

MINUTES OF THE House COMMITTEE ON Communication, Computers and Technology

The meeting was called to order by Representative Mike Meacham at
Chairperson

3:30 ~~am~~/p.m. on February 10, 1983 in room 522-S of the Capitol.

All members were present except:

Committee staff present:

Marlin Rein, Chief Legislative Fiscal Analyst, Committee Staff Director
Sherry Brown, Fiscal Staff, Research Department
Chris Stanfield, Fiscal Staff, Research Department
Arden K. Ensley, Revisor of Statutes
Betty Ellison, Secretary to the Committee

Conferees appearing before the committee:

Ed Whitacre, Vice President of Southwestern Bell for Kansas Operations

Mr. Ed Schaub of Southwestern Bell introduced Mr. Whitacre who has been involved in the planning of divestiture and deregulation from a corporate headquarters standpoint. Mr. Whitacre remarked that divestiture and deregulation have been brought about by the explosion of new technology in the business, by the desires of others to compete in the business and the mood of the country toward deregulation. (Attachment 1)

Mr. Whitacre said that divestiture began in 1968 but has moved very rapidly recently; it applies only to the Bell system, not to independent companies. He said that on January 1, 1984, Southwestern Bell will be a separate company with no connection to AT&T. Southwestern Bell will have its own stock and stockholders. Southwestern Bell will provide local service, dial tone and local calling and will still have the Yellow Pages. Southwestern Bell will provide long distance service within LATAs (Local Access and Transport Areas). A LATA is a geographical section of Kansas in which Southwestern Bell can provide service after divestiture. There are three LATAs in Kansas, the Topeka LATA, the Wichita LATA, and the Kansas City LATA.

Mr. Whitacre stated that in order to achieve its goal of keeping the price low so that everyone can have a telephone, Southwestern Bell has in the past subsidized local rates with profits from long distance and other services. With divestiture, Southwestern Bell keeps most of its investment; most of the investment in Kansas is used to provide more local service than long distance. With divestiture, Southwestern Bell has lost much more revenue than investment. In order to earn a fair return as determined by the KCC, Southwestern Bell must increase revenues; those revenues must come in the form of higher bills to customers, and most must come from local service. The price charged for local service will be very close to what it costs to provide the service. Mr. Whitacre said that at the same time, long distance rates will go down substantially. Long distance rates will also be priced according to what it costs to provide that service; competition may drive long distance rates even lower.

Mr. Whitacre explained the term "access charge" as a method of recovering the cost of providing service to a customer. He said that a tentative plan would require customers to pay a flat rate plus a usage charge on a monthly basis for five years and at the end of five years, the customer would be paying a flat rate. This plan was developed by the Federal Communications Commission. Long distance carriers, AT&T, MCI, etc., will also pay for the use of switching equipment and for switching costs, so not all of the cost will go to the customer.

CONTINUATION SHEET

MINUTES OF THE House COMMITTEE ON Communication, Computers and Technology
room 522-S, Statehouse, at 3:30 ~~xx~~ p.m. on February 10, 1983

The conferee quoted Professor Charles Phillips of Washington and Lee University, who is an expert in this field, as saying, "Universal service will not vanish, but universal service will be much more complex to achieve". Some alternatives to raising the rates to the level described would be:

1. The OLCP Plan, which is measured service or cost based on amount the telephone is used.
2. Flat rate service offering, a high-priced, premium service.
3. Alternative lifeline-type service, for those people on fixed incomes who need a telephone to stay in touch with the outside world.

Representative Roper asked who is responsible for maintenance of components now in use - Mr. Whitacre answered that after January, 1984, they will belong to AT&T and it will be AT&T's responsibility to maintain them. Southwestern Bell has testing equipment to determine if a problem is in the telephone or in the line; if it is in the line, Southwestern Bell will repair it.

Another term the conferee explained was "equal access", which means that a customer may place a long distance call on AT&T, MCI, or whichever service he chooses. He will be billed by the service he has used.

In answer to another question, Mr. Whitacre said that the FCC is responsible for regulating inter-state charges and the KCC regulates intra-state charges as in the past. These usage charges have to be on an equal basis - this is called parity. In answer to a question by Representative Dean, Mr. Whitacre commented that all costing is done at the origination of a call.

Chairman Meacham announced that on Tuesday and Wednesday of next week, the committee will take up the Telecommunications Plan; he encouraged everyone to study the Plan carefully before making this important decision. He said the agenda is unannounced for Thursday in case the committee needs more time for this consideration.

Representative Friedeman announced that the sub-committee on Distribution of Public TV Grants will meet at 3:30 p.m. on Monday, February 14, in room 522-S.

The meeting was adjourned at 4:35 p.m. by the Chairman.

The next meeting of the committee will be held at 3:30 p.m. on February 15, 1983.

