordable in high cost areas of Embarq PA's local service territory.

Q. IS THE $18 RATE CAP "ARBITRARY," AS AT&T ASSERTS ON PAGE 6 OF THEIR DIRECT TESTIMONY?

A. No. As Ms. Londerholm shows, it is not cost based, but that does not mean it is "arbitrary" as AT&T claims. As I explained above, the existing state USF was established by the Commission for the purpose of keeping basic local service affordable in high cost areas of the Commonwealth. The existing PA USF was designed to work in tandem with local rate caps. The rates of retail telephone consumers of rural ILECs remain affordable through a rate cap concept, and the state USF is the mechanism to ensure affordability as rural ILECs draw from the state USF.

Q. DO YOU AGREE WITH AT&T'S ASSERTION ON PAGE 4 OF THEIR DIRECT TESTIMONY THAT THE $18 LOCAL RATE CAP IS INCONSISTENT WITH ACT 183?

A. No. Messrs. Nurse and Oyefusi claim that Act 183 eliminated the productivity offset and thereby allowed ILECs to raise their local rates by the rate of inflation. In support, AT&T argues that the incentive to deploy broadband networks benefits local consumers (pages 4-6). AT&T further asserts at page 16 that increasing the PA USF would be contrary to legislative intent and policy (pages 16-17) because customers benefit from available broadband networks. These assertions are illogical and unfounded. I am not an attorney, but based upon my plain reading of Act 183 nowhere in there did the General Assembly expressly state that the inflation offset would and could be used, as AT&T now asserts, as a means to unravel the PA USF and the availability of universal service at affordable rates in the Commonwealth of Pennsylvania. AT&T's views of Act 183, if adopted, would mean that the General Assembly intended to <u>force</u> ILECs to increase basic local residential and business rates. There is nothing in Act 183 that explicitly binds the Commission in terms of setting the appropriate balance between allowable basic local rate increases and draws from the PA USF. My layman's reading of Act 183 leads to the conclusion that the intent of the Legislature was to give just as much value to universal service as to any other intended goal of Act 183. The PA USF was in existence when Act 183 was passed and the Pennsylvania General Assembly did not see fit to eliminate or bind the Commission's authority regarding the PA USF. As addressed in my Direct Testimony, Embarq PA maintains that rural ILECs can and should be afforded the opportunity to demonstrate a need to pierce a rate cap and go to the PA USF to ensure that retail end user rates remain affordable.

Q. ON PAGE 10 OF MR. BUCKALEW'S DIRECT TESTIMONY, HE STATES THAT THE WAY TO DETERMINE WHETHER THERE REMAINS ANY NEED FOR A SUBSIDY IS TO EXAMINE EACH COMPANY'S COST TO PROVIDE SERVICE. DO YOU AGREE?

A. I do not necessarily agree. By permitting and prescribing alternative forms of regulation, the state legislature wisely abandoned rate-base, rate of return regulation of local exchange carriers. The legislature instead focused regulation on local exchange carrier rates for basic local service. The legislature developed a formula by which local exchange carriers can adjust their noncompetitive revenues to reflect the annual impact of inflation. In addition, the General Assembly permitted local exchange carriers additional pricing flexibility for their more competitive and optional services. In doing so, the legislature offered local exchange carriers the incentive to keep their costs low and at the same time invest in their networks to provide new and innovative services to generate new and additional revenue. In doing so, the General Assembly also streamlined and reduced regulation. Mr. Buckalew would have the Pennsylvania Commission do the opposite of what the legislature intended.

Q. MR. BUCKALEW ALSO SUGGESTED ON PAGES 6 AND 7 IN HIS DIRECT TESTIMONY THAT RATE CAPS MAY NOT EXIST. DO YOU AGREE?

A. That is largely a legal debate. However, as I explained above, rate caps have been used as means to keep basic local residential and business rates affordable to determine the point at which a rural ILEC can draw from the PA USF. The continued application of the concept of rate caps as a means for keeping rates affordable and for determining, in part, an individual rural ILEC's draw from the PA USF are issues to be determined in this proceeding. Embarq PA maintains that a generic rate cap applicable to all rural ILECs is not necessary. As addressed above, individual rural ILECs should be afforded, within the context of the annual price cap filings, the ability to demonstrate the need for additional PA USF need based upon the operation of a rural ILEC's alternative regulation plan and upon other information that may be relevant to the demonstration of need.

Q. IN HIS DIRECT TESTIMONY AT PAGE 23, MR. PRICE STATES THAT IT IS NOT NECESSARY OR APPROPRIATE TO ESTABLISH A GENERIC CAP ON RLEC RATES IN THIS PROCEEDING. DO YOU AGREE?

A. Yes, I agree. As I said in my Direct Testimony and above, rural ILECs should be free to seek rate levels permitted by their alternative regulation plans. Economic and affordability considerations will dictate the rate levels RLECs can sustain in their markets. Rural ILECs should be free to demonstrate to the Commission that a proposed rate level permitted by its alternative regulation plan is appropriate and affordable. Rural ILECs should also be free to demonstrate to the Commission that, even though a given rate level permitted by the RLEC's alternative regulation plan is appropriate and affordable, rates can not rise above certain levels without the rural ILEC losing access lines to competitors and, thus, losing needed support from lower cost, more competitive areas to higher cost, less competitive areas. In this latter instance, the rural ILEC should be permitted additional support from the state USF, so long as the additional revenue is no more than the amount generated by its alternative regulation plan. As Embarq PA witness Mr. Lindsey explains in his Rebuttal Testimony, continuation of the PA USF is even more critical as rural ILECs lose subsidies that have historically flowed from their low cost to high cost exchanges and that support sustainability of rural ILEC networks.

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

A Yes.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	**Docket No. I-00040105**

SUR

REBUTTAL TESTIMONY OF
RUSSELL R. GUTSHALL

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 1.2

Prefiled: February 10, 2009

Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

A. My name is Russell R. Gutshall. I am the Senior Regulatory Affairs manager for Embarq Pennsylvania. My business address is 240 North Third Street, Suite 201, in Harrisburg, Pennsylvania, 17101.

Q. HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY IN THIS PROCEEDING?

A. Yes. I submitted Direct Testimony (Statement 1.0) in this proceeding on December 10, 2008. I also submitted Rebuttal Testimony (Statement 1.1) on January 15, 2009.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. My testimony is offered again on behalf of Embarq Pennsylvania and responds to the Rebuttal Testimonies offered by other parties in this proceeding.

Q. ON PAGE 18 OF THE REBUTTAL TESTIMONY OF E. CHRISTOPHER NURSE AND DR. OLA OYEFUSI, THEY DISAGREE WITH EMBARQ'S CONCLUSION THAT THE COMMISSION SHOULD DO NOTHING WITH RESPECT TO THE $18 RATE CAP. DO YOU HAVE COMMENTS CONCERNING THEIR STATEMENT?

A. Absolutely. AT&T has mis-characterized my Direct Testimony by excluding several important words. In my Statement 1.0 on page 5, I stated that Embarq PA is not requesting to raise the $18.00 monthly residential benchmark and the associated business monthly service rate **at this time** (emphasis added). I certainly was not suggesting that the Commission should totally ignore the issue of a cap or benchmark change, but rather pointing out that it is Embarq PA's recommendation that it is not necessary to alter the cap for Embarq PA **at this time**.

