



Rebecca B. DeCook
Senior Attorney

Room 1575
1875 Lawrence Street
Denver, CO 80202
303 298-6357

August 29, 2002

Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65101

Re: Case No. TR-2001-65

Dear Judge Roberts:

Attached for filing with the Commission is the original and eight (8) copies of AT&T Communications of the Southwest, Inc.'s Surrebuttal Testimony of R. Matthew Kohly and Michael J. Pauls in the above-referenced docket.

I thank you in advance for your cooperation in bringing this to the attention of the Commission.

Very truly yours,

A handwritten signature in cursive script that reads "Rebecca B. DeCook (je)".

Rebecca B. DeCook

Attachment

cc: All Parties of Record

Exhibit No.:
Issue: Telephone Specific – Other
Telephone Specific Issues
Witness: R. Matthew Kohly
Sponsoring Party: AT&T Communications of
the Southwest, Inc
Type of Exhibit: Surrebuttal Testimony
Case Nos.: TR-2001-65

AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.,

SURREBUTTAL TESTIMONY

OF

R. MATTHEW KOHLY

CASE NO. TR-2001-65

Jefferson City, MO
August 29, 2002

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of an Investigation of the Actual Costs)
Incurred in Providing Exchange Access Service and)
the Access Rates to be Charged by Competitive Local) Case No. TR-2001-65
Exchange Telecommunications Companies in the)
State of Missouri)

AFFIDAVIT OF R. MATTHEW KOHLY

STATE OF MISSOURI)

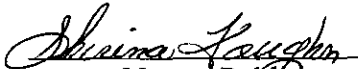
COUNTY OF COLE)

I, R. Matthew Kohly, of lawful age, being first duly sworn deposes and states:

1. My name is R. Matthew Kohly. I am the District Manager for AT&T Communications of the Southwest, Inc. in its Law and Government Affairs organization.
2. Attached hereto and made a part hereof for all purposes is my Surrebuttal Testimony.
3. I hereby swear and affirm that my answers contained in the attached document to the questions therein propounded are true and correct to the best of my knowledge and belief.


R. Matthew Kohly

Subscribed and sworn to this 29th Day of August, 2002


Notary Public

My Commission Expires: June 24, 2005

SHIRENA FAUGHN
Notary Public - Notary Seal
STATE OF MISSOURI
County of Moniteau
My Commission Expires June 24, 2005

**BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI
SURREBUTTAL TESTIMONY OF
R. MATTHEW KOHLY
TR-2001-65**

1 **Q. PLEASE STATE YOUR NAME AND ADDRESS.**

2 **A. My name is R. Matthew Kohly. My business address is 101 West McCarty Street,**
3 Jefferson City, Missouri 65101.

4 **Q. HOW ARE YOU EMPLOYED?**

5 **A. I am employed by AT&T in its Law and Government Affairs organization as District**
6 Manager -- Government Affairs. In this position I am responsible for the development
7 and implementation of AT&T's regulatory activities in Missouri.

8 **Q. ARE YOU THE SAME R. MATTHEW KOHLY THAT HAS FILED DIRECT**
9 **AND REBUTTAL TESTIMONY IN THIS CASE?**

10 **A. Yes. I am.**

11 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY IN THIS**
12 **CASE?**

13 **A. The purpose of my surrebuttal testimony is to address the issues raised in rebuttal**
14 testimony concerning the appropriate cost to be used in determining the cost of switched
15 access service in Missouri and the appropriateness of allocating loop costs to switched
16 access service. In response, I explain why the Commission should adopt a Total Service
17 Long Run Incremental Cost (TSLRIC) standard, consistent with the FCC's pricing rules
18 and explain why allocating the cost of the loop to switched access service based upon
19 accounting rules is contrary to incremental cost principles and is neither appropriate nor
20 practical. I also respond to rebuttal testimony regarding the CLEC access rate cap and
21 propose the existing cap be maintained with three exceptions. Those exceptions would

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1 permit a company to increase its rates above the cap if it demonstrates that higher rates
2 are justified, based upon a showing of higher costs or if the ILEC access rates are
3 reduced and the revenues loss is offset via universal service funding, surcharges or rate
4 increases and the CLEC does not have a similar revenue opportunity. The final
5 exception would be to permit CLECs to charge reciprocal terminating access rates.
6 Finally, I respond to the continued disagreement about the purpose of this case and
7 explain why access rates need to be addressed and make a specific proposal for reducing
8 access rates to TSLRIC levels.

9
10 **PURPOSE OF THIS PROCEEDING**

11 **IN REBUTTAL TESTIMONY, PARTIES ARE STILL CONTENDING THAT THE**
12 **PURPOSE OF THIS CASE IS TO ADDRESS CLEC ACCESS RATES. DO YOU HAVE**
13 **A RESPONSE?**

14 The issues surrounding the purpose and scope of this case have been debated through out the
15 entirety of this docket. This issue should have been resolved long ago so that testimony, much
16 less surrebuttal testimony, in this case did not have to address the most fundamental question of
17 why we are here. However, the rebuttal testimony of SWBT's witness Craig Unruh and Sprint's
18 witness Mark Harper illustrates that parties are still insisting this case was created only to
19 address CLEC access rates. For example, Mr. Unruh testifies that the "purpose of this case was
20 to determine a long-term solution for determining maximum rates for switched access service by
21 a CLEC." (Unruh, Rebuttal, pg. 2) Mr. Unruh makes this statement even though he previously
22 testified that this case was an "access reform case" and was an appropriate vehicle for examining
23 ILEC switched access rates¹.

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1 Not surprisingly, AT&T agrees with Mr. Unruh's earlier testimony that this is a broader access
2 reform case, rather than one focused only on CLECs. This conclusion is supported by the
3 Request For Proposal issued by the Staff in this proceeding, and the work actually performed by
4 the consultant hired by Staff. Also, the Commission must ask itself why it should focus on
5 CLEC access charges, as the incumbents suggest, when the real problem is with the incumbent
6 LEC's access charges as the comparison of Missouri access rates provided herein demonstrates.
7 It is not surprising that the incumbent LECs seek to divert the Commission's attention to CLEC
8 in an effort to maintain these excess access charges.
9 The incumbent LECs generally point to the fact that this case was created as a result of TO-99-
10 596, *In the Matter of the Access Rates to be Charged by Competitive Local Exchange Companies*
11 *in the State of Missouri* to support their claim that this case is limited to CLEC access charges.
12 Actively participating in that case were Southwestern Bell Telephone (SWBT), GTE Midwest,
13 Inc. (now Verizon Midwest, Inc), Sprint Missouri Inc, the Mid-Missouri Group (now known as
14 Mid-Missouri Independent Telephone Group), as well as the CLEC affiliates of incumbent local
15 exchange carriers ALLTEL Missouri, Inc, Green Hill Telephone Corporation, and Mark Twain
16 Communications Company.² While it may have originally been about CLEC access rates, the
17 ILECs were certainly active in that proceeding.

18 In TO-99-596, there was much discussion about access rates in general; including ILEC
19 access rates as is clearly shown in the Report and Order for that case.³ Some of the issues
20 discussed in that proceeding included attempts to justify historic ILEC access rates⁴, comments
21 that an ILEC would be unfairly required to incur rate case expenses if it attempted to modify its

¹ Case No. TO-98-329, Testimony of Craig Unruh, Trans. p. 3672

² At that time, GTE Midwest, Inc. included the exchanges now served by Verizon Midwest, Inc. (soon to be transferred to CenturyTel Missouri, Inc.) and Spectra Communications Group, Inc d/b/a CenturyTel.

³ Case No. TO-99-596, Report and Order, pg. 16, 19, and 23

⁴ TO-99-596, Reply Brief of Sprint Missouri, Inc. and Sprint Communications Company, L.P. pg. 4.