Date: Feb. 10, 1983

GUEST REGISTER

HOUSE

COMMITTEE ON COMMUNICATION, COMPUTERS AND TECHNOLOGY

NAME	ORGANIZATION	ADDRESS
Don Hoover	American Bell Inc	2702 Rockcreek ^{no Kansas City}
JEFF ROSSER	UNITED Telephone	TOPEKA
Harold Bush	Court	Atchison
Dorothy Bush	Court	Atchison
L. J. Kunkel	Dept of Admin - Telecomm Dtc	Topeka
J. P. Gilbert	Dept of Admin - Telecommunications	Topeka
John Jennings	" "	"
Ed C. Rapp.	Public Rep. "	"
Don Low	KLL	50B
David Brivity	KCC	State office Bldg.
J. B. ELLIS	S.W. Bell	220 E. 6th
Ed. WHITACKER.	S.W. Bell	220 E. 6th
DON HOFFMAN	SW BELL & LWA	938 WABASH
G.W. EWING	S.W.B.	220 E. 6TH
BURR SIFERS	CHANNEL 19	
Ed Schaub	A.W.B.T.	Topeka
Edman Schmidt	TELEPHONE TIMES	TOPEKA
J. CAREY BROWN	DOFA - DISC	50B
Reggie Seif	KSNT	Lawrence

DIVESTITURE
A STATUS REPORT

PRESENTATION TO THE HOUSE COMMUNICATION,
COMPUTERS AND TECHNOLOGY COMMITTEE OF THE
KANSAS LEGISLATURE

EDWARD E. WHITACRE
SOUTHWESTERN BELL
VICE PRESIDENT-KANSAS

FEBRUARY 10, 1983

Attachment 1

House Communication, Computers and Technology 2/10/83

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE, I'M ED WHITACRE,
VICE PRESIDENT OF SOUTHWESTERN BELL'S KANSAS OPERATIONS.
THANK YOU FOR INVITING ME TO BE WITH YOU TODAY.

I WOULD BE REMISS IF I DID NOT FIRST COMMEND THE KANSAS
HOUSE LEADERSHIP FOR HAVING THE FORESIGHT TO FORM THIS, THE
COMMUNICATION, COMPUTERS AND TECHNOLOGY COMMITTEE.

AND, I WOULD BE EQUALLY REMISS IF I DID NOT COMMEND YOU,
THE COMMITTEE'S CHAIRMAN AND MEMBERS, FOR TAKING THE TIME
THIS WEEK TO EXPLORE THE SIGNIFICANT CHANGES TAKING PLACE IN
THE TELECOMMUNICATIONS INDUSTRY.

TO THE CASUAL OBSERVER, THE CHANGES WHICH ARE UPON US,
AND THOSE WHICH ARE IMPENDING, MAY HAVE SEEMED TO BE A SHARP
AND UNEXPECTED DEPARTURE IN THE NATION'S PUBLIC POLICY TOWARD
TELECOMMUNICATIONS. IN A SENSE, THAT IS CORRECT. BUT IT IS
NOT THE WHOLE STORY.

IN RETROSPECT, THOSE OF US IN THE TELECOMMUNICATIONS
INDUSTRY CAN NOW SEE THAT THE CHANGES ARE SIMPLY THE CULMINATION
OF A SERIES OF PRESSURES THAT HAD BEEN BUILDING IN THE
PRECEDING TWO DECADES...PRESSURES BROUGHT ABOUT BY THE ADVANCES
IN TECHNOLOGY THAT HAVE MERGED COMMUNICATIONS AND DATA PROCESSING,
AND THE PRESSURES OF THE NATION'S GROWING INCLINATION TO MOVE
AWAY FROM REGULATION AND TOWARD COMPETITION IN REGULATED INDUSTRIES.

THE WORK OF YOUR COMMITTEE THIS WEEK HAS TAKEN YOU TO OUR ELECTRONIC SWITCHING SYSTEM OFFICE AT 820 JACKSON WHERE YOU SAW THE \$10 MILLION WORKHORSE OF THE LOCAL COMMUNICATIONS SYSTEM FOR MORE THAN 45,000 CUSTOMERS IN CENTRAL TOPEKA.

YOU'VE HEARD FROM THE KANSAS CORPORATION COMMISSION AND FROM THE DEPARTMENT OF ADMINISTRATION.

MY ROLE IN YOUR WEEK-LONG REVIEW OF THE TELECOMMUNICATIONS INDUSTRY IS TO DESCRIBE TO YOU THE CHANGES DIVESTITURE BRINGS TO SOUTHWESTERN BELL AND WHAT ALL THIS MEANS TO OUR CONSTITUENTS -- YOUR'S AND MY COMPANY'S, FOR THEY ARE ONE IN THE SAME.