Q. PLEASE EXPLAIN FURTHER.

A. Embarq PA has not asked or petitioned the Commission to have its cap or benchmark increased, nor has there been any widespread requests by rural ILECs to do so. The need for such a change should be determined on a company-specific basis, based on a company specific request, and further supported by that specific company's need for doing so as contained in their alternative regulation plan.

Q. ON PAGES 20 AND 21 OF THE AT&T REBUTTAL TESTIMONY, THE WITNESSES STATE THAT ACCORDING TO EMBARQ'S TESTIMONY, EMBARQ ACKNOWLEDGES THAT ITS ALTERNATIVE REGULATION PLAN CANNOT BE USED FOR PURPOSES OF FUNDING ITS BROADBAND DEPLOYMENT. DO YOU AGREE?

A. No. I do not. Embarq Pennsylvania's amended alternative regulation was submitted and approved by the PUC in accordance with the provisions of Act 183. The legislative intent of Act 183 was to encourage the accelerated deployment of broadband throughout Pennsylvania and to provide Pennsylvania's Incumbent

Local Exchange Carriers (ILECs), including EMBARQ Pennsylvania , with the ability to increase revenues to be able to meet this broadband deployment commitment. While the legislation resulted in changes to EMBARQ's price-cap formula as a method to recoup the costs of broadband deployment, it did not in any manner limit nor prohibit EMBARQ from seeking revenues from other sources, such as the PA USF.

Q. DOES EMBARQ PA'S ALTERNATIVE REGULATION PLAN PROVIDE FOR THE OPPORTUNITY TO ACQUIRE ADDITIONAL FUNDS FOR SUPPORTING ITS NETWORK INFRASTRUCTURE AS WELL AS FOR BROADBAND DEPLOYMENT?

A. Yes. Embarq's alternative regulation plan defines the formula for calculating its overall revenue need. This calculation is performed annually and filed with the Commission in EMBARQ's annual price cap filing, and represents the need to maintain the integrity of the legacy network and management of the current infrastructure as well as the necessary revenues to meet the statutorily-mandatory deployment of advanced services. There is nothing in EMBARQ's amended alternative regulation plan that limits the acquisition of additional revenues to the company's annual price cap filing.

Q. IN VERIZON'S STATEMENT 1.1 AT PAGE 5, MR. PRICE CLAIMS THAT THE PUC SHOULD PLAN TO REDUCE AND ULTIMATELY ELIMINATE THE CURRENT USF. DO YOU AGREE?

A. No. When the PA USF was established, it contained no specific expiration date, and it does not have one now. Embarq's draw from the fund that was established in the Commission's Global Order was predicated at that time on a revenue neutral rebalancing of decreased intrastate access and toll charges. Those decreased rates remain in effect today, and therefore, the same fund contribution to Embarq that was implemented deserves to be continued. Embarq's draw from the fund is not only necessary to compensate for the revenue foregone due to those decreased access and toll rates, but also for the responsibility of an incumbent's obligation to continue to maintain its legacy network, the carrier of last resort responsibility that the ILECs' competitors do not have, and the ILEC's commitment to deploy its broadband services. The PA USF funding is more critical today than when it was established by the Global Order. In 2007, Embarq PA's receipts from the PA USF compared to intrastate basic local service revenues was 6.7%. This comparison has increased in recent years. In 2005, the comparison was less than 6%. By contrast, Verizon's contribution to the PA fund in 2007 was only 1.3% of basic local service revenues based on 2007 ARMIS 43-01 revenue information (line 1010, column G for Verizon local companies).

Q. ON PAGE 17 OF THE Verizon Statement 1.0, PRICE REBUTTAL, MR. PRICE STATES THAT THE RLECS ARE ACTUALLY PROFITING FROM THE CURRENT USF. DO YOU AGREE?

A. No. Upon Embarq PA's implementation of the PUC's Global Order, access and intraLATA rates were reduced in an amount equal to Embarq's draw from the USF. Those same reduced rates continue to be in effect today and continue to provide a financial benefit to those long distance companies (and their customers) who do business with Embarq. And Embarq has an ongoing obligation to maintain its legacy network. Whether a customer chooses to stay on Embarq's network or not, that obligation to sustain that network and facilities remains.

Q. FURTHER IN MR. PRICE'S STATEMENT 1.1 AT PAGE 43, HE CLAIMS THAT EMBARQ DID NOT JUSTIFY WHY IT SHOULD CONTINUE TO BE TREATED THE SAME AS SMALL COMPANIES. DO YOU HAVE COMMENTS?

A. Yes. When the state USF was established, the Commission included Embarq PA (Sprint LTD at that time) in the Small Company Plan along with all of the other rural incumbent telephone companies. Embarq PA was recognized then and continues to be a "rural" Company. Embarq PA's PUC approved Chapter 30 Plan that was attached to my Direct Testimony, states on page 1, footnote 1, that "Sprint (Embarq PA) is a "Rural Telecommunications Carrier" as defined in Section 3 of the Telecommunications Act of 1996 and for the purposes of Act

183. The mere fact that Embarq PA has a greater number of exchanges within the Commonwealth than most other RLECs does not make it any less rural.

Q. PLEASE EXPLAIN FURTHER.

A. Embarq's Pennsylvania service territory proves that Embarq is a very rural company. Embarq's franchised territory in Pennsylvania includes ninety-two exchanges. The average number of access lines served per square mile is 54, and approximately two-thirds of these exchanges include fewer than 25 access lines per square mile, with 6 exchanges serving 10 or fewer access lines per square mile. Indeed, Embarq Pennsylvania's territory is much more rural than non-rural.

Q. DOES THIS CONCLUDE YOUR TESIMONY?

A. Yes it does.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	**Docket No. I-00040105**

REBUTTAL TESTIMONY OF
JEFFREY L. LINDSEY

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 2.0

RECEIVED
MAR 2 6 2009
PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

Prefiled: January 15, 2009

Embarq
3

INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

A. My name is Jeffrey L. Lindsey. I am employed by Embarq Management Company ("Embarq") as Director, Regulatory Policy. My business address is 5454 West 110th Street, Overland Park, KS 66211.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on behalf of The United Telephone Company of Pennsylvania LLC d/b/a Embarq Pennsylvania ("Embarq PA" or "Company").

Q. BRIEFLY DESCRIBE YOUR EDUCATION AND PROFESSIONAL EXPERIENCE.

A. I earned a B.S. in Accounting from Ball State University and an M.B.A. with an emphasis in Finance from the University of Kansas. I am also a C.P.A. (inactive) licensed in the state of Ohio. I have twenty years of experience in the communications industry, having been employed by Embarq its predecessors (Sprint Nextel Corporation, Sprint Corporation, United Telecommunications, Inc.) since 1989. During my tenure, I have held a variety of responsibilities in regulatory, finance, consumer marketing, and wholesale marketing for local service, long distance, and wireless entities affiliated with Embarq's predecessors. My current responsibilities include managing regulatory policy matters in the areas of intercarrier compensation reform, universal service reform, retail service deregulation, interconnection agreement (ICA) arbitrations, among others. Prior to my current assignment, I served as Director of Federal Government Relations for Embarq's predecessor company in Washington, D.C. During that time I actively participated in industry intercarrier compensation reform efforts, universal service reform proceedings, and other matters under consideration by the Federal Communications Commission (FCC). My experience has provided opportunities to advocate policy positions before the FCC, U.S. Congressional members and committee staff, and various state public utility commissions, including Pennsylvania. Prior to my position as Director of Federal Government Relations, I managed state regulatory affairs on behalf of Embarq's predecessor for the states of California, Idaho, Indiana, Ohio, Oregon, and Washington. I have advocated regulatory policy matters before public utility commissions in these and several other states.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION AND ELSEWHERE?