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1 access rates⁵ and even concerns expressed that an ILEC may be required to cost justify its access
2 rates.⁶

3 More importantly, it is also clear that the Commission established "to examine all of the
4 issues affecting exchange service and to establish a long-term solution which will result in just
5 and reasonable rates for exchange access service."⁷ Approximately six weeks after establishing
6 this case, the Commission issued a press release with a similar proclamation and further noted,
7 "[f]or smaller local exchange companies, a majority of its revenue comes from switched access
8 rates."⁸ All of these factors support the conclusion that the immediate case was about both ILEC
9 and CLEC costs and rates.

10 Arguably, the impetus of this case was based upon the Commission's conclusion in Case
11 No. TO-99-596 that "the public interest would best be served by reductions in exchange access
12 rates rather than by increases."⁹ Given that the Commission found that requiring CLECs to
13 charge a rate less than the competing ILEC constituted a barrier to entry; it is completely illogical
14 to assert the Commission was going to serve the public interest of reducing access rates by
15 erecting a barrier to entry. The only logical conclusion that can be drawn is that this case was
16 intended to address the cost and rates of both ILECs and CLECs.

17 **ISSUE I - APPROPRIATE COST STANDARD FOR SWITCHED ACCESS**

**IN REBUTTAL TESTIMONY, PARTIES DEBATE THE MEANING OF THE PHRASE
ACTUAL COSTS WITH RESPECT TO HISTORIC (BACKWARD LOOKING) OR FORWARD
LOOKING COSTS. DO YOU HAVE A RESPONSE?**

21
22 Yes. With respect to the issue of historic vs. forward-looking, I agree with Dr. Johnson
23 and others that the term "actual cost" does not mean historic embedded costs, as some parties

⁵ TO-99-596, Reply Brief of Alltel Communications Group, Inc., Green Hills Telecommunications Services, and Mark Twain Communications Company, pg. 10.

⁶ TO-99-596, Reply Brief of Alltel Communications Group, Inc., Green Hills Telecommunications Services, and Mark Twain Communications Company, pg. 6.

⁷ Case No. TO-99-596, Report and Order, p. 28.

⁸ Missouri Public Service Commission Press Release, PSC establishes case to examine access charges in Missouri, Issued September 28, 2000.

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1 advocate. In rebuttal testimony, Dr. Johnson cited a decision from the United States Supreme
2 Court that addressed this very issue and concluded that the term "cost" can mean forward-
3 looking (Johnson, Rebuttal, pg. 6). The addition of the adjective "actual" does not change this.
4 In a competitive market where businesses make decisions based upon cost, the only relevant
5 actual costs are forward-looking costs as this represents the "actual" costs the firm will pay if it
6 makes the purchase or sell decision. Just ask the consultants advocating the use of historic costs
7 what the actual cost of retaining their services for a future project will be. Most likely, they will
8 not respond by telling you their billable rate from two years ago.

9 SWBT's Witness Mr. Barch testifies that the Commission should calculate switched
10 access costs based upon the Long Run Incremental Cost ("LRIC") because this "is the
11 appropriate basis on which pricing decisions can be made." (Barch, Rebuttal, pg. 18). I agree
12 and specifically recommend that the Commission adopt the Total Service Long Run Incremental
13 Cost ("TSLRIC") standard consistent with the FCC's pricing rules. As the TSLRIC standard
14 includes an allocation of common costs, I believe this should also be the basis for setting
15 switched access prices.

16 **HAS STAFF TAKEN A POSITION ON THE APPROPRIATE COST METHODOLOGY**
17 **FOR ACCESS SERVICES?**
18

19 Staff has not made any recommendations in this docket. However, in Case No. TO-
20 2001-467, Staff's Witness William Voight testified that the "incremental costing methodology is
21 the most appropriate costing methodology to base costs in a competitive environment"¹⁰.

22 **WHY DO YOU RECOMMEND THAT COST OF ACCESS SHOULD BE CALCULATED**
23 **AND ACCESS RATES BE PRICED AT TSLRIC?**

24 I agree with the testimony filed by Sprint witness Farrar that 1) TSLRIC is the
25 appropriate cost standard to be used in this proceeding; 2) TSLRIC is the only standard that is

⁹ Case No TO-99-596, Report and Order, p. 28.

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1 consistent with the FCC's forward looking economic cost standard developed to comply with the
2 requirements of the Act; 3) TSLRIC complies with the cost standard required by Missouri law;
3 and 4) TSLRIC is the cost standard that is almost universally employed by other state
4 commissions in determining network costing issues
5 TSLRIC recognizes the principal of cost-causation and serves as the appropriate and efficient
6 basis for making pricing decisions. The use of TSLRIC best simulates the conditions in a
7 competitive marketplace and will encourage efficient levels of entry and investment.

8 In addition, pricing access at TSLRIC is necessary to prevent companies that provide
9 both switched access services and interexchange services from leveraging its monopoly in
10 switched access and the above cost-based access rates to engage in discriminatory pricing against
11 unaffiliated inter-exchange carriers in what is commonly referred to as a 'price squeeze'. To the
12 extent that access charges exceed forward looking economic costs, the combined switched
13 access/toll provider faces a lower cost of providing long distance services than competitors who
14 must pay the entirety of the access rates priced above economic costs. The FCC recognized this
15 competitive advantage when it adopted the CALLS Order, which reduced interstate access
16 charges into the range of estimated economic cost. In that Order, the FCC concluded the
17 following:

18 The reduction in switched access usage charges will promote competition in the
19 long distance market between BOC affiliates entering the market and IXC's. To
20 the extent switched access usage charges paid by IXC's are significantly above
21 cost, BOC affiliates would have a competitive advantage because they would
22 obtain switching services from the BOCs at cost.... the CALLS proposal will
23 minimize the competitive advantage BOC affiliates would have over IXC's in
24 offering long-distance services while the switched access rates were significantly
25 above cost." (CALLS Order at para. 158.)
26
27

28 The CALLS Order, of course, did not address the problem of intrastate access charges so the
29 concerns still remain with respect to intrastate access rates.

¹⁰ Case No. TO-2001-467, Cross-Examination of William L. Voight, Transcript, pg. 732.

1 **SOME PARTIES HAVE ARGUED THAT MONOPOLY SWITCHED ACCESS**
2 **PROVIDERS HAVE NO INCENTIVE TO DISCRIMINATE AGAINST LONG**
3 **DISTANCE COMPETITORS BECAUSE THEY WOULD LOSE THE PROFIT THEY**
4 **ARE MAKING ON ACCESS AS A RESULT. DO YOU AGREE?**
5

6 No. This argument basically assumes that the combined entity will seek to maximize the profit
7 of the switched access provider and the interexchange provider independently, rather than
8 maximize the profit of the combined entity. This assumption is overly simplistic and is belied by
9 the realities of the market.

10 A monopolist or integrated access/toll provider that is permitted to charge above cost
11 access rates has the incentive and ability to engage in discriminatory pricing in the more
12 competitive toll market, while requiring customers to purchase additional, less competitive,
13 higher margin local services. This essentially shifts revenues from a more competitive market to
14 a less competitive, more secure market. Additionally, the joint switched access/local exchange
15 provider will have the incentive to offer volume discounts or other discount plans that
16 competitors cannot match without incurring a financial loss. This will generate additional toll
17 revenues because of the stimulation in minutes. If the IXC competitor tries to match these offers
18 in the short-run, that will further stimulate access minutes and provide additional increases in
19 access revenues.