CI-II

SOUTHWESTERN BELL TODAY IS OPERATING IN ITS NEW ENVIRONMENT MANDATED BY THE FCC'S COMPUTER INQUIRY II DECISION. AS OF JANUARY 1, OF THIS YEAR, OUR CUSTOMER EQUIPMENT OFFERING IS RESTRICTED TO THE EQUIPMENT IN OUR INVENTORY AS OF DECEMBER 31, 1982.

BY INVENTORY, I MEAN THAT EQUIPMENT WE HAD ON OUR SHELVES OR INSTALLED ON OUR CUSTOMER'S PREMISES ON DECEMBER 31, 1982. CUSTOMERS WISHING EQUIPMENT NOT IN SOUTHWESTERN BELL'S INVENTORY ARE NOW GOING TO AMERICAN BELL, INC., THE NEW AT&T SUBSIDIARY SET UP TO HANDLE EQUIPMENT OFFERINGS, OR TO THE MANY VENDORS WHICH ALSO MERCHANDISE COMMUNICATIONS EQUIPMENT.

GONE TODAY ARE SOUTHWESTERN BELL'S 31 KANSAS PHONE CENTER STORES. THE FIVE WHICH REMAIN IN KANSAS ARE NOW OWNED AND OPERATED BY AT&T. OUR'S HAVE BEEN REPLACED BY CUSTOMER SERVICE CENTERS WHERE CUSTOMERS CAN PICK UP TELEPHONES ORDERED THROUGH OUR BUSINESS OFFICE OR DROP OFF TELEPHONES THAT REQUIRE REPAIR.

GONE, TOO, ARE SOME 225 EMPLOYEES WHO USED TO WORK FOR SOUTHWESTERN BELL IN KANSAS BUT NOW WORK FOR AMERICAN BELL IN KANSAS.

AS WE EXPECTED, THE CHANGES WHICH TOOK PLACE JANUARY 1 HAVE SO FAR HAD VERY LITTLE EFFECT ON OUR CUSTOMERS.

THOSE WHO CHANGE SERVICE, WHICH IS ABOUT ONLY ONE OF EVERY 10 IN A YEAR, SHOULD BE THE ONLY CUSTOMERS AFFECTED BY THE CI-II ENVIRONMENT.

FOR EXAMPLE, IT'S LIKELY THAT DURING THE YEAR, WE'LL RUN SHORT OF CERTAIN TELEPHONES IN OUR INVENTORY. IF SO, WE'LL DIRECT CUSTOMERS WHO DO NOT SELECT ALTERNATE STYLES OR COLORS OF PHONES THAT WE HAVE IN INVENTORY TO THE YELLOW PAGES TO BUY FROM ANOTHER SUPPLIER, WHICH MAY INCLUDE AMERICAN BELL.

THE BOTTOM LINE IS THAT SOUTHWESTERN BELL IS TODAY SUCCESSFULLY IMPLEMENTING THE FCC'S CI-II DECISION WITH ONLY MINIMAL NOTICE BY THOSE WE SERVE.

DIVESTITURE

BUT THE BIGGEST CHANGE HAS YET TO COME. THAT, AS YOU KNOW, IS THE DIVESTITURE OF SOUTHWESTERN BELL AND THE OTHER BELL OPERATING COMPANIES FROM AT&T...SCHEDULED TO TAKE PLACE A LITTLE MORE THAN 10 MONTHS FROM NOW. UNLIKE THE IMPLEMENTATION OF CI-II, DIVESTITURE WILL BRING WITH IT AN ARRAY OF READILY NOTICEABLE CHANGES.

COMMUNICATING THE IMPENDING CHANGES AND THEIR EFFECTS ON OUR CUSTOMERS IS ONE OF OUR TOP PRIORITIES FOR 1983. WE HAVE PLANNED AN EXTENSIVE FACE-TO-FACE AND ADVERTISING EFFORT TO INFORM ALL KANSAS TELEPHONE CUSTOMERS ABOUT DIVESTITURE PRIOR TO JANUARY 1, 1984. AS YOU CAN APPRECIATE, THIS IS GOING TO BE A MASSIVE UNDERTAKING.

AT&T

LET'S TAKE A LOOK AT WHAT AT&T WILL OFFER AFTER JANUARY 1, 1984.

(CHART)

- INTERSTATE, INTERLATA LONG DISTANCE SERVICE. *INTERLATA*
- NEW CUSTOMER PREMISES EQUIPMENT.
- ENHANCED SERVICES, SUCH AS DATA COMMUNICATIONS.
- (WESTERN ELECTRIC AND BELL TELEPHONE LABORATORIES STILL PART OF AT&T.)

SOUTHWESTERN BELL

Now, SOUTHWESTERN BELL. WE WILL PROVIDE:

(CHART)

- BASIC LOCAL TELEPHONE SERVICE.
- YELLOW PAGES.
- IN-STATE, INTRALATA LONG DISTANCE SERVICE.
- ADVANCED MOBILE PHONE SERVICE.
- ACCESS TO FUTURE NETWORK SERVICES.