A. Yes. I testified on the topic of intercarrier compensation in 2006 before the Pennsylvania Public Utility Commission. Additionally, I have testified in Indiana and New Jersey.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to rebut statements made in the direct testimonies of several parties as pre-filed on December 10, 2008 in this proceeding. Specifically, I will respond to several overarching policy issues raised and/or implicated by the direct testimonies of Verizon witness Mr. Don Price ("Price"), AT&T witnesses Mr. E. Christopher Nurse and Dr. Ola Oyefusi ("Nurse and Oyefusi"), Comcast witness Dr. Michael D. Pelcovits ("Pelcovits") and The Office of Small Business Advocate ("OSBA") witness Mr. Allen G. Buckalew ("Buckalew").

Q. PLEASE SUMMARIZE YOUR TESTIMONY

A. Several parties request reducing or eliminating the Pennsylvania state USF. First, I shall respond and explain the vital role played by explicit universal service funding to ensure the promise of universal service is kept and that communications services remain available. Suggestions made that federal USF receipts are somehow sufficient (OSBA witness Buckalew at 11, 12) absent a Pennsylvania USF remain fractured and reckless propositions. These parties focus on meaningless financial measures (e.g., Price at 14-21, Table 1) rather than on the relevant issue that the Pennsylvania Commission in 1999 embarked on a policy to ensure universal access to communications services at reasonable and affordable rates. Second, several parties baldly claim that the Pennsylvania USF is -- and/or if expanded would be -- anti-competitive. These assertions are incomplete and misguided, as addressed below. I will show how competition increases the need for explicit universal service support, particularly those customers at greatest risk: the rural, high-cost consumers. Finally, I will rebut Verizon's and Comcast's argument that larger rural carriers should not be entitled to USF receipts while smaller rural carriers should be permitted to maintain them.

Q. IS THE CONCEPT OF UNIVERSAL SERVICE VIABLE AND NECESSARY IN THE CURRENT COMPETITIVE ENVIRONMENT?

A. Yes. Universal service policy has been a historic success. It has been used to provide communications services to all consumers at comparable rates, terms and conditions, irrespective of cost. This was largely accomplished through a system of product and geographic cross subsidization. Residential basic local service, particularly in high-cost rural areas, was priced below cost. To recover this difference in the form of implicit support, toll services, switched access services and business basic local services were typically priced above cost. In a monopoly environment, this system worked quite well as U.S. telephone penetration rates increased from less than 36.9% in 1940 to greater than 97% by 2000.[1] However, it is obvious that the monopoly environment is largely a relic of the past. VoIP, wireless, and cable competitors, are strong and growing competitors in urban and suburban areas, in addition to rural town centers. But, competition remains elusive in rural unincorporated areas. In these rural outlying areas, cable

[1] Universal Service Monitoring Report, Table 6.2, "Historical Telephone Penetration Estimates", *CC Docket 98-202*, prepared by the Federal and State Staff for the Federal-State Joint Board on Universal Service in *CC Docket 96-45*, p. 6-13, *rel. January 2008*.

telephony is frequently not available, wireless services are less prevalent (and where they are they tend to offer less reliable service than more populated areas), and VoIP services that rely on broadband availability are not as readily available. The competitors of the ILEC do not bear the burden of the Carrier-Of-Last-Resort ("COLR") and tend to not serve the highest-cost customers in areas of low population density. To compound the problem for these rural consumers, competition in other areas erodes the very implicit subsidy on which they have depended to receive high quality, reliable communications services and rates comparable to urban consumers. For these reasons, it is imperative that explicit universal service funding remain available and sufficient to fulfill COLR obligations in a competitive environment, despite statements to the contrary by Verizon witness Mr. Don Price, (at 3,4 and response to PTA DR #10.) and AT&T witnesses Mr. Christopher Nurse and Dr. Ola Oyefusi (at 16).

Q. CAN YOU FURTHER EXPLAIN THE COLR OBLIGATION?

A. Yes. The COLR obligation is not merely providing service to new customers. It is much, much more than this one component. COLR is also maintaining and enhancing the ILEC's existing network. Where competition is less than robust, generally in the most rural of areas, Pennsylvania residents are even more dependent on the ILEC network than residents in other areas. Rural Pennsylvania consumers deserve dependable, advanced communications services at affordable rates. This is the essence of the COLR obligation.

Q. SHOULD THE COMMONWEALTH OF PENNSYLVANIA CONTINUE TO PROVIDE A MECHANISM TO FUND UNIVERSAL SERVICE?

A. Yes. Contrary to the statement of Verizon witness Price, the PUC should not "look to reduce and eventually eliminate the Pennsylvania USF." (Price at 4) If the PUC were to take such action and not sufficiently fund universal service, carriers must be relieved of their COLR obligations, and a long-held policy of universal service will effectively come to an end. The results of ending universal service policy are clear. Rural network buildout would become unsustainable and eventually cease. As a result, network reliability in rural areas could be significantly impaired. Retail rates in rural areas could increase significantly, by multiples of current rates in some areas as shown by Embarq witness Londerholm (at 14-15 and Table 1), to fully recover costs. The effect of such a policy shift would be to drive many lower income customers off the communications network. Obviously, an explicit universal service fund is a necessary component to provide reliable communications networks and services at comparable terms as those offered to urban and suburban customers once competition appears in these markets. To do less only exacerbates the digital divide and is unfair to rural customers.

Q. IS IT FAIR TO REQUIRE ALL PROVIDERS, INCLUDING 'COMPETITIVE' PROVIDERS, TO CONTRIBUTE TO AN EXPLICIT UNIVERSAL SERVICE FUND?

A. Absolutely. In fact, it would be unfair not to do so. Despite the statements of Verizon (Price at 3, at Response to PTA #10), Comcast (Pelcovits at 22) and AT&T (Nurse and Oyefusi at 15), the presence of competition is the very reason to establish an explicit universal service fund as traditional implicit support can no longer be sustained. And because competitive carriers are not required to serve all customers while ILECs bear the costs of the COLR obligation, it is necessary and appropriate for all carriers to share the funding burden to maintain the promise of universal service. Embarq remains committed to the concept of universal service and supporting rural consumers, despite efforts of behemoth urban-focused carriers to reduce their costs at the expense of these rural consumers and expand the digital urban/rural divide. Verizon and AT&T would have this Commission ignore the important goal of universal service and focus on the goal of competition, which may be illusory. Obviously, availability (one provider) is a condition precedent to competition (multiple providers). The fact that competition is not ubiquitous in Pennsylvania is not the fault of the state USF. It is the result of non-ILECs choosing to not offer service in areas where it is uneconomic to compete. Finally, it is important to note that the state legislature has recognized the validity of competitive carriers supporting the concept of universal service when it explicitly excepted state USF contributions from its recent VoIP deregulation bill[2]. State agencies are permitted to require VoIP competitors to contribute to the Pennsylvania USF.