20 In addition, if the monopolist believes it will lose both the customer's local service,
21 especially from high-revenue local customers, and the toll business, the monopolist is better off
22 retaining the local customer even if it prices toll below the imputed cost of access. By retaining
23 the customer, it still receives the local revenues as well as earns an economic profit by providing
24 toll services at rates that exceed the underlying economic cost. Meanwhile, an unaffiliated IXC
25 will have to incur a financial loss to match the other company's rate. In similar fashion, the
26 above cost access rates create the ability and incentive to engage in discriminatory pricing in one
27 market to protect a monopoly in another market. In this instance, the integrated provider would

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1 use the above cost-based switched access rates to engage in discriminatory pricing in the
2 interexchange market in order to protect its monopoly in the local exchange market. This is
3 similar to the strategy employed by Microsoft in which it attempted to monopolize the Internet
4 browser market to protect its monopoly in the operating system market.

5 Consider the reality of the market. In order for residential customers located in SWBT
6 territory to be eligible for the SBC LD's Domestic Saver Gold, which offers an intrastate rate of
7 7 cents per minute, the customer must also purchase Simple Solutions from SWBT, which ranges
8 in price from \$39.95 to \$89.95 depending upon the options. The minimum option requires the
9 customer to subscribe to a bundle of eight high margin vertical features as well as unregulated
10 services such as voice mail (**CallNotes® Plus**), **inside wiring (InLine®)**, and even hand set
11 protection (**Phone-ProtectSM**). If the customer does not wish to purchase these extraneous
12 services from SWBT, the customer must pay SBC LD \$1.95 more per month to get the same rate.
13 On the business side, a customer may enroll in the Business Long Distance Total Solutions Plus
14 plan that provides interstate calling for 7 cents a minute and intrastate calling for 10 cents a
15 minute with no monthly fee levied by SBC LD. However, to be eligible, SBC LD's customer
16 must also purchase Access Advantage Plus or On-Line Office, Plexar I, Plexar II, or Complete
17 Link Basic from SWBT. If the customer does not want to purchase all of these extraneous
18 services from SWBT, the customer will pay 12 cents a minute.

19 As is readily apparent, any supposed lost opportunity cost from pricing below the
20 imputed cost of access is readily recovered through the sale of high margin local and unregulated
21 services which also requires the customer to continue to be a basic local customer of the
22 integrated access/toll provider. The difference between the access rate and TSLRIC provides
23 the integrated switched access/interexchange carrier with a revenue cushion to engage in
24 discriminatory pricing without ever incurring a financial loss while an IXC competitor would

1 incur a financial loss if it tried to match the lower interexchange toll rates. Pricing access rates at
2 TSLRIC eliminates this advantage.

3 **HAVE ANY PARTICIPANTS TO THIS PROCEEDING AGREED THAT ACCESS**
4 **RATES PRICED ABOVE COST CREATES THE INCENTIVE AND ABILITY FOR A**
5 **PROVIDER OF BOTH SWITCHED ACCESS AND INTEREXCHANGE SERVICE TO**
6 **ENGAGE IN DISCRIMINATORY PRICING?**

7 Yes. In a prior proceeding in Missouri, David E. Stahly appearing on behalf of Sprint
8 Communications, L.P. testified that when SWBT is both a switched access provider and an
9 interexchange carrier through its long distance affiliate, the intra-company switched access
10 payment between the long distance affiliate and the local access provider is merely a paper
11 transaction and does not represent the real economic cost upon which pricing decisions are
12 made¹¹. According to his testimony, the difference between TSLRIC and the access rates is what
13 provides the incentive and ability to engage in discriminatory pricing. While his testimony
14 focused on SWBT, the same advantage applies on the intrastate side within each ILEC's
15 franchise territory.

16 **DOES AT&T HAVE ANY TSLRIC ESTIMATES OF THE COST OF SWITCHED**
17 **ACCESS IN MISSOURI?**
18

19 As a result of protective order limitations, AT&T has not been able to review the
20 incremental cost studies produced by Staff's consultant or those produced by individual carriers.
21 However, there are public TSLRIC surrogates that are readily available that serve as a useful cost
22 proxy. The incremental cost of terminating local and interexchange traffic involves the same
23 network functions and, therefore, has the same costs. As the FCC stated:

24 We recognize that transport and termination of traffic, whether it originates
25 locally or from a distant exchange, involves the same network functions.

¹¹ Case No. TO-99-227, Application of Southwestern Bell Telephone Company to Provide Notice of Intent to File an Application for Authorization to Provide In-Region InterLATA Services Originating in Missouri Pursuant to Section 271 of the Telecommunication Act of 1996, Direct Testimony of David E. Stahly, pgs 28 - 47, January 5, 1999.

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1 Ultimately, we believe that the rates that local carriers impose for the transport
2 and termination of local traffic and for the transport and termination of long
3 distance traffic should converge¹².
4

5 Because of this cost relationship, I am proposing that the Commission consider the
6 following reciprocal compensation rates as the set forth in Table MK-1 as a proper estimate of
7 the TSLRIC cost associated with the network facilities used in the provision of switched access
8 service

¹² CC Docket No. 96-98, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 First Report and Order, ¶ 1033.

1

Table MK-1 Comparison of Reciprocal Compensation Rates to Corresponding Switch Access Rates.				
Company	Rate Source	Local Compensation Rate per end	Intrastate and Interstate Access Rate	Comments
Verizon	Recip. Comp.	0.52¢	8.19¢ / 0.40¢	Recip. Comp. Rate set in Case No. TO-97-63, AT&T – GTE arbitration
SWBT	Recip. Comp.	0.56¢	2.97¢ / 0.31¢	Rate for SWBT's Rate Group A – exchanges 0 – 4,999 access lines, set in Case No. TO-97-40, AT&T/MCI – SWBT arbitration
Sprint	Recip. Comp.	1.32¢	9.47¢ / 0/082¢	Negotiated Rate contained in Sprint Master Interconnection and Resale Agreement, 3/31/2000
Spectra	Recip Comp.	1.79¢	9.70¢ / 3.1¢	Negotiated Rate – Footnote indicates rate based upon Spectra Cost Studies
Orchard Farm*	Wireless Termination	1.9655¢	9.48¢ / 3.8¢	Negotiated Rate
New London*	Wireless Termination	1.954¢	9.80¢ / 3.45¢	Negotiated Rate
Stoutland*	Wireless Termination	1.476¢	14.12¢ / 2.92¢	Negotiate Rate
<p>* - Wireless termination rates reflect the rates by CMRS providers paid for terminating a call. Therefore, the wireless termination rates are compared to the equivalent interLATA access rates for terminating a call.</p> <p>** - the access rates listed in this table are based upon those presented by Staff's Witness Dr. Ben Johnson in his direct testimony.</p>				

2

3 By way of background, the rates for SWBT and Verizon are arbitrated UNE rates established by
4 the Commission in 1997. Since the Commission set the arbitrated rates, SWBT has reduced
5 these rates by modifying the M2A. Also, SWBT's reciprocal compensation rates that are
6 presented are from Rate Zone A, which has the highest rates in SWBT's four rate zones. GTE
7 has gone through a number of sales and corporate changes since the time the PSC established the

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1 reciprocal compensation rates. The rural exchanges were purchased by Spectra, while the
2 remaining exchanges are now served by Verizon as a result of a merger. Because of the sale of
3 the more rural exchanges, the reciprocal compensation rates for the remaining Verizon exchanges
4 (soon to be transferred to CenturyTel) are likely overstated. The other rates are negotiated rates
5 that have not been reviewed by the Commission. Because these rates were agreed to by the
6 incumbent, it is unlikely that they are below cost. In fact, given the superior bargaining power of
7 the ILECs in interconnection negotiations, to the extent these rates differ from the true forward-
8 looking costs, these rates are likely *in excess* of the true costs and therefore, would serve as a
9 ceiling. Similarly, the wireless termination rates I have provided are also negotiated and would
10 most likely serve as a ceiling as well, for the same reason. In addition, the traffic from CMRS
11 providers is typically not balanced so that more traffic terminates to the LEC than the LEC
12 terminates to the CMRS provider. Given that imbalance, LECs would have an incentive to
13 overstate the true costs in order to experience a financial windfall. I am not trying to
14 unnecessarily create an argument over these rates but do want to put them into the proper
15 perspective.