MOST OF THE SERVICES AT&T AND SOUTHWESTERN BELL EACH WILL PROVIDE CUSTOMERS ARE EASILY UNDERSTOOD...EXCEPT LONG DISTANCE. AND, HERE, A NEW TERM HAS ENTERED THE TELECOMMUNICATIONS VOCABULARY---LATA, (OR) LOCAL ACCESS AND TRANSPORT AREA.

AN "EXCHANGE" OR LATA MAY INCLUDE SEVERAL TOWNS AND WE'VE PROPOSED THAT KANSAS BE DIVIDED INTO THREE SOUTHWESTERN BELL "EXCHANGES"...OR "LATA'S".

(CHART)

MOST OF THE STATE WOULD BE DIVIDED ALONG A LINE THAT CORRESPONDS TO OUR PRESENT AREA CODE BOUNDARY. SO, THE 316 AREA CODE, WHICH OF COURSE INCLUDES WICHITA AND GENERALLY THE SOUTHERN HALF OF THE STATE, WOULD BE ONE "EXCHANGE". THE 913 AREA CODE IN THE NORTHERN HALF OF THE STATE WOULD COMPRISE THE SECOND OF THESE NEW "EXCHANGES". AND, FINALLY, METROPOLITAN KANSAS CITY -- INCLUDING COMMUNITIES ON BOTH SIDES OF THE STATE LINE -- WOULD BE THE THIRD.

IF A CALL IS BETWEEN TWO TOWNS IN THE SAME EXCHANGE, IT WOULD BE HANDLED BY SOUTHWESTERN BELL. IF IT BEGINS IN ONE EXCHANGE AND ENDS IN ANOTHER, IT'S AT&T'S OR MCI'S OR SOME OTHER COMPANY'S BUSINESS.

IF YOU PLACE A CALL FROM TOPEKA TO WICHITA, FOR EXAMPLE, IT WOULD BE HANDLED BY AT&T OR ONE OF THE OTHER LONG DISTANCE COMPANIES SEEKING YOUR BUSINESS. A CALL FROM TOPEKA TO SALINA, ON THE OTHER HAND, WOULD BE HANDLED BY SOUTHWESTERN BELL OR BY COMPETITORS SINCE THE CALL WOULD BE TOTALLY WITHIN THE NEWLY DEFINED "EXCHANGE".

PRICING

WITH EACH PASSING DAY, ALL ASPECTS OF DIVESTITURE ARE COMING INTO CLEARER FOCUS. AND FROM THAT FOCUS HAVE EMERGED THE VERY CRITICAL IMPLICATIONS WITH REGARD TO THE PRICING PHILOSOPHY OF TELECOMMUNICATIONS SERVICES.

THIS BRINGS US TO THE KEY QUESTION OF DIVESTITURE'S COST EFFECT ON THE GOOD PEOPLE OF KANSAS. THE ANSWER TO THAT QUESTION IS AS BIG A CONCERN OF OUR'S AS I KNOW IT IS OF YOUR'S.

WE'VE CERTAINLY HAD NO SHORTAGE OF SPECULATION ON WHAT DIVESTITURE WILL MEAN TO THE COST OF TELEPHONE SERVICE. THAT SPECULATION BEGAN ALMOST AS SOON AS THE DIVESTITURE AGREEMENT WAS ANNOUNCED EARLY LAST YEAR...WITH PREDICTIONS OF A DOUBLING OR TRIPLING OF LOCAL RATES BEING VOICED ACROSS THE COUNTRY.

TODAY, JUST 10 MONTHS AWAY FROM DIVESTITURE, IT APPEARS THAT THOSE PREDICTIONS ARE ANYTHING BUT FAR-FETCHED.

ANYTHING BUT FAR-FETCHED BECAUSE DIVESTITURE, COMPETITION AND OTHER CHANGES ALREADY AT WORK IN THE TELECOMMUNICATIONS INDUSTRY MAKE IT NECESSARY THAT TELEPHONE USERS BEGIN PAYING THE TRUE COST OF LOCAL TELEPHONE SERVICE.

HISTORICALLY, THE DIFFERENCE BETWEEN WHAT IT COSTS US TO PROVIDE LOCAL SERVICE AND WHAT THE COMPANY CHARGES HAS BEEN MADE UP BY LONG DISTANCE REVENUE, INCOME FROM THE RENTAL OF COMMUNICATIONS EQUIPMENT AND LENGTHY DEPRECIATION SCHEDULES ON EQUIPMENT.