Q. SHOULD LARGER CARRIERS BE DISADVANTAGED VIS-À-VIS SMALLER CARRIERS IN TERMS OF ELIGIBILITY TO RECEIVE USF FUNDING?

A. No. Carrier size should have no bearing on the question of eligibility to receive USF funding. Further, many of the financial metrics cited by Verizon (Price at 14-21) and Comcast (Pelcovits at (14-16, 19, 20) are of little use to determine funding eligibility. It is quite ironic that Verizon, as one of the nation's largest carriers[3] which benefits enormously from economies of scale, would attempt to argue that larger rural carriers should be disadvantaged versus smaller rural carriers in terms of eligibility to receive Pennsylvania USF distributions. (Price at 14-21). Verizon, and AT&T, enjoy scale benefits above all other carriers. I am confident that efforts to reduce or eliminate the scale benefits they enjoy via regulatory or legislative change would be met with vigorous objections by AT&T and Verizon. But, Verizon seeks to deny similar benefits to vastly smaller carriers, such as Embarq, Windstream, Frontier, Consolidated, and D&E because they are larger than the smaller rural LECs in Pennsylvania. This appears to be a hypocritical and economically unsound position to advocate. The size of the serving ILEC does not drive the need for USF. The need for USF is driven by the

[2] Act 52, passed in 2008.
[3] AT&T and Verizon's respective approximate market values as of January 9, 2009 were $158 billion and $92 billion. AT&T's market capitalization is more than 30 times that of Embarq's $5 billion value and Verizon's is greater by a factor of nearly 20.

existence of COLR obligations in high-cost areas. High costs are largely a function of customer density and distance: the lower the customer density, the higher the cost. Consider, for example, that Verizon service areas in Pennsylvania reflect a density of 195 access lines per square mile, while there are only 54 access lines per square mile in Embarq's Pennsylvania service areas. In areas of low customer density, revenues from existing customers in those areas will not cover costs due to affordability and competitive pressures. The size of the serving LEC is irrelevant. Verizon's position, if implemented, would have the effect of discouraging economy of scale by penalizing it. To follow this logic would be to say that Verizon should pay more for cost inputs such as cable and wire facilities, cell towers, handsets, gasoline, vehicles, building rent, etc, simply because it is larger. This argument is illogical. If this question is to be seriously considered, then the reverse must also be considered: does Verizon not possess sufficient scale to easily afford current Pennsylvania USF contribution obligations? And, in fact, does it not have capacity to contribute much more? Accordingly, it would be required to increase its contributions solely as a result of its size. It is disconcerting that a carrier of Verizon's level of sophistication would base its position on irrelevant financial measures instead of very relevant cost characteristics.

Q. WOULD SUCH A POLICY BE FAIR TO RURAL MID-SIZE CARRIERS?

A. Absolutely not. Such a policy would be unfair to rural mid-size carriers by forcing them to uniquely bear the COLR burden in high-cost areas. While smaller

RLECs would continue to receive Pennsylvania USF, mid-size rural carriers would not. This would cause great financial harm to mid-size rural carriers and impact their ability to continue to serve and invest. The outcome is analogous to FCC Chairman's Martin's ill-conceived intercarrier compensation and universal service reform proposed order[4] which generated a firestorm of opposition late last year. The Chairman's proposed order, supported by AT&T and Verizon, would have greatly reduced their intercarrier compensation and universal service expenditures[5] on the backs of mid-size rural carriers and the customers served by them: disproportionately high-cost rural customers. The Chairman's order would have drastically reduced mid-size carrier intercarrier compensation revenues and federal universal service fund receipts without providing an opportunity to recover revenues lost through operation of the proposed order. Wall Street analyst Frank Louthan of Raymond James Associates, Inc., released an Equity Research report[6] analyzing Chairman Martin's proposed order noting, "... mid-sized price cap carriers...stand to have an unfunded obligation. This means they have regulatory-imposed obligations to be the carrier of last resort (COLR) in their service territory but will not be able to service those obligations without losing money." Such an outcome is poor public policy and would be punitive to

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[4] *See ISP Remand Order and Intercarrier Compensation/Universal Service Reform*, Order on Remand and Report and Order and Further Notice of Proposed Rulemaking
[5] *See , e.g.*, Wall Street Journal, CALL TRANSFER RATE PLAN IS ON HOLD, The Wall Street Journal (November 4, 2008), ("Analysts say the proposal was worth millions to large phone companies such as AT&T, Inc., Verizon Communications, Inc. and Qwest Communications International Inc. Small and midsize carriers like Embarq Corp. and CenturyTel Inc. would have taken a hit.") Available at http://online.wsj.com/article/SB122574357296494187.html
[6] *See, Equity Research, Intercarrier Compensation Reform: Potential Impact from an FCC Order*, Raymond James Associates, Inc. (October 27, 2008) at 3.

rural LECs and their customers. Accordingly, the Pennsylvania USF should not be reduced or eliminated.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	Docket No. I-00040105

SURREBUTTAL TESTIMONY OF
JEFFREY L. LINDSEY

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 2.1

Prefiled: February 10, 2009

Embarq
4

INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

A. My name is Jeffrey L. Lindsey. I am employed by Embarq Management Company ("Embarq") as Director, Regulatory Policy. My business address is 5454 West 110th Street, Overland Park, KS 66211.

Q. ARE YOU THE SAME JEFFREY L. LINDSEY WHO SUBMITTED REBUTTAL TESTIMONY ON BEHALF OF THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC D/B/A EMBARQ PENNSYLVANIA ("EMBARQ PENNSYLVANIA") ON JANUARY 15, 2009?

A. Yes.

Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?

A. The purpose of this testimony is to rebut statements made in the rebuttal testimony of several parties as pre-filed on January 15, 2009 in this proceeding. Specifically, I will rebut the testimony of Verizon witness Mr. Don Price ("Price"), AT&T witnesses Mr. E. Christopher Nurse and Dr. Ola Oyefusi ("Nurse and Oyefusi"), Pennsylvania Office of the Consumer Advocate ("OCA") Mr. Roger D. Colton ("Colton"), and The Office of Small Business Advocate ("OSBA") witness Mr. Allen G. Buckalew ("Buckalew").

Q. PLEASE SUMMARIZE YOUR TESTIMONY

A. My position remains unchanged, despite the testimony of other parties in this proceeding. Competition increases the need for explicit support for ILECs with Carrier of Last Resort ("COLR") obligations. Unless and until the Commonwealth of Pennsylvania is ready and willing to relieve ILECs of these obligations, which require ILECs to serve all – profitable and unprofitable – customers, then explicit support will continue to be required. The Pennsylvania state USF plays a vital role in this regard. Competitive carriers are not required to serve unprofitable customers, so assuming they operate according to sound economic principles, they will not serve them. Requiring all carriers, including competitive and ILECs, to contribute to the Pennsylvania state USF is a fair and equitable policy to ensure all customers, including the unprofitable ones, have access to telecommunications services at rates comparable to profitable ones. The PA PUC must take a stand for its rural, high-cost, unprofitable consumers and continue its policy of maintaining a state USF, despite the claims of huge, urban-focused carriers who seek to eliminate their funding obligations and increase their profits regardless of the obvious detrimental impacts such action would cause to many rural Pennsylvania consumers.

In its rebuttal testimony Verizon again argues that the size of an ILEC and its corporate family should be determinative of its ability to receive USF funding. This is illogical because corporate family size has nothing to do with whether an ILEC, which has COLR obligations and must serve high cost unprofitable customers, is entitled to, and should receive, USF support. Verizon's thinly veiled attempt to escape its USF funding obligation, if successful, will produce one of two outcomes: (1) leaving rural Pennsylvanians at increased risk of losing the promise of universal service or (2) putting the question of alternative funding sources squarely in the lap of the PA PUC.