16
17 **ISSUE II – DOES THE COMMISSION HAVE TO TREAT ALL LOCAL EXCHANGE**
18 **CARRIERS IN THE SAME MANNER OR USE THE SAME COST STANDARD FOR**
19 **ALL LOCAL EXCHANGE CARRIERS?**

20 No. As long as there is a rational and justifiable reason for differing treatment, the Commission
21 does not need to adopt a one-size fits all approach. The Missouri statutes have differing
22 requirements for small ILECs than for large ILECs, as well as differing requirements for ILECs
23 regulated under price cap regulation versus ILECs regulated under rate of return regulation. The
24 Federal Telecommunications Act of 1996 and the FCC's rules also have different requirements
25 for different companies.

ISSUE III - LOOP COSTS

As part of the disagreement about the appropriate cost standard for switched access service, there is a related disagreement about the treatment of loop costs. There are two issues in this category that the Commission should consider. The first is the allocation of the loop costs and the second is matching the loop cost recovery with the manner in which loop costs are incurred.

The first issue has been substantially addressed in the testimony so I will only briefly address this issue. Ms. Meisenheimer contends that the loop should be treated as a common cost because multiple services can make use of it (Meisenheimer Rebuttal, pp. 11-13.). Dr. Johnson and witnesses appearing on behalf of the rate of return ILECs generally support this conclusion as well. The joint use of an input or a product does not mean that input is a joint cost (Rebuttal, Dr. Shaihr, pg. 18). Common costs are those costs that cannot be unequivocally associated to any one service. A customer cannot purchase basic local service without the full use of local loop. Without basic local service, a customer cannot receive the benefit of E-911, purchase vertical or other ancillary services or have the ability to place or receive toll calls. Therefore, loop costs are incurred as a direct result of the decision to purchase basic local service and do not represent a common cost. Sprint's Witness Dr. Staihr's comparison to televisions and personal computers highlights the flaw in this logic (Staihr Rebuttal, pg. 18, pg. 20).

As another example, consider the market for compact disc players and compact discs (CD). If a customer wants to listen to a particular CD, she has to buy "access" to a CD player. Since the CD player is necessary for the usage of the CD, should the price of the CD include an allocation of the costs involved in manufacturing the CD player? Of course it should not, and in reality it does not. Such cost allocation, and therefore the

1 resulting price, is inefficient and not found in competitive market settings. In line with
2 efficiency requirements, CD prices are independent of the costs associated with the
3 manufacturing of CD players.

4 In summary, the costs of the local loop are directly caused by the
5 provision of subscriber access, not the many services carried over the network.

6
7 **DOES ALLOCATING THE LOOP ACROSS MULTIPLE SERVICES CREATE**
8 **COMPETITIVE IMPACTS AS WELL?**

9 Yes. Section 392.455 RSMo. 2000 of the Missouri statutes require CLECs to provide basic local
10 service as a separate and distinct service. In complying with this statutory requirement, CLECs
11 incur the full loop costs and yet are forced to offer basic local service at rates that do not reflect
12 their costs because the prevailing market price of basic local service reflects the fact that residual
13 recovery of cost attributable to local service has been allocated to other services which the CLEC
14 may or may not provide or that customer may or may not subscribe to.

15
16 **FROM A PRACTICAL STANDPOINT, CAN LOOP COSTS BE ALLOCATED IN A**
17 **NON-DISCRIMINATORY MANNER?**

18 No. If one were to agree that allocating the cost of the local loop across all services is
19 appropriate (which I do not), there is simply no practical and non-discriminatory method to allocate
20 the cost of the loop facility to all of the individual services that use the loop in a non-discriminatory
21 manner. Ms. Meisenheimer acknowledges that any such allocation is "primarily a matter of
22 judgement and discretion". (Meisenheimer, Rebuttal, pg. 9) Similarly, Dr. Johnson
23 acknowledges that allocation procedures necessarily involve a degree of arbitrariness. This task
24 is made incredibly complex by "the ever increasing variety of services" that use of the loop. Add
25 into this mix, the differing service providers such as CLECs that most likely have a unique

1 customer base and unique service offerings and it is simply not possible. In recognition of this
2 impossibility, Staff Witness Mr. William L. Voight testified in another proceeding that the
3 inability to accurately spread the loop across all services was one of the "fatal flaws of the fully
4 allocated method."¹³

5 **HOW ARE THE PROPONENTS OF LOOP ALLOCATION PROPOSING TO**
6 **ALLOCATE LOOP COSTS IN THIS PROCEEDING?**

7 The loop allocation methods proposed in this case arbitrarily select two services to bear the
8 cost of the local loop; basic local service (measured in terms of local minutes) and switched access
9 service, (also measured in terms of minutes) and then allocate the costs between the two services
10 based upon differing accounting rules. While this may have been done in the past, the
11 telecommunications market has changed and this arbitrary selection method is discriminatory, is
12 inappropriate and can no longer be sustained.

13 Supporters of the theory that the loop is a common cost because of common use must
14 recognize that many services beyond local minutes and landline interexchange minutes rely upon
15 the loop and non-traffic sensitive switching elements. In Missouri, basic local service includes E-
16 911, which whether used or not provides a benefit to the end-user. Basic local service also includes
17 the ability to place and to receive calls which has a value whether used or not. Vertical features
18 such as CallerID, Call Waiting, Auto Call Return among others generate significant revenues for
19 local exchange companies and just like E-911, these services are only made possible by the use of
20 the loop. Many local exchange carriers also provide voice-mail service either directly or through
21 an unregulated affiliate. Each of these services jointly uses the loop. If the Commission is going
22 to engage in allocating the cost of the loop, it must do so across all services in a non-discriminatory
23 manner. Even if it somehow possible to arrive at a non-discriminatory allocation mechanism at a

¹³ Id. pg. 778.

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1 point in time, that mechanism would require constant tinkering as usage changed and new services
2 were introduced.

3 Consider the recent example of xDSL that relies upon the High Frequency Portion of the
4 Loop (HFPL) when provisioned via line-sharing or line-splitting. This service provides
5 dedicated access without interfering with the production of minutes or other services on the low
6 frequency portion of the loop. Under the allocation mechanisms proposed in this case, the entire
7 cost of the loop would be spread across local minutes and interexchange minutes while a service
8 such xDSL which provides 24 hour, 7 day a week dedicated service (which may include the
9 ability to make and to receive packet-switched interexchange voice messages) contributes
10 nothing to the local loop costs under the proposed allocation mechanisms.

11 In the most recent Northeast Missouri Rural Telephone Cooperative ("NEMO") rate
12 case, the loop investment that led to the increase in intrastate-switched access rates also enabled
13 NEMO to provide xDSL service. In fact, NEMO's witness Gary Godfrey testified that the entire
14 purpose of that investment was to provide voice, data and whatever telecommunications services
15 its members wanted¹⁴. However, under the loop allocation methods proposed in this case, that
16 investment would be recovered from two services with the costs allocated by accounting rules
17 based primarily upon minutes. This practice would be unsustainable and would seriously distort
18 the telecommunications market and the development of competition in the market.