BUT WITH DIVESTITURE, THOSE SUBSIDIES WILL NO LONGER EXIST. THE LONG DISTANCE REVENUE SOUTHWESTERN BELL HAS SHARED WITH AT&T VANISHES. INCOME FROM THE RENTAL OF TELEPHONE EQUIPMENT DISAPPEARS. DEPRECIATION IS BEING ACCELERATED ON EQUIPMENT USED TO PROVIDE LOCAL SERVICE.

AS A RESULT OF THESE LOST SUBSIDIES TO LOCAL SERVICE, MOST OF THE COMPANY'S FUTURE REVENUE NEEDS MUST COME FROM THE LOCAL TELEPHONE CUSTOMER.

I THINK THIS CHART DOES A GOOD JOB OF ILLUSTRATING THE PRICING DILEMMA DIVESTITURE BRINGS UPON US.

(CHART)

-- <u>COST</u> OF LOCAL SERVICE	\$24/MONTH
-- AMOUNT <u>CHARGED</u> FOR LOCAL SERVICE	\$10/MONTH

What is this?
?
1
-- \$47 MILLION OF LD REVENUES GOES TO HELP PAY FOR LOCAL TELEPHONE SERVICE

NOW LET'S EXAMINE THE STRUCTURE OF OUR CUSTOMER'S TELEPHONE COSTS IN A DIVESTITED ENVIRONMENT...WITHOUT SUBSIDIES.

THERE WILL BE THREE BASIC PARTS:

(CHART)

1) CHARGES FOR THE TWO-WAY LOCAL TRANSMISSION LINK, ~~OFTEN~~ REFERRED TO ~~WITHIN THE TELEPHONE COMPANY AS NON-TRAFFIC SENSITIVE PLANT.~~

2) CHARGES FOR SWITCHING AND TRUNKING COSTS FOR LOCAL CALLING, AND

3) LONG DISTANCE CALLING, BOTH WITHIN AND BEYOND OUR LATAs.

ACCESS CHARGES

IT IS THE FIRST OF THESE THREE ELEMENTS THAT POSES THE IMMEDIATE PROBLEM FOR SOUTHWESTERN BELL. ON DECEMBER 22, 1982, THE FCC ANNOUNCED ITS PLAN TO IMPOSE NEW CHARGES FOR WHAT THE FCC CALLS ACCESS TO THE LONG DISTANCE NETWORK.

THESE CHARGES ACTUALLY APPLY TO THE COST OF THE LOCAL TRANSMISSION LINK WHICH CONNECTS THE SUBSCRIBER'S TELEPHONE TO THE LOCAL CENTRAL SWITCHING OFFICE AND THUS TO THE OUTSIDE WORLD. THEY ARE CALLED FIXED OR NON-TRAFFIC SENSITIVE COSTS. AND THESE COSTS ARE INCURRED BY SOUTHWESTERN BELL WHETHER THE CUSTOMER USES LONG DISTANCE SERVICE OR NOT.

IMPOSING CHARGES MANDATED BY THE FCC FOR THIS TRANSMISSION LINK IN A SINGLE STEP WOULD NOT BE PALATABLE TO MANY CUSTOMERS.

INSTEAD, THE SHIFT IN THE COST RECOVERY PROCESS FROM LONG DISTANCE TO THE CUSTOMER'S LOCAL SERVICE BILL WILL BE PHASED IN OVER FIVE YEARS, WITH A PORTION OF THE COST REMAINING ON THE LONG DISTANCE CARRIERS DURING THE FIRST FIVE YEARS OF THE PHASE-IN.

DURING THE FIRST YEAR OF THE PHASE-IN, NON-TRAFFIC SENSITIVE PLANT COSTS WILL BE BORNE BY CUSTOMERS AND CARRIERS, WITH THE CUSTOMER SHARE INCREASING IN EACH OF THE FIRST FIVE YEARS.

THE CUSTOMER CHARGE WILL BE IN TWO PARTS.

FIRST, A FLAT MONTHLY CHARGE OF AT LEAST \$2 A MONTH FOR RESIDENCE CUSTOMERS AND AT LEAST \$4 PER LINE FOR BUSINESS CUSTOMERS.

SECOND, A USAGE CHARGE WILL BE APPLIED TO EACH INTERSTATE LONG DISTANCE CALL AND CHARGED TO THE INDIVIDUAL LOCAL CUSTOMERS UP TO A PREDETERMINED MAXIMUM TOTAL CHARGE OR TOPPING AMOUNT PER MONTH.

AT THE END OF THE FIFTH YEAR OF TRANSITION, ALL NON-TRAFFIC SENSITIVE COSTS MUST BE BORNE BY LOCAL CUSTOMERS. THIS COULD BE ACCOMPLISHED THROUGH A MIX OF USAGE AND FLAT CHARGES. AT THE END OF SEVEN YEARS, ALL OF THESE CHARGES WILL BE COLLECTED ON A FLAT RATE BASIS.