Q. DO YOU AGREE WITH AT&T'S WITNESSES NURSE AND OYEFUSI'S STATEMENTS REGARDING THE PRESENCE OF COMPETITON IN PENNSYLVANIA (AT&T REBUTAL AT 2, 3)?

A. No. AT&T's witnesses mischaracterize and overstate the statements of mid-size carriers regarding the level of competition in Pennsylvania. Although AT&T accurately quotes public statements of Embarq, PTA, Frontier, and North Pittsburgh (AT&T Rebuttal at 2, 3), it claims, "the evidence proves beyond any serious argument that there is an abundance of competition, in all corners of Pennsylvania." (at 2) But no carrier stated that competition is available to 100% of its customers, and it is not so available. Competition is simply available to a varying majority of ILEC customers. This distinction makes all the difference. This is why the Pennsylvania USF is so critical. Competitors, without a COLR obligation, generally serve only below average and average cost customers. Without a similar COLR obligation, they can operate business plans to largely avoid high-cost areas. In fact, it is economically rational to do so. However, this competition erodes historical implicit support available to ILECs, implicit support that was used to fund the ILEC's COLR operations. Accordingly, it is a fair and sound public policy to require all providers to contribute to a universal service fund in order to provide sufficient funding to continue the COLR mandate. AT&T admits that "market forces will ensure that rates are kept just and reasonable." (at 4) This is the very reason a USF is necessary as ILECs' historical support is eroded by competitive price reductions and market share loss. The existence of this "lost" implicit support is confirmed by research prepared by Comcast witness Pelcovits' firm, Microeconomic Consulting and Research Associates ("MiCRA"). In this report, MiCRA claims a potential consumer benefit of $111 billion from cable voice service competition.[1] Of this amount, $71.7B comes from "ILEC Competitive Response, Residential Market." Some portion of this $71.7B is indisputably implicit support that is no longer available to support the high cost rural consumers who are far less likely to have competitive alternatives, including cable voice alternatives.

Q. DO YOU AGREE WITH OCA WITNESS COLTON'S STATEMENT THAT COMPETITION FOR BASIC LOCAL SERVICE WILL NOT CONTINUE TO GROW IN PENNSYLVANIA (OCA REBUTTAL PAGE 2)?

A. No. Mr. Colton's answer appears to rely on the claim that when basic local service is included in a bundled service offering, it is no longer competition for basic local service. I disagree with this assessment because a customer lost to a CLEC's bundled offering is just as "lost" as a customer who leaves for a

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[1] "Consumer Benefits from Cable-Telco Competition," Michael D. Pelcovits and Daniel E. Harr, Updated November 2007, http://www.micradc.com/news/publications/pdfs/Updated_MiCRA_Report_FINAL.pdf

competitor's basic local service. Basic local service competition is clearly growing, primarily through bundled and intermodal service offerings. When an ILEC loses a customer to competition, it is irrelevant whether that customer is lost to a provider with a stand-alone offering or a bundled service offering. Customers are increasingly indicating a strong preference for bundled services, and providers are increasingly striving to meet this demand. Bundled services create a ceiling for stand-alone basic local services. As the price differential between stand-alone basic local services and bundled services (inclusive of basic local service) decreases, an increasing number of customers will step up to the increased value provided by bundled services. This is a general principle of marketing, applicable across markets and products.

Q. DO YOU AGREE WITH THE TESTIMONY OF OCA WITNESS LOUBE REGARDING WHY CLECS ARE NOT ACTIVELY PROVIDING COMPETITION IN THE STAND-ALONE BASIC EXCHANGE MARKET (OCA REBUTTAL AT 19, 20)?

A. While not factually incorrect, I believe his answer is incomplete. Three additional factors are important to completely answer this question. The first is that competitive carriers do not have COLR obligations, so they simply choose not to serve rural residential customers, whose lower population densities produce higher costs. Second, universal service goals restrict ILEC pricing to rural customers, requiring service in many areas to be provided below cost. Third, practically all providers recognize customers overwhelming preference for bundled service offerings, so their business plans are designed to reflect this reality.

Q. DO YOU AGREE WITH THE TESTIMONY OF OCA WITNESS LOUBE THAT WIRELESS DOES NOT PROVIDE COMPETITION FOR THE STAND-ALONE BASIC EXCHANGE MARKET (OCA REBUTTAL AT 20)?

A. No. Wireless service does compete for and is a substitute service for stand-alone basic exchange service. Substitute services are services that satisfy the same demand and have the ability to take business away from each other (e.g., using a taxi or a shuttle service from an airport to a hotel). Complements are products and/or services that are used together (e.g., peanut butter and jelly). To make a call, customers use a wireless phone or a wireline phone, not both. And wireless service as a substitute for wireline service is growing rapidly as the number of wireless only "cord cutting" customers continues to expand. Wireless service is available for the overwhelming majority of Embarq's customers. While I do not dispute Loube's data cited on pages 20-21, I disagree with his conclusion. Loube mentions that because wireless prices tend to be significantly higher than basic local service rates, that they cannot be substitutes for each other. I disagree. Services can be substitutes for each other despite wide price disparities. Additionally, there are growing wireless alternatives which offer lower price points in the market. Dr. Loube's analysis fails to mention prepaid wireless service offerings, which can be much cheaper than the $49 per subscriber per month listed on page 21. Prepaid wireless service is growing and offers a more affordable alternative than traditional post-paid wireless plans to compete with wireline stand-alone basic exchange services. Wireless services are clearly a fast-growing substitute for basic local exchange services.

Q. DO YOU AGREE WITH OCA WITNESS LOUBE'S STATEMENTS REFUTING VERIZON WITNESS PRICE REGARDING THE CONTINUING NEED FOR THE PENNSYLVANIA STATE UNIVERSAL SERIVICE FUND (OCA REBUTTAL AT 24,25)?

A. Yes. The "additional responsibilities" include the long-standing COLR obligation. It would be both unfair to ILECs with the COLR obligation and a poor public policy result to refrain from providing the necessary amounts to adequately fund the COLR obligation. Further, Loube accurately states that the Pennsylvania USF was created to offset the loss of certain ILEC intrastate switched access revenues. It did not produce a "direct benefit" in the form of new revenues to these ILECs.

Q. DO YOU AGREE WITH AT&T WITNESSES' STATEMENT THAT COMMISSION PRECEDENT AND PUBLIC POLICY DICTATE "REDUCING SUBSIDIES" (AT&T REBUTTAL AT 26)?

A. No. Commission precedent and public policy do not dictate that implicit subsidies be made explicit. However, if the PA PUC decides to reduce or eliminate implicit support, sound public policy dictates that it must be replaced through an explicit mechanism.

Q. DO YOU AGREE WITH OCA WITNESS LOUBE'S STATEMENTS THAT THE 1996 ACT REQUIRES THE FCC TO ESTABLISH RULES THAT PRESERVE AND ENHANCE UNIVERSAL SERVICE (OCA REBUTTAL AT 26)?

A. Yes. The concept of universal service requires a minimum of one provider. Universal service fund policies must ensure service availability through a minimum of one provider before considering policies to promote competition. Requiring an ILEC to serve a high cost customer at below cost rates without USF support is grossly unfair to the ILEC because it places the ILEC at a competitive disadvantage. Policies that create unfunded mandates on COLR providers will ultimately result in some areas where service is no longer available from any provider, an outcome clearly contrary to universal service goals.