19
20 **YOU IDENTIFIED THE SECOND ISSUE REGARDING THE RECOVERY OF LOOP**
21 **COSTS IN THE MANNER THEY ARE INCURRED. CAN YOU ELABORATE ON**
22 **THAT?**

¹⁴ Case No. TR-2001-344, In the Matter of Northeast Missouri Rural Telephone Company's Rate Case in Compliance With the Commission's Orders in Case Nos. TO-99-530 and TO-99-254. Cross-Examination of Gary Godfrey, Tr. p. 75

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1 Yes. The second issue to be considered is the recovery of loop costs in the manner in
2 which those costs are incurred. Loop costs as well as portions of the switching costs are non-
3 traffic sensitive or non-service specific. However, the portion of these non-traffic sensitive costs
4 that has been historically subsidized by access service are recovered, via the traffic sensitive rate
5 elements known as the Carrier of Common Line (CCL). While this rate element is an implicit
6 subsidy that the Act requires be made explicit and funded via a universal service fund, to the
7 extent this rate element is retained, economic efficiency dictates that those costs should be
8 recovered in the same manner. The current mechanism of using a traffic sensitive CCL element
9 is discriminatory and inefficient. By recovering the cost of this facility in usage rates, such as the
10 Carrier Common Line, some high volume customers will pay far more than the cost to serve them --
11 in effect, providing an added "subsidy" through higher rates. Meanwhile low volume users will
12 pay less than the cost to serve them. It needs to be recognized that, regardless of how the loop
13 costs are allocated, in the long run customers in total will pay rates that will recover those costs.
14 Any allocation methodology is really just an exercise in determining which retail customers will
15 pay more or less for the dedicated access line into their home or business. An allocation
16 mechanism based upon minutes will create a subsidy regardless of the customer's ability to pay
17 and represents an economically inefficient subsidy mechanism. This is not an efficient subsidy
18 mechanism as it is not means-tested and is in direct conflict with the purpose of the Life-Line
19 program which is designed to create an explicit subsidy targeted to those that need it, which is a
20 much more economically efficient subsidy mechanism.

21 The FCC addressed the CCL in its recent "MAG Plan Order,"¹⁵ and found that the
22 interstate CCL is "an inefficient cost recovery mechanism and implicit subsidy" and should be
23 phased out of the common line rate structure. (MAG Plan Order at paragraphs 40-41, 61-68.)

¹⁵ "Second Report And Order And Further Notice Or Proposed Rulemaking, etc.," In the matter of the Multi-Association Group (MAG) Plan, etc., CC Docket Nos. 00-256, 96-46, 98-77, and 98-166, issued November 8, 2001.

1 From a competitive standpoint, the Commission must also realize that interexchange
2 carriers increasingly compete against wireless carriers. Interexchange carriers incur higher
3 intrastate call termination expense as FCC rules mandate that wireless carriers pay traffic
4 termination charges that are based upon TELRIC costs and cannot include any rate element
5 designed to recover non-traffic sensitive costs for IntraMTA calls. IXC's such as AT&T compete
6 on the same toll routes as wireless carriers and even though the calls may even utilize the exact
7 same facilities for termination, IXC's incur higher termination rates. In this sense, the current
8 access mechanism is discriminatory and favors one type of service provider for no justifiable
9 reason. This is contrary to the mandates of the Act.

10 **IN THE STATE OF KANSAS, THE KCC RECENTLY ADDRESSED MANY OF THESE**
11 **SAME ISSUES. CAN YOU PLEASE ELABORATE ON THEIR CONCLUSION ON**
12 **THESE ISSUES?**

13 Yes. The Kansas Corporation Commission (the "KCC") recently adopted a stipulation and
14 agreement that significantly restructured SWBT and Sprint's switched access rates and moved the
15 non-traffic sensitive costs into the local rates. In doing so, the KCC found that "the issue is not so
16 much about how costs are allocated among services, but how the costs are recovered – whether on a
17 fixed or variable basis". In support of that conclusion the KCC stated:

18 The cost of the local loop is essentially fixed, that is, it does not vary based on
19 the volume of usage or whether the usage is local or long distance. Each
20 customer has the same basic capabilities and opportunities for use of the loop
21 once the customer is connected. The rate structure for telephone services (as it
22 has happened historically) generally includes a flat rate for unlimited local
23 calling, and access rate based on minutes of usage, which is paid the customer's
24 IXC to the LEC, and passed through to the consumer in the IXC's rates for toll
25 and long distance services. Under this structure, to the extent that access rates
26 includes the cost of the loop and is charged based on minutes of use, a consumer
27 that is a heavy user of toll and long distance services pays more to support the
28 loop costs than a customer who uses his phone only to make local calls¹⁶.
29

¹⁶ Kansas Corporation Commission, In the Matter of a General Investigation into the Reformation of Intrastate Access Charges, Docket No. 01-GIMT-082-GIT, September 25, 2001, page 12.

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1 The KCC further found:

2 These basic facts show the inefficiency, as well as the unfairness, of a
3 usage sensitive recovery mechanism when "the loop would be necessary even if
4 no long distance calls were made or if the customer only received calls."
5 [citation omitted] Thus it is reasonable and appropriate that those costs be
6 recovered through a flat rate charge to the end-user.¹⁷
7

8 In recognition of the need to structure cost recovery in an efficient manner consistent with the
9 manner in which costs are incurred, the KCC found that:

10 The recovery mechanism becomes all the more important as the
11 Commission attempts to implement the legislative mandate to transition to a
12 more competitive environment. Consumer may bypass the wireline network and
13 make their toll calls using wireless or voice over internet services. Providers of
14 these services do not pay access charges so they can offer services at lower costs.
15 Since the providers do not pay access charges, implicit subsidies are not
16 sustainable because LECs will recover ever-decreasing amounts¹⁸.
17

18 While Ms. Meisenheimer opined that states like Kansas that are reforming access rates are
19 blindly following the FCC in lemming-like fashion, it is clear that Kansas reasoned its decision
20 based upon sound economic rational.

21 Regardless of the cost standard adopted by the Commission, the Commission should move
22 immediately to restructure access rates to eliminate the CCL element. Where it is necessary to
23 provide revenue neutrality, the CCL elements should be restructured into a flat-monthly charge
24 to reflect the manner in which costs are incurred.

25

26 **ISSUE V. IS THE CURRENT CAPPING MECHANISM FOR INTRASTATE CLEC**
27 **ACCESS RATES APPROPRIATE AND IN THE PUBLIC INTEREST?**
28

29 **Q. THE REBUTTAL TESTIMONY INDICATES THERE SEEMS TO BE GENERAL**
30 **CONSENSUS ABOUT RETAINING THE ACCESS CAP ON CLEC ACCESS RATES.**
31 **DOES AT&T AGREE WITH THAT?**

¹⁷ Ibid. p. 13

¹⁸ Ibid.

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1 AT&T does agree that the unique nature of switched access creates a locational monopoly and
2 necessitates retaining a cap on the access rates charged by CLECs. That cap should be equal to
3 maximum access rate that can be charged by the ILEC in whose territory the CLEC is competing.
4 In a competitive market, competitors should be permitted the same revenue opportunity and be
5 permitted to charge a rate equal to the prevailing market price, which is the incumbent's switched
6 access rates.

7 **ISSUE VI - ARE THERE CIRCUMSTANCES WHERE A CLEC SHOULD NOT BE**
8 **BOUND BY THE CAP ON SWITCHED ACCESS RATES?**
9

10 **Q. ARE THERE INSTANCES WHERE A CLEC SHOULD BE ALLOWED TO**
11 **CHARGE A RATE HIGHER THAN ALLOWED UNDER THE ACCESS RATE CAP?**
12

13 A. Yes. MITG witness Kent Larsen and Sprint witness Harper have testified in rebuttal
14 regarding certain exceptions to the application of the cap. (Larsen Rebuttal, p. 21-22; Harper
15 Rebuttal, pp 6-7). While I don't necessarily disagree with these exceptions, I believe there are at
16 least three exceptions where CLECs should be permitted to deviate from the cap on switched
17 access. The first exception is for a CLEC that files an appropriate TSLRIC cost study that
18 demonstrates its costs of providing switched access are higher than the rates allowed under the
19 cap. This is consistent with Mr. Harper's proposal although I propose the cost standard necessary
20 to justify higher rates be TSLRIC while Mr. Harper does not propose a definite cost standard. If
21 the CLEC can cost justify the higher rates, it should be permitted to charge a cost-based access
22 rate even it is if higher than the rate charged by the ILEC.