FROM MOST ANYONE'S POINT OF VIEW, THE ACCESS CHARGE CONCEPT ITSELF IS INDEED A VALID ONE. I DOUBT FEW WOULD ARGUE THE NEED FOR SUCH A MECHANISM WITH MONOPOLY LONG DISTANCE CONTRIBUTIONS DISAPPEARING.

THE ISSUES GET TOUGHER, THOUGH, WHEN THE DISCUSSION SHIFTS TO HOW THOSE CHARGES SHOULD ACTUALLY BE SET...AND PERHAPS MOST FUNDAMENTALLY, WHERE THEIR BURDEN SHOULD FALL.

THERE IS AN UNDENIABLE FACT THAT THE FIXED COSTS OF LINKING CUSTOMERS TO THE OUTSIDE WORLD MUST NOW, SOMEHOW, BE FULLY RECOVERED. THE QUESTION BECOMES ONE OF HOW TO ACHIEVE THAT RECOVERY.

SHOULD THE FULL AMOUNT BE PAID BY THE LOCAL END USER?

IF THE COST BURDEN BECOMES TOO GREAT -- OR IF IT'S SHIFTED TOO SUDDENLY -- WE COULD VERY EASILY PRICE A SIGNIFICANT NUMBER OF CUSTOMERS OFF THE LOCAL NETWORK. NEITHER REGULATORY COMMISSIONS NOR LOCAL TELEPHONE COMPANIES WANT THAT TO HAPPEN.

WHAT IF THE FULL AMOUNT IS PLACED ON THE LONG DISTANCE CARRIERS? TO DO SO BRINGS US FACE-TO-FACE WITH A VERY COMPELLING REALITY: THE REALITY OF BYPASS.

OF COURSE, BYPASS -- THE ACT OF A BUSINESS BUILDING ITS OWN TELEPHONE SYSTEM TO ESCAPE BELL CHARGES OR OBTAINING BYPASS SERVICE FROM ANOTHER CARRIER TO ACCOMPLISH THE SAME THING -- ISN'T REALLY A NEW CONCERN AT ALL.

THE TECHNOLOGY HAS BEEN AVAILABLE FOR SOME TIME NOW. AND BYPASS IS A REALITY IN VIRTUALLY EVERY MAJOR MARKET IN SOUTHWESTERN BELL TERRITORY. THE URGENCY ATTACHED TO BYPASS TODAY, OF COURSE, IS A DIRECT RESULT OF THE ACCESS CHARGES BEING FILED WITH FEDERAL AND STATE COMMISSIONS.

AS WE SEE IT, THE WAY THOSE CHARGES ARE ULTIMATELY SET COULD EASILY TURN A VERY LEGITIMATE CONCERN INTO A BONAFIDE THREAT...JEOPARDIZING NOT ONLY THE FUTURE FINANCIAL WELL-BEING OF THE INDEPENDENT REGIONAL COMPANIES...BUT ALSO THE LONG-TERM AFFORDABILITY OF LOCAL TELEPHONE SERVICE.

IF THE LOCAL NETWORK IS BYPASSED...WHETHER BY A MAJOR BUSINESS OR A MAJOR USER OF TELECOMMUNICATIONS SERVICES SUCH AS THE STATE OF KANSAS, WHICH AS YOU KNOW IS CONSIDERING BUILDING ITS OWN SYSTEM...THE RESIDENTIAL CUSTOMER WILL ULTIMATELY FEEL THE IMPACT.

I WOULD LOOK FORWARD TO MEETING WITH YOU AGAIN IN THE NEAR FUTURE TO SHARE MY THOUGHTS ON A STATE-OWNED TELEPHONE SYSTEM.

COST TO KANSAS CUSTOMERS

BACK TO THE IMPORTANT QUESTION OF HOW MUCH WILL KANSAS CUSTOMERS WIND UP PAYING. WE'RE TAKING A CLOSE LOOK RIGHT NOW AT THOSE PROBABLE COSTS. BUT IT APPEARS THE COSTS WILL AT LEAST DOUBLE.

NO MATTER WHAT THE FIGURES TURN OUT TO BE, HOWEVER, IT'S IMPORTANT TO REMEMBER THAT MY COMPANY'S NEED FOR ADDITIONAL REVENUES DUE TO DIVESTITURE IS JUST ONE REASON FOR INCREASED CHARGES TO OUR CUSTOMERS. ANOTHER IS THAT SERVICE IS ALREADY SEVERELY UNDERPRICED -- WITH OR WITHOUT DIVESTITURE.

AS YOU KNOW, WE'VE JUST CONCLUDED HEARINGS BEFORE THE KCC ON A \$63.5 MILLION RATE REQUEST IN WHICH WE HOPE TO BRING LOCAL SERVICE REVENUES MORE IN LINE WITH THE COSTS OF PROVIDING THE SERVICE.