Q. DO YOU AGREE WITH OSBA WITNESS BUCKALEW'S STATEMENT THAT FEDERAL USF SUPPORT IS APPLIED IN A UNIFORM FASHION (OSBA REBUTTAL AT 2)?

A. Absolutely not. The federal USF is full of distinctions based on carrier size, rural or non-rural status, number of access lines, eligible telecommunications carrier ("ETC") status or competitive eligible telecommunications carrier ("CETC") status, wireline or wireless, among others. The federal USF simply does not provide sufficient support to ILECs that are required to serve high-cost customers at below cost rates.

Q. DO YOU AGREE WITH OSBA WITNESS BUCKALEW THAT THE PA USF SHOULD BE DISCONTINUED (OSBA REBUTTAL AT 6)?

A. Consistent with my earlier statements, competition is the reason to continue the PA USF. Competitors routinely "cherry-pick" and leave unprofitable high-cost areas to be served by ILECs bound by COLR obligations. This obligation must be funded or, in the alternative, eliminated. Universal service availability must be the primary objective of the Pennsylvania USF, with competition being a secondary consideration.

Q. DO YOU AGREE WITH AT&T'S CLAIM THAT ASKING PENNSYLVANIA CONSUMERS, PRIMARILY VERIZON CONSUMERS, TO FUND THE PENNSYLVANIA USF WOULD BE ANTI-COMPETITIVE (AT&T REBUTTAL AT 27)?

A. No. Such a policy is consistent with the tenets of historical universal service. The many non-rural, urban customers each bear a small financial burden to support the relatively few rural customers to ensure everyone has access to comparable network services at comparable rates. To suggest otherwise would be unfair to these rural customers and likely bring an end to universal service.

Q. DO YOU AGREE WITH OSBA WITNESS BUCKALEW'S STATEMENTS THAT A LOW INCOME FUND SOLVES THE UNIVERSAL SERVICE PROBLEM (OSBA REBUTTAL AT 3, 10)?

A. No. As stated above, the primary problem is a combination of uniquely-borne ILEC COLR obligations to serve high-cost areas and competition in lower cost areas. Although the low income USF serves an important and sound public policy purpose, it is solving a different problem than the high cost problem. Further, Buckalew's use of electric, gas, water, and wastewater service "analogies" (at 10) is faulty because these industries do not face competition. Thus, they permit historic implicit support regimes to continue. This is why use of only a low-income USF-like support system is sufficient in these industries. Before the advent of competition in telecommunications markets, a "low income only" solution may have been sufficient. But with the advent of competition and the current state of increasing and widespread competition, a high cost USF is necessary.

Q. DO YOU AGREE WITH AT&T'S WITNESSES' STATEMENT THAT THERE IS NO NEED FOR A REGULATORY-IMPOSED RATE CAP WHEN COMPETITION EXISTS (AT&T REBUTTAL AT 3)?

A. Yes. However, this a separate question than whether a rate should be used as part of a formula to determine the proper level of USF support, commonly referred to as a rate benchmark. If retail rates are part of a computation to determine the proper level of USF support, two major considerations exist to determine the proper rate level. First, the rate level must be high enough to ensure the ILEC has sufficient incentive to keep prices at least comparable to urban rates. To set a rate benchmark below this level could produce a USF that is larger than necessary. Second, it is imperative that the rate not be set too high. If the benchmark is set too high, the result would be to effectively force ILECs to price higher than comparable urban rates and lose market share to competitors, an outcome noted by AT&T (at 4). Or, the ILEC would be faced with forgoing needed USF support in an attempt to maintain a greater number of customers even in the face of the resulting unfunded mandate. Competitive carriers have the incentive to use USF reform proceedings as an opportunity to set a rate benchmark too high and gain a competitive advantage through regulatory fiat. Such an outcome would be poor public policy. The question of retail customer affordability and the proper retail rate benchmark, if applicable, are two different questions designed for two different purposes.

Q. DO YOU AGREE WITH AT&T'S STATEMENT THAT LECS "WILLINGNESS TO FOREGO REVENUE INCREASES SHOULD SPEAK VOLUMES ABOUT THOSE CARRIERS' ALLEGED NEED FOR THOSE ADDITIONAL REVENUES" (AT&T REBUTTAL AT 27)?

A. No. AT&T's earlier statement that competitive markets keep rates just and reasonable (at 4) answers this question. The market will not permit rate increases without additional market share loss. Accordingly, the LECs face a true Hobson's choice: either raise the retail rate and forego revenue as a result of market share loss or forego revenues by not increasing retail rates up to levels permitted by regulation. In either event, the ILEC will not realize the amount of authorized regulatory revenue. Accordingly, the revenue is not truly foregone. The "volumes" being spoken in this regard is that a retail rate benchmark for USF purposes, if utilized, must not exceed market-based rates.

Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?

A. Yes.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund	: : : :	Docket No. I-00040105

REBUTTAL TESTIMONY OF
CHRISTY V. LONDERHOLM

ON BEHALF OF
THE UNITED TELEPHONE COMPANY OF PENNSYLVANIA LLC
d/b/a EMBARQ PENNSYLVANIA
("Embarq Pennsylvania")

STATEMENT 3.0

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Prefiled: January 15, 2009

Embarq
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I. INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, EMPLOYER AND CURRENT POSITION.

A. My name is Christy V. Londerholm. My business address is 5454 West 110th Street, Overland Park, Kansas 66211. I am employed as Manager – Cost Support for Embarq.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on the behalf of The United Telephone Company of Pennsylvania LLC, d/b/a Embarq Pennsylvania ("Embarq PA" or "Embarq Pennsylvania").

Q. PLEASE SUMMARIZE YOUR QUALIFICATIONS AND WORK EXPERIENCE.

A. I received a Bachelor of Science degree in Mathematics from the University of Missouri – Kansas City in 1990. In 2005, I received a Masters of Arts in Finance from Webster University – Kansas City.

I began my career with Sprint in 1998 as a Project Manager in the Customer Service Organization's Decision Support group. In this role, I worked directly with Sprint's financial reporting and operational systems. My responsibilities included projects associated with Outside Plant Engineering and Construction, Labor, Installation and Repair metrics, and General Accounting.

In 2002, I was promoted to the position of Costing Manager. In that role, I was responsible for developing and maintaining programming necessary to process Sprint's Economic Cost Model. I was responsible for enhancing and assisting in the investment development and expense development of the Model. I facilitated the processing and analyzed the results for Sprint's Total Element Long Run Incremental Cost ("TELRIC"), Total Service Long Run Incremental Cost ("TSLRIC"), Switched Access, Reciprocal Compensation, and Basic Service Studies. I performed analyses on external cost models and business cases presented to Sprint.

In 2005, I was promoted and given responsibility for Sprint's Loop Costing Module and Expense Modules. These responsibilities include input analysis, algorithm development, and output validation for these Embarq in-house built modules. In May of 2006, the Local Telephone Division of Sprint was spun off into a stand-alone company, Embarq. My title with Embarq is Manager – Costing Support, and I have the same responsibilities in my current position with Embarq that I previously had with Sprint.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE OTHER PUBLIC UTILITY COMMISSIONS?