23 The second exception is the situation that may occur when an ILEC reduces access rates
24 and receives offsetting receipts from the Missouri Universal Service Fund or offsetting revenues
25 from some other mechanism that is not available to the CLECs. In this instance, the CLEC
26 would most likely not be able to receive Universal Service Fund receipts to offset its access
27 reductions because of the statutory requirement to be a Carrier of Last Resort in order to received

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1 MO USF High Cost funds. The ILECs rates would be reduced with revenue neutral offsets while
2 a CLEC may be denied the same revenue opportunity as its competitor. This is not reasonable
3 and would create the same direct and undeniable competitive advantage as permitting the ILEC
4 to charge higher access rates than its competitors. However, I would agree that this exemption
5 should not apply in a situation where the ILECs is not permitted to offset its access rate
6 reductions via a revenue neutral offset, such as in a typical rate case, or when a CLEC is a
7 Carrier of Last Resort and is able to receive USF receipts.

8 The third exception is to permit a CLEC, at its discretion, to charge reciprocal
9 terminating access in the same manner as the compensation scheme that applies to the exchange
10 of local traffic. Under this mechanism, a CLEC may elect to assess reciprocal terminating
11 access rates for terminating interexchange traffic from other ILECs or CLECs and their
12 identifiable wholly-owned affiliates terminating interexchange traffic to the CLEC providing the
13 access services.

14 **WILL YOU PLEASE ELABORATE ON THIS THIRD EXCEPTION?**

15 This reciprocal mechanism is identical to the reciprocal compensation mechanism mandated by
16 the FCC for the exchange of local traffic. In the First Report and Order, the FCC concluded that
17 the costs an ILEC would incur in the termination and transport of local services would be similar
18 to those of a new entrant. As the costs were presumed to be similar, the FCC established a
19 presumption of symmetry in setting reciprocal compensation rates for the transport and
20 termination of local traffic. Specifically, the FCC directed state commissions to depart from the
21 presumption of symmetry only if the CLEC rebuts the presumption of symmetrical costs by
22 showing it incurs higher costs using a forward looking cost study. Because the transport and
23 termination of local traffic involve the same network functions as access traffic and cause the
24 provider to incur the same costs that are incurred in the provision of access services, the

1 presumption of symmetry between the costs incurred by new entrants and incumbents in the
2 provision of transport and termination of local traffic is equally applicable to access services.

3

4Q. **WHAT BENEFITS WOULD PERMITTING CLECS TO CHARGE SYMMETRICAL**
5 **ACCESS RATES PROVIDE?**

6

7A. Such a rate proposal would provide many competitive benefits. First, it promotes revenue
8 symmetry by permitting a CLEC to receive the same compensation that another carrier charges it
9 for providing the very same service. For example, under the current access rate cap, AT&T
10 operating as a CLEC in SWBT's exchanges is permitted to charge Sprint Missouri, Inc. a end-
11 office terminating access rate of 3.37¢ per minute for terminating calls. Meanwhile, Sprint
12 Missouri, Inc. is able to charge the CLEC a terminating access rate of 10.86¢ per minute.
13 Permitting Sprint or any company operating in that franchise territory to charge a rate that is over
14 3 times higher than the rate AT&T is permitted to charge for the exact same service is
15 unreasonable; especially when the rate is not cost-justified. As part of this proceeding, Sprint
16 filed TSLRIC switched access cost studies advocated by Sprint. While the current protective
17 order prohibits me from seeing the results of those studies, it is incomprehensible that those cost
18 studies will support Sprint's current terminating access rates. Based upon the comparison
19 provided in Table MK-1, I do not believe a credible TSLRIC standard would justify the
20 terminating access rates for many of the ILECs in Missouri.

21

22 **ARE THERE ADDITIONAL BENEFITS IN PERMITTING CLECS TO CHARGE**
23 **RECIPROCAL TERMINATING ACCESS RATES?**

24

25 Permitting CLECs to begin charging reciprocal access rates would provide an incentive for the
26 incumbents to reduce terminating access rates that does not exist today. In agreeing that
27 terminating switched access was a locational monopoly, Dr. Debra Aron testifying on behalf of
28 SWBT in TO-2001-467 acknowledged that creating competitive incentives to reduce terminating

1 access "would involve more institutional changes about how we bill calls to originating and
2 terminating customers."¹⁹ I believe that permitting CLECs to begin charging reciprocal
3 terminating access is the type of institutional change that has the potential to create the incentive
4 to reduce terminating access rates. As local competition develops, reciprocal access rates will
5 certainly create the incentive to reduce terminating access rates. Permitting reciprocal switched
6 access rates would provide necessary revenues to assist in offsetting the CLECs terminating
7 access expense.

8 While permitting CLECs to charge reciprocal access rates will not fix all of Missouri's
9 access rate issues, it should be an immediate component of an overall strategy to address a
10 widely recognized problem. In addition to direct benefits to CLECs, reciprocal terminating
11 access rates serves the broader public interest by creating a competitive incentive to produce
12 access rate reductions.

13 **ISSUE VII - WHAT, IF ANY, COURSE OF ACTION CAN OR SHOULD THE**
14 **COMMISSION TAKE WITH RESPECT TO SWITCHED ACCESS RATES AS A**
15 **RESULT OF THIS CASE?**
16

17 For the reasons previously stated, I believe this case was established to address access charges of
18 both ILEC and CLECs, with the goal of establishing a long-term solution that will result in just
19 and reasonable rates for exchange access service. I disagree with the rebuttal testimony of the
20 incumbent LECs that this case only involves the access charges of the CLECs and that the
21 Commission can and should do nothing to address the excessively high, non-cost-based access
22 charges of the incumbents. The Commission must develop an overall strategy to accomplish
23 what it set out to do at the start of this proceeding: establish a long-term solution that will result
24 in just and reasonable rates for exchange access service.

25 **WHY SHOULD THE COMMISSION ADDRESS BOTH ILEC AND CLEC ACCESS**
26 **RATES?**

¹⁹ Case No. TO-2000-467, , Cross-Examination of Dr. Debra Aron, Tr.

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1 First, the Commission has already found that the public interest is best served by lower
2 rather than higher switched access rates. If the public interest is served by lower access rates it
3 makes no sense to focus on CLECs and ignore the remaining 90+% of the switched access
4 market. If the Commission is going to affect any significant change, it needs to address ILEC
5 access rates as well.

6 Undeniably, Missouri's access rates are among the highest in the nation. Based upon
7 AT&T's own data, Missouri ranks fifth in the nation for the highest average switched access rates.
8 The only states exceeding Missouri in this category are North Dakota, South Dakota, New Mexico
9 and Alaska. These are some "big square states" that have lower population densities than
10 Missouri. AT&T's own data is consistent with the data presented in Dr. Johnson's Direct
11 Testimony. The access rates charged by SWBT in Missouri are higher than those charged in the
12 other four SWBT states or even those charged by its affiliate PacBell or Ameritech. Dr.
13 Johnson's shows the same results for Sprint and Verizon. Yet, Missouri is not one of the highest
14 cost states in the nation. Comparing the current access rates with the TSLRIC surrogates
15 presented in my testimony shows that for SWBT, Sprint and Verizon, Missouri access rates are
16 well above TSLRIC levels.