WHATEVER THE KCC'S DECISION ON THAT REQUEST, WE WILL BE FILING AN APPLICATION SOMETIME THIS SPRING THAT WILL REFLECT THE TRUE COSTS OF PROVIDING SERVICE TO OUR CUSTOMERS IN THE DIVESTED ENVIRONMENT.

SOUTHWESTERN BELL HAS A \$1 BILLION INVESTMENT IN KANSAS... AN INVESTMENT THAT WILL REMAIN OUR'S FOLLOWING DIVESTITURE. WE MUST EARN AN ADEQUATE RETURN ON THAT INVESTMENT. THE ONLY WAY FOR US TO MAKE UP THE LOST REVENUES CAUSED BY DIVESTITURE IS TO PRICE SERVICE AT WHAT IT COSTS US TO PROVIDE THE SERVICE.

UNIVERSAL SERVICE

ALL OF THIS TALK OF SIGNIFICANT PRICE INCREASES RIGHTFULLY PROMPTS TALK OF THE VERY FOUNDATION OF TELEPHONE SERVICE PRICING THAT HAS EXISTED IN AMERICA FOR ALMOST 50 YEARS...THE CONCEPT OF UNIVERSAL SERVICE.

IS UNIVERSAL SERVICE DOOMED? I SAY NO...NOT IF WE REDEFINE IT AND IF WE -- ALL OF US, THE TELEPHONE COMPANY, REGULATORS AND LAWMAKERS -- DILIGENTLY STRIVE TO SEE THAT IT IS NOT DOOMED.

I THINK ECONOMICS PROFESSOR CHARLES F. PHILLIPS OF WASHINGTON AND LEE UNIVERSITY PHRASED IT WELL WHEN QUOTED IN THE KANSAS CITY STAR LAST WEEK. HE SAID: "I DON'T THINK UNIVERSAL SERVICE IS IN DANGER, BUT IT WILL BE MORE COMPLEX TO ACHIEVE."

WITHOUT QUESTION, UNIVERSAL SERVICE IS A SOCIALLY SOUND PHILOSOPHY...A PHILOSOPHY THAT'S PUT AN AFFORDABLE-PRICED PHONE IN VIRTUALLY EVERY HOME IN THE COUNTRY (AN ACCOMPLISHMENT NOT ACHIEVED IN OTHER NATIONS)...A PHILOSOPHY TO WHICH WE IN SOUTHWESTERN BELL INTEND TO REMAIN COMMITTED.

AS WITH OTHER SOCIAL AND POLITICAL ISSUES TODAY, THOUGH, TO CONTINUE TO WORK, IT MUST BE GROUNDED IN ECONOMIC REALITY AS WELL.

WORKING TOGETHER

AND FOR STATE REGULATORY COMMISSIONS AND THE TELEPHONE COMPANIES THEY REGULATE, THIS IS PERHAPS THE MOST PRESSING AND IMMEDIATE CHALLENGE AHEAD.

WE MUST WORK TOGETHER TO DEVELOP NEW AND RESPONSIVE LOCAL PRICING STRUCTURES THAT ADDRESS TODAY'S REALITIES:

- THAT ENABLE FULL RECOVERY OF THE ACTUAL COSTS OF PROVIDING LOCAL SERVICE...
- THAT TAKE INTO ACCOUNT OUR CUSTOMER'S IMPORTANT NEED FOR CHOICE AND CONTROL...
- AND, EQUALLY SIGNIFICANT, THAT RECOGNIZE WE MUST CONTINUE TO OFFER AN APPROPRIATE, PERHAPS SUBSIDIZED, PRICING OPTION FOR THOSE WHO MIGHT OTHERWISE BE PRICED OFF THE LOCAL NETWORK.

DEVELOPING SUCH PRICING SOLUTIONS WILL BE NO SMALL ORDER. BUT I'M ENCOURAGED BY THE SIGNALS BEING SENT BY THE KANSAS CORPORATION COMMISSION WHICH REVEAL ITS AWARENESS OF SOME OF THE ISSUES SUCH AS THIS...AND BY THE VERY FACT THAT WE'RE EXAMINING SUCH ISSUES IN IMPORTANT FORUMS SUCH AS THIS TODAY.

AN EXAMPLE OF THIS COOPERATIVE WORKING TOGETHER IS TAKING PLACE IN KANSAS RIGHT NOW. IT'S A FIRST STEP DESIGNED TO PRESERVE THE CONCEPT OF UNIVERSAL SERVICE BY ALLOWING LOW USAGE CUSTOMERS TO PAY LESS FOR LOCAL SERVICE.

