

MINUTES OF THE SENATE UTILITIES COMMITTEE

The meeting was called to order by Chairman Jay Scott Emler at 9:30 A.M. on February 21, 2005 in Room 526-S of the Capitol.

Committee members absent: Senator Roger Reitz- excused

Committee staff present: Athena Andaya, Kansas Legislative Research Department
Raney Gilliland, Kansas Legislative Research Department
Bruce Kinzie, Revisor of Statutes' Office
Diana Lee, Revisor of Statutes' Office
Ann McMorris, Committee Secretary

Conferees appearing before the committee: Janet Buchanan, Kansas Corporation Commission
Steve Rarrick, Citizen' Utility Ratepayer Board

Others in attendance: See attached list

Chair continued the hearing on
SB 120 - Telecommunications, regulation thereof, KUSF

Opponents:

Janet Buchanan, Chief of Communications, Kansas Corporation Commission, enumerated the concerns of KCC on the amended language in **SB 120** on (1) depreciation rates; (2) price deregulation of bundled offerings; (3) price deregulation of new services; (4) price cap formula; and (5) determining of KUSF support. (Attachment 1)

Steve Rarrick, staff attorney, Citizens' Utility Ratepayer Board, noted, as written, this bill would completely price deregulate Southwestern Bell and Sprint in every exchange they operate in the State of Kansas, leaving the vast majority of Kansans without any protection against price increases for basic local telephone service. CURB is opposed to **S.B. 120** in its entirety. The price deregulation proposed in **SB 120** is contrary to the public policy set forth in K.S.A. 66-2001 and the mandates set forth in K.S.A. 66-2002 c). He addressed the proposed changes to K.S.A. 66-2005 and K.S.A. 66-2008 separately in order of importance. (Attachment 2)

Written testimony was provided by Patrick Knorr, Sunflower Broadband, Lawrence. (Attachment 3)

Chair closed the hearing on S.B. 120.

Approval of minutes

Moved by Taddiken, seconded by Apple, the minutes of the meeting of the Senate Utilities Committee held on February 17, 2005, be approved. Motion carried.

Adjournment.

Respectfully submitted,

Ann McMorris, Secretary

Attachments - 3

SENATE UTILITIES COMMITTEE GUEST LIST

DATE: FEBRUARY 21, 2005

Name	Representing
JANET BUCHANAN	Kee
Mike Murray	Sprint
Paul Snider	SBC
Debbie Vignatelli	SBC
John Federine	KCTA
Dick Carter	RTG
Nelson Krueger	Everest
Rachel Reiber	Everest
Steve Parrick	CurB
Mike Rea	Dachs Bruder
Anne Spiess	K.T.A.



KANSAS

CORPORATION COMMISSION

KATHLEEN SEBELIUS, GOVERNOR
BRIAN J. MOLINE, CHAIR
JOHN WINE, COMMISSIONER
ROBERT E. KREHBIEL, COMMISSIONER

Testimony of
Janet Buchanan, Chief of Telecommunications
Kansas Corporation Commission

Before the House Utilities Committee
Regarding SB 120
February 16, 2005

Chairperson Emler and Committee Members:

Thank you for allowing me to appear before you this morning on behalf of the Kansas Corporation Commission to express the Commission's views regarding SB 120. My name is Janet Buchanan. I am the Commission's Chief of Telecommunications.

Legislation similar to SB 120 has been introduced in each of the last four legislative sessions. As it has with past proposals, the Commission has several concerns with this bill. While the Commission supports the general movement toward reduced regulation of telecommunications