17 Undeniably, Missouri's access rates not only distort the interexchange market, but also
18 create disincentives to serve certain areas, create the ability as well as incentive and ability to
19 engage in discriminatory pricing and cause other adverse competitive consequences. While the
20 Commission is certainly accustomed to hearing complaints about high access rates from AT&T,
21 complaints about the adverse impacts of high access rates are popping up in other proceedings.
22 For example, recently in the recent on-the-record presentation in the ongoing MCA case, Mr.
23 England complained that high terminating access rates impacted his client's ability to offer
24 expanded calling into neighboring exchanges, especially into exchanges served by Sprint and

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1 Verizon²⁰. High terminating access rates were the reason cited by SWBT for eliminating the
2 Local Plus service. In Case No. TM-2002-465, SWBT's witness Jason Olson testified that high
3 terminating access rates might deter entry in exchanges that are next to ones with high access
4 rate-related business expense.²¹ I agree with that testimony and would add that high terminating
5 access rates in general deter local entry as they increase business expenses for new entrants.

6 Rather than address the issue of the underlying compensation, past efforts have focus on
7 band-aid approaches, such as expanded local calling where the underlying compensation is
8 switched access. These short-term fixes will not work. As the Commission has seen, the
9 willingness and ability to offer these services while incurring financial losses erodes in a
10 competitive market. In the same recent MCA presentation, Mr. Craig Johnson representing the
11 MITG addressed the practicality of offering expanded local calling in rural areas by concluding
12 "the solution or the answer lies in the inter-company compensation"²² and stated that the only
13 reason the MCA has survived is because the terminating mechanism compensation is bill-and-
14 keep. Mr. Johnson is correct - inter-company compensation must be fixed. Inter-company
15 compensation needs to be priced correctly so that a carrier's cost to terminate a call is not
16 dependent upon technology, the exchange boundaries, or the retail classification. If both access (for
17 "toll") and call termination (for "local") charges are the same, then carriers will be free to design
18 products with differing boundaries, with the goal to attract subscribers by offering a "better" local
19 calling area. Such an environment, however, requires non-discriminatory termination rates that do
20 not differentiate between types of calls or different types of carriers. Otherwise, all carriers will

²⁰ Case No. TO-2001-391, In the Matter of a Further Investigation of the Metropolitan Calling Area Service After the Passage and Implementation of the Telecommunication Act of 1996 On-the Record Presentation, Response of Mr. England to Questions from Commissioner Lumpe, pg. 148-149.

²¹ Case No. TM-2002-465, In the Matter of the Joint Application of Northeast Missouri Rural Telephone Company and Modern Telecommunications Company for Approval to Merge Modern Telecommunications Company and Northeast Missouri Rural Telephone Company, Direct Testimony of Jason Olson, pg. 4.

²² Case No. TO-2001-391, In the Matter of a Further Investigation of the Metropolitan Calling Area Service After the Passage and Implementation of the Telecommunication Act of 1996 On-the Record Presentation, Response of Craig Johnson to Questions from the Bench, Tr. p. 153.

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1 have their cost-structure defined by Missouri's existing exchange boundaries -- a lower cost to
2 terminate a "local" call, a higher cost to complete a "toll" call.

3 A far better outcome would be a market based on non-discriminatory, cost-based charges
4 for call termination, irrespective of the *label* on the call. With such non-discriminatory charges,
5 carriers, including incumbent local exchange carriers, would be free to decide the scope of their
6 own local calling areas, sizing these areas to match their own perception of the market and to reflect
7 their own pricing and marketing strategies. In this way, the market -- which is to say, *consumers* --
8 will decide the size and shape of the local calling area as carriers compete along this important
9 dimension of service.

Q10 IS THIS TYPE OF COMPETITION ONE OF THE GOALS OF THE FEDERAL ACT?

A11 Yes. I believe that the competitive end-point of the Act is a discrimination-free environment of
12 cost-based carrier charges that permits free and unfettered competition for every service at every
13 level (including calling boundaries). I am not alone in this opinion; this is also the endpoint
14 described by the United States Telephone Association, of which SBC is a member):

15 Ultimately, the 1996 Act contemplates a competitive endpoint where the pricing of
16 local interconnection is not dependent upon the identity of the interconnecting
17 entity, e.g. an IXC, a CAP, a CLEC, a CMRS provider or an information service
18 provider.²³
19

20 Similarly, this Commission should move to implement a comprehensive cost-based pricing system
21 that does not discriminate between types of calls or carriers. The long-run goal of this process
22 should be to price the traffic sensitive switched access rate elements at TSLRIC for all
23 companies. While this is a far-reaching goal, if it addressed in steps in concert with other
24 pending cases, such as the Missouri Universal Service Fund proceeding, it can be accomplished.

**25 CAN YOU DESCRIBE THE STEPS YOU BELIEVE THE COMMISSION SHOULD
26 TAKE TO ACCOMPLISH THIS GOAL?**

²³ USTA Comments, FCC Docket CC 96-98, page 3.

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1 The first step is to maintain the existing cap on CLEC access rates and to issue an Order
2 permitting the three exceptions outlined above. This will provide CLECs with the same revenue
3 opportunity as their ILEC competitors and will provide some incentive for the incumbents to
4 reduce terminating switched access rates as local competition expands.

5 The second step should be to reduce and ultimately eliminate the per minute Carrier of
6 Common Line rate element from the current exchange access rate structure, replacing it with a
7 flat monthly per-line charge. As explained earlier, this step will allow costs to be recovered in
8 the manner in which they are incurred. Taking this action will eliminate a current implicit
9 subsidy mechanism that forces high volume toll users to pay disproportionately more than low
10 volume toll users for facilities which bear the same cost regardless of use and regardless of
11 customers' ability to pay. This step can be initiated quickly and does not require the
12 Commission to make any decision on the TSLRIC cost of switched access.

13 The third step will be to move the traffic sensitive access rate elements towards their
14 TSLRIC costs in recognition of the fact that business decisions are based upon economic costs.
15 Differing regulatory schemes may require separate approaches for ILECs regulated under price
16 cap regulation as compared to ILECs regulated under rate-of-return regulation. As has already
17 been addressed, I believe this is certainly permissible.

18 **CAN YOU ELABORATE ON HOW THE SECOND STEP OF ELIMINATING THE CCL**
19 **RATE FOR PRICE CAP COMPANIES BE ACCOMPLISHED?**

20 For ILECs regulated under price regulation, Section 392.245 sets forth the maximum
21 prices that can be charged for exchange access service. Pursuant to Section 386.020(17) RSMo.
22 2000, exchange access service is defined broadly as "a service provided by a local exchange
23 telecommunications company which enables a telecommunications company or other customer
24 to enter and exit the local exchange telecommunications network in order to originate and
25 terminate interexchange telecommunications service." Within the umbrella of exchange access
26 service is switched access service that includes multiple rate elements such as end-office

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1 switching, tandem switching, and interoffice transport. Based upon a layman's reading of the
2 price cap statutes, which only focus on the maximum rates for the umbrella of exchange access
3 service, I believe the Commission can require the restructuring of the individual rate elements as
4 long as it does not result in an overall increase in the maximum rates for exchange access service
5 other than those contemplated by the statutes. It does not seem reasonable that the election of
6 price-cap regulation mandated every individual rate element be frozen in time. Such
7 restructuring would be analogous to a price cap LEC modifying a monthly rate for basic local
8 service to eliminate a mileage charge or restructuring toll rates from a mileage sensitive rate
9 structure to a postalized rate structure.

10 **HOW COULD THE REVENUES THAT WERE LOST AS A RESULT OF**
11 **ELIMINATING THE CCL BE RECOVERED?**

12 Revenues associated with the CCL could be shifted and recovered via a flat monthly rate element
13 assessed directly to retail customers in the same manner as a subscriber line charge. The
14 monthly rate would reflect the underlying cost of the loop facilities that are currently subsidized
15 via the CCL rate element and would provide for the proper recovery of those costs in a non-
16 traffic sensitive manner.