OPTIONAL LOCAL CALLING

THE KANSAS CORPORATION COMMISSION WORKED WITH US TO IMPLEMENT A TWO-YEAR TEST OF OUR OPTIONAL LOCAL CALLING PLAN IN 14 KANSAS COMMUNITIES. IN A SENSE, THIS PLAN REDEFINES THE TERM UNIVERSAL SERVICE TO MEAN UNIVERSAL ACCESS, RATHER THAN THE UNIVERSAL, UNLIMITED CALLING SERVICE CONCEPT THAT EXISTING FLAT RATES NOW ALLOW. OUR OPTIONAL LOCAL CALLING PLANS PERMIT CUSTOMERS TO PAY A RATE LOWER THAN THE FLAT MONTHLY RATE. ADDED CHARGES, THEN, ARE BASED ON THE NUMBER OF LOCAL CALLS CUSTOMERS PLACE.

SUCH A CALLING PLAN ALLOWS CUSTOMERS TO CONTROL THEIR OWN BILLS, BUT STILL OFFERS THEM ACCESS TO THE LOCAL CALLING NETWORK. SINCE WE STARTED OFFERING THIS OPTION IN NOVEMBER, MORE THAN 6,000 KANSAS CUSTOMERS HAVE SIGNED UP FOR THE SERVICE.

PRICING SUMMARY

TO SUM UP MY COMMENTS ON PRICING, LET ME AGAIN ACKNOWLEDGE THAT THIS FOCUS ON LOCAL RATES IS PROMPTED BY UNUSUAL CHANGES WHICH ARE TAKING PLACE IN THE TELECOMMUNICATIONS INDUSTRY---CHANGES WHICH REQUIRE A COMPREHENSIVE RESTRUCTURING OF THE FINANCIAL BASE OF OUR BUSINESS.

THIS IS THE UNAVOIDABLE RESULT OF A NEW NATIONAL PUBLIC POLICY THAT CALLS FOR COMPETITION, NOT REGULATION, TO RULE MAJOR PARTS OF THE TELECOMMUNICATIONS BUSINESS.

DESPITE OUR SWEEPING CHANGES TO COMPLETE THE EVOLUTION OF COMPETITION IN OUR INDUSTRY, I AM DETERMINED TO WORK WITH OUR CUSTOMERS AND THE KANSAS CORPORATION COMMISSION TO DO EVERYTHING POSSIBLE--INCLUDING NEW PRICING CONCEPTS--TO MINIMIZE INCONVENIENCE TO OUR SUBSCRIBERS.

I AM EQUALLY DETERMINED TO SEE THAT MY COMPANY HAS THE FINANCIAL VIABILITY IN 1984 AND BEYOND TO CONTINUE PROVIDING GOOD SERVICE AND TO CONTINUE MODERNIZING THAT SERVICE.

COMMITMENT

FINALLY, I PLEDGE TO YOU, MY PERSONAL COMMITMENT AND MY COMPANY'S COMMITMENT THAT THE IMPACT OF CHANGES IN OUR INDUSTRY ON THE LOCAL TELEPHONE CUSTOMER BE MANAGED IN SUCH A WAY THAT THE CUSTOMER CAN STILL HAVE AFFORDABLE TELEPHONE SERVICE.

FOR THIS TO HAPPEN, THOUGH, WE MUST WORK TOGETHER... THIS COMMITTEE, THE KANSAS CORPORATION COMMISSION AND OUR CUSTOMERS -- YOUR CONSTITUENTS AND OURS.

THE FUNDAMENTALS OF SOUTHWESTERN BELL IN KANSAS...GOOD MANAGEMENT, EXPENSE CONTROL AND EXCELLENT SERVICE...WILL NOT CHANGE. WE HAVE A STRONG TRACK RECORD IN THOSE FUNDAMENTALS.

A HEADLINE IN THE KANSAS CITY TIMES LAST WEEK ACCURATELY NOTED THE DAWNING OF A NEW ERA FOR THE BELL SYSTEM.

AS THAT NEW ERA DAWNS, WE IN SOUTHWESTERN BELL RECOMMIT OURSELVES TO THE RESPONSIBILITIES OF BEING YOUR LOCAL TELEPHONE COMPANY.

THAT COMMITMENT WILL NOT CHANGE. MY COMPANY AND ITS 7,500 KANSAS EMPLOYEES -- THE SAME PEOPLE YOU'VE WORKED WITH IN UNITED WAY DRIVES, IN COACHING LITTLE LEAGUE TEAMS, IN HELPING GROUPS OF SCOUTS, IN JOINING WITH YOU TO MAKE OUR TOWNS AND CITIES A BETTER PLACE TO LIVE -- WILL CONTINUE TO BE YOUR NEIGHBORS AND YOUR PARTNERS IN PROGRESS OF THIS GREAT STATE.

I THANK YOU FOR THE INVITATION TO SPEAK WITH YOU TODAY. I'LL BE HAPPY TO ANSWER QUESTIONS.

KANSAS LATAs

(LOCAL ACCESS AND TRANSPORT AREAS)

(See page 5 of text)