A. Yes. I have previously testified before state regulatory commissions in Texas, Nevada, Florida, Ohio, and Georgia.

II. PURPOSE AND SUMMARY OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My testimony addresses several conclusions reached in the direct testimony of PA OCA witness Dr. Robert Loube. Specifically, I will discuss the cost study presented by Dr. Loube that purports to represent Embarq's cost. I will discuss Dr. Loube's use of his cost study results to reach incorrect conclusions.

Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY

A. I begin my testimony discussing OCA's results for Embarq's monthly line costs. I will explain that, contrary to Dr. Loube's testimony, loop costs are a direct cost of basic local service. I show that there is no relationship between the development of the rate cap benchmark and the cost of the underlying service thereby showing Dr. Loube is incorrect to assert that the rate cap benchmark covers incremental costs. I will present evidence that Embarq's existing revenue from residential customers do not cover the costs of the services to which they subscribe. Lastly, I provide a schedule showing Embarq's estimated draw from a revamped Pennsylvania Universal Service Fund ("PA USF") funding mechanism based upon revenue and cost.

III. COST STUDY PRESENTED BY OCA

Q. ARE YOU FAMILIAR WITH THE COST MODEL DR. LOUBE USED IN DEVELOPING EMBARQ'S COST PER LINE?

A. Yes. The cost model employed by Dr. Loube is the High Cost Proxy Model 2.6 ("HCPM"). The HCPM is publicly available from the FCC website.

Q. ARE THERE REASONS TO DOUBT THE COST STUDY RESULTS PRESENTED BY DR. LOUBE?

A. Yes. The HCPM is of limited value. It has not been updated to take advantage of current desktop computer capabilities or of the substantive advancements in cost modeling. Cost modeling has advanced significantly from this version of the model. The HCPM default input values have not been updated for almost 10 years and were not publicly supported at their outset. As Dr. Loube himself points out, there have been numerous criticisms of the cost model used to produce his results (Loube at p. 23). Embarq is not currently seeking to adjust or establish rates (and is not now seeking additional support from the PA USF.) However if specific rates for services are to be adjusted or established for Embarq based upon *__costs__*, a more accurate cost model must be used. Moreover, Messrs. Lindsey and Gutshall provide rebuttal to various policy issues. Any potential policy arguments seeking to adjust Embarq's existing rates and revenues (e.g., intrastate switched access rates) or to reduce Embarq's current draw from the PA USF (as some parties have suggested) would necessitate such a more accurate, Embarq-specific cost model.

Q. CAN THE RESULTS OF DR. LOUBE'S COST MODEL BE USED FOR A BASIC UNDERSTANDING OF COST?

A. Yes, the *results* of his cost model work can be used for a basic understanding of costs. However, both the methodology and the results of Dr. Loube's study give only a cursory understanding of the costs. Although Dr. Loube updated the cost model inputs for loop investment, he did not update the cost model inputs for switch and transport investment. I disagree with Dr. Loube's use of old default cost model input values for Embarq's switch and transport cost (Loube at p. 25). These default values grossly underestimated Embarq's cost at the time and continue to do so. Although Dr. Loube's cost model results are understated, I believe they can be used for the level of understanding needed in this docket.

Q. HAVE YOU HAD THE TIME TO FULLY REVIEW THE COST MODEL INPUTS DR. LOUBE USED FOR EMBARQ?

A. No. Embarq did not receive the final results until just two weeks prior to the due date for my Rebuttal Testimony (January 15, 2009). Therefore, I have not had sufficient time to analyze all the input values used for Embarq's results. With only a quick review, I am unable to reconcile the line counts we provided to Dr. Loube with the counts he used. As Dr. Loube states (and I have confirmed) he has not updated all input values with those provided through discovery (Loube at pp. 24. p. 25).

IV. LOOP COSTS ARE A DIRECT COST OF BASIC LOCAL SERVICE

Q. DR. LOUBE DIVIDES THE RESULTING MONTHLY COST PER LINE INTO 2 COMPONENTS. ONE HE CALLS NON-LOOP OR INCREMENTAL AND ONE HE CALLS LOOP OR NON-INCREMENTAL (LOUBE P. 17.) DR. LOUBE OPINES FURTHER THAT THE LOOP COST IS NOT INCREMENTAL TO BASIC EXCHANGE SERVICE (LOUBE AT P. 17). DO YOU AGREE?

A. No. When a customer contacts Embarq for service it is to establish basic local exchange service. Embarq builds loops to customers to provide basic local exchange service. Therefore the cost causation to Embarq for the loop is basic local exchange service. Dial tone requires a loop to a requesting customer. If a customer chooses to add other services, such as long distance or a custom calling feature, the dial tone must be there first. Loop investment is a direct cost of basic local exchange service.

Q. HAVE EMBARQ PA'S RESIDENTIAL CUSTOMERS HISTORICALLY BEEN REQUIRED TO COVER THE ENTIRE COST OF THEIR RESIDENTIAL BASIC LOCAL SERVICES?

A. Absolutely not. As Embarq's witness Jeffrey Lindsey discusses, there are numerous policy issues around universal service. Service availability at affordable rates has been a "historic promise" that has kept residential customers from bearing the total cost of their basic service for decades.

Q. DR. LOUBE CONCLUDES THAT CHAIRMAN CAWLEY ENDORSES LOOP COSTS AS NON-INCREMENTAL TO BASIC EXCHANGE SERVICE. DO YOU READ THE MOTIONS AND CONCLUDE THE SAME (LOUBE AT P. 17)?

A. No. The differences between costs and prices are often blurred. In our industry and as I stated above, individual residential service rates do not equate to their corresponding costs. Rather a system of end-user rates, explicit and implicit subsidies have existed to achieve universal service goals. As Dr. Loube states, the loop cost is by far the largest component of the total monthly cost per line (Loube at p. 21). The shell game of allocating loop cost recovery to any other service than the one under examination has been used to avoid dealing with the reality of pricing residential basic local service rates below cost. Loop costs are a direct result of an order for basic local service, but to maintain universal service the costs must be recovered across a combination of mechanisms. I read Chairman Cawley's motion to state the <u>recovery</u> (prices) of loop costs will be through multiple services that utilize the loop and not just the single initial cost causer service of basic local.

Q. IS THERE FURTHER EVIDENCE THAT THE PA PUC DISTINGUISHES BETWEEN COSTS AND THE VARIOUS SOURCES OF RECOVERY OF THOSE COSTS?

A. Yes. As the PA PUC pointed out to the FCC regarding the FCC's use of an incremental cost study, the proposed exclusion of loop costs is a means to justify a rate.[1] The PA PUC goes on to rightly say:

> The supporters of the new incremental cost model do not present convincing arguments that joint and common costs should be excluded in ***developing rates*** for access services and reciprocal compensation.(Emphasis added)

Q. You state loop cost is a direct cost. The Pa PUC calls it a joint cost. Is this a new debate on how to categorize loop costs?

A. Not at all. And this Commission should not be distracted by this difference in defining loop cost as direct or joint. What is inarguable is that the totality of cost at an appropriate level of de-averaging must be dealt with in relation to cost recovery.

Q. Are you recommending a cost allocation methodology or cost recovery mechanism?

A. No, I am not testifying to any specific cost allocation methods or rate design. I am pointing out the importance of understanding the relationship between costs and final prices to recover costs. As Chairman Cawley stated in his "Statement Concurring In Results" of April 9, 2008:

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[1] Reply Comments of the Pennsylvania Public Utility Commission. December 22, 2008, *In the Matter of Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, Universal Service Contribution Methodology*, WC Docket No. 06-122. Page 26.

> "In short, the rural ILEC rate cap, the rural ILEC access charges, the implementation of the Pa. USF, and the Chapter 30 original alternative regulation and price stability mechanism plans for the majority of the rural ILECs operated in a manageable and synchronized fashion under the regulatory oversight of this Commission."

The recovery of cost is not so simple as determining a single incremental cost for switching and transport as Dr. Loube has asserted. It must be done in a "synchronized fashion" or holistic system as Chairman Cawley states.

V. THE RESIDENTIAL RATE CAP BENCHMARK WAS NOT DEVELOPED BASED UPON COSTS

Q. WAS THE $18 RATE CAP BENCHMARK DETERMINED BASED UPON COSTS?

A. No. My understanding is the $18 rate cap benchmark was not developed based upon costs. Embarq PA witness Russell R. Gutshall discusses the history behind the $18 rate cap benchmark. I understand the rate was set to meet the "statutory requirements for maintaining and enhancing universal telecommunications services at affordable rates." Page 24, Order of April 9, 2008.

Q. WAS THE $18 RATE CAP BENCHMARK SET TO ENSURE RECOVERY OF INCREMENTAL COSTS AS DEFINED BY DR. LOUBE?

A. No. It is my understanding that this Commission had not undertaken cost study reviews to set the $18 rate cap benchmark. Therefore, it is not correct to conclude that the $18 rate cap benchmark is appropriate *based upon costs*.

Q. YOU STATED EARLIER THAT EMBARQ PA'S RESIDENTIAL CUSTOMERS DO NOT REMIT PAYMENTS THAT ALLOW EMBARQ PA TO FULLY RECOVER THE MONTHLY LINE COSTS AS PRESENTED BY DR. LOUBE. CAN YOU PRESENT EVIDENCE FOR THIS ASSERTION?

A. Yes. Table CVL-1 below shows exchange level detail of the revenues received directly from residential customers and an estimated residential cost per line for the exchanges Dr. Loube has provided. Based upon Dr. Loube's cost model results, only 3 of the 61 exchanges need no subsidy from other sources. I suspect that, if these 3 exchanges were further de-averaged, the cost per line of the customers in the non town center areas would be greater than the revenue as shown on Table CVL-1.

Q. ARE YOU RECOMMENDING THE $18 RATE CAP BENCHMARK BE INCREASED?

A. No. I make no recommendations about the proper rate cap benchmark for Embarq PA. Embarq PA's witness Russell Gutshall has submitted testimony supporting Embarq's positions on this issue. Mr. Lindsey is also addressing policy issues affecting pricing. I am recommending *if* this Commission chooses to set rates based upon costs that a holistic system be applied that properly accounts for all costs. To use an incremental standard, as proposed by Dr. Loube, creates an incorrect view of the total costs that must be recovered. As the PA PUC stated in their Comments to the FCC the appropriate cost model is based upon the TELRIC/TSLRIC methodology.[2] If any company set all prices equal to incremental cost as defined by Dr. Loube, they would go out of business.

VI. ESTIMATE OF EMBARQ'S RECOVERY REQUIREMENT FOR UNIVERSAL SERVICE PURPOSES

Q. HOW MUCH COULD EMBARQ EXPECT TO DRAW IF THE PENNSYLVANIA COMMISSION IMPLEMENTED A STATE USF PROGRAM THAT ALLOWED RECOVERY OF THE COST DIFFERENCE BETWEEN RESIDENTIAL CUSTOMER PAYMENTS AND THE COST TO SERVE THOSE CUSTOMERS?

A. Table CVL-1 includes an estimate of the annual amount Embarq PA requires to fully recover the difference between residential end-user revenues and the estimated residential cost results presented by Dr. Loube for 61 of Embarq PA's exchanges. Embarq sent detail to Dr. Loube for 96 exchanges for modeling purposes. But due to cost model problems as discussed earlier the model produced results for only 61. I estimate the excluded residential line count to be 9.500. For the excluded lines, I used an overall average to estimate a PA USF

[2] *Id at* 4.

draw. I estimate a conservative total amount to be **[BEGIN PROPRIETARY]** [redacted] [END PROPRIETARY]

[BEGIN PROPRIETARY] – TABLE CVL – 1

[redacted]

[redacted]

[END PROPRIETARY]

Q. WHAT IS THE COLUMN TITLED "RESIDENTIAL MONTHLY COST PER LINE – EQ ADJUSTED" IN TABLE CVL-1?

A. Residential customer monthly line costs are higher than the overall average. As Dr. Loube points out lower density drives higher costs and longer distances drive higher costs. Residential customers generally have longer loops and tend to be more dispersed. Those facts cause a higher cost per line for residential customers than for business customers. To accurately compare the revenue from residential customers to their specific costs, I found it necessary to adjust Dr. Loube's average cost per line for each exchange. If the subsidy that flows from business customer revenues to residential customer revenues is to be eliminated, the cost specific to residential customers by exchange is needed. Current modeling techniques allow for this level of detail. Specifically, I multiplied exchanges with fewer than 10,000 lines by 1.05% and the ones greater than 10,000 lines by 1.12%. Larger exchanges generally have a higher percentage of business customers thus creating greater average weighting to the lower business monthly cost per line.

Q. ARE YOU RECOMMENDING THE PA USF BE INCREASED TO FUND THE AMOUNT OF RECOVERY IN TABLE CVL-1?

A. No. I make no recommendation about the proper funding or policy for the Pa USF. Mr. Gutshall has submitted testimony supporting Embarq's positions on this issue. Mr. Lindsey is also addressing policy issues on universal service. I prepared the data in Table CVL-1 to allow this Commission a better opportunity to understand Embarq's cost and in support of the testimony of Mr. Gutshall and Mr. Lindsey.

Q. CAN YOU PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY?

A. Yes. Dr. Loube's own cost study results show that Embarq PA has an overall estimated average monthly cost per line of approximately [Begin Confidential] $42 [End Confidential]. Thus the $18 residential rate cap benchmark is not enough to recover all of these costs. Therefore, other revenue sources are necessary to fully recover the cost of providing residential basic local services for customers in Pennsylvania. Tinkering in a non-holistic fashion that fails to recognize this fact will be harmful to universal service as discussed by Mr. Jeffrey Lindsey. Historically, this Commission has recognized the appropriateness of "synchronized" rates and that TSLRIC/TELRIC studies are the appropriate methodology for understanding the costs.

Q. Does this conclude your Rebuttal Testimony?

A. Yes.

Q. CAN YOU PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY?

A. Yes. Dr. Loube's own cost study results show that Embarq PA has an overall estimated average monthly cost per line of approximately **[Begin Confidential]** [redacted] **[End Confidential].** Thus the $18 residential rate cap benchmark is not enough to recover all of these costs. Therefore, other revenue sources are necessary to fully recover the cost of providing residential basic local services for customers in Pennsylvania. Tinkering in a non-holistic fashion that fails to recognize this fact will be harmful to universal service as discussed by Mr. Jeffrey Lindsey. Historically, this Commission has recognized the appropriateness of "synchronized" rates and that TSLRIC/TELRIC studies are the appropriate methodology for understanding the costs.

Q. Does this conclude your Rebuttal Testimony?

A. Yes.