17 **IS IT PERMISSIBLE TO IMPOSE A SUBSCRIBER LINE CHARGE ON RETAIL**
18 **CUSTOMERS UNDER THE PRICE CAP STATUTES?**

19 Again, based upon a layman's reading, I believe so. Nothing in the price cap statutes dictates
20 how or from whom the rates for exchange access service must be recovered. The statutes only
21 focus on the broad category of exchange access service. Also there is precedent for the
22 implementation of such a surcharge based upon the Commission's ruling in a similar situation,
23 where Southwestern Bell was permitted to recover the cost of implementing IntraLATA Dialing

1 Parity over a three-year period as a new access rate element assessed on total intrastate
2 originating minutes while under price cap regulation²⁴.

3 **DOES SUCH A SUBSCRIBER LINE CHARGE RESULT IN AN INCREASE IN BASIC**
4 **LOCAL RATES?**

5 No. Basic local rates are set forth in the current tariffs and the imposition of subscriber line
6 charge or other new rate element does not change those rates.

7 **HOW WOULD THIS RESTRUCTING BE ACCOMPLISHED FOR ILECS**
8 **REGULATED UNDER RATE OF RETURN REGULATION?**

9 This can certainly be accomplished in the context of a rate case where all rates are reviewed. The
10 existing rate structure could also be restructured on a revenue neutral basis outside of a general
11 rate case.

12 **HAS AT&T ESTIMATED THE FINANCIAL IMPACTS OF THIS TYPE OF**
13 **RESTRUCTING?**

14 Yes. Based upon the analysis performed by AT&T witness Michael Pauls, the statewide
15 monthly per line impact of this restructuring equates to \$3.49 ranging from \$1.06 per month for
16 SWBT and \$26.42 for Steelville. Given the magnitude of this charge, the Missouri Universal
17 Service fund should be used to maintain affordable rates.

18 **HOW COULD THE MISSOURI USF FUND BE USED AS PART OF THIS PROCESS?**

19 Under the existing Commission USF rules, the Commission is required to establish a just,
20 reasonable and affordable rate for Essential Local Telecommunications Service as defined by
21 that rule.

²⁴ Case No. TO-99-535, *In the Matter of Southwestern Bell Telephone Company intraLATA long distance dialing parity plan*, Issued 6/10/99, download from <http://168.166.4.147/orders3.asp>

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1 In instances where the basic local rate and the subscriber line charge I have proposed exceed a
2 just reasonable and affordable rate, the high cost portion of the MO USF should be used fund
3 that difference.

4
5 **IN REBUTTAL TESTIMONY, SWBT'S WITNESS MR. UNRUH ARGUES THAT THE**
6 **MO USF COULD NOT BE USED TO REDUCE EXCHANGE ACCESS RATES. WHAT**
7 **IS YOUR RESPONSE?**

8
9 I do not agree. I believe the overriding purpose of the High Cost Fund is to remove
10 implicit subsidies from the existing rates and replace those with explicit, predictable, and
11 competitively neutral subsidies necessary to ensure the availability of local service at just,
12 reasonable and affordable rates in a competitive market. In accomplishing this, switched access
13 rates are properly reduced through the universal service fund. Eliminating the CCL and moving
14 the other switched access rates towards TSLRIC is consistent with that approach.

15 However, I would also note that the position taken s by Mr. Unruh is contrary to the
16 position taken by SWBT's other witness, Mr. Barch. Consistent with the cost-causer approach,
17 Mr. Barch argues that loop costs are directly attributable only to basic local service. Therefore,
18 even under SWBT's view, I believe the Missouri Universal Fund can properly be used to, at a
19 minimum, reduce CCL rates, as the costs reflected in those rates are part of the cost of basic local
20 service and bear no relationship whatsoever to the cost of providing access service. This
21 principal holds true for essential local service, which requires the full functionality of the loop.

22
23 **YOU MENTIONED THE THIRD AND FINAL STEP WAS TO THEN MOVE THE**
24 **REMAINING TRAFFIC SENSITIVE RATE ELEMENTS TOWARDS THEIR TSLRIC.**
25 **HOW CAN THIS BE DONE?**

26 This should be done in a similar fashion. Either in this proceeding or a subsequent proceeding,
27 the Commission needs to determine the appropriate TSLRIC for each rate element. Once that is

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1 done, those costs can be compared to the existing rates. To the extent there are differences
2 between the TSLRIC and the current access rates, the first choice would be to rebalance within
3 the differing rate elements to match the rates with the TSLRIC results. For price cap LECs, any
4 excess revenue that needs to be offset should be recovered through the Missouri Universal Fund.
5 While this may not seem ideal, it is the only way those revenues may be recovered on a
6 competitively neutral basis. For rate of return LECs, any differences can be dealt with in a
7 subsequent earnings case, through a similar use of the MO USF, or both.

8 **IN YOUR PREVIOUS QUESTION, YOU ASSUMED THAT THE TSLRIC RESULTS**
9 **WOULD BE LESS THAN THE EXISTING RATES. WHAT IF THAT WAS NOT THE**
10 **CASE?**

11
12 If the situation did arise where the existing rates were less than the TSLRIC results, it would be
13 appropriate to increase those rates to TSLRIC levels. For price cap LECs, increasing the various
14 rate elements and reducing receipts from the MO USF to make the adjustment revenue neutral
15 could accomplish this. With rate of return LECs, this can be accomplished in a rate case
16 proceeding or another revenue neutral mechanism if that would not require a rate case.

17 **HAS AT&T BEEN ABLE TO QUANTIFY THE TOTAL IMPACT OF THIS PROPOSAL**
18 **TO MOVE ACCESS RATES TO TSLRIC?**

19 Yes. Using the same methodology, Mr. Pauls has calculated that the total monthly per line
20 amount required to reach this final step would be \$6.41 ranging from \$1.06 per month for SWBT
21 and \$26.42 for Steelville. Again the magnitude of this charge, the Missouri Universal Service
22 fund should be used to maintain affordability of rates.

23 **HOW SHOULD THE COMMISSION PROCEED IN ADDRESSING ILEC ACCESS RATES?**

24 At a minimum, in this proceeding, the Commission should make the current interim CLEC rate
25 cap permanent and adopt the three exceptions I have proposed. In addition, the Commission
26 should adopt a specific cost standard and methodology to be used in assessing the cost of access
27 so that it will be in a position at some point, to determine how much access rates should be

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1 reduced. I also recommend that the Commission take steps now to eliminate the CCL and, to the
2 extent it determines it is necessary to offset the revenues associated with the CCL to shift the
3 recovery of those costs/revenues to a per-line surcharge, the MO USF, or both. Taking the action
4 is required by the Act to make the implicit subsidy that currently is recovered through the CCL
5 explicit.

6 Finally, my testimony provides a roadmap that I believe is a proper way to address Missouri's
7 access rates. Whether the Commission adopts this proposal or looks to another one, I believe the
8 Commission must first resolve all jurisdictional issues affecting the ability to make changes to
9 access rates. Based upon a layman's reading, I believe the roadmap I have presented can be
10 implemented but I am certain that others will disagree. If the Commission decides to address
11 access rates in a subsequent phase of this proceeding or a different proceeding altogether, the
12 Commission must make it clear that it is serious about addressing access rates and provide a clear
13 scope and purpose so that parties are not still debating whether their access can be reduced or
14 whether access rates in general should be reduced but rather, the focus should turn to how should
15 the long-term solution be implemented.

16 DOES THAT CONCLUDE YOUR TESTIMONY?

17 Yes.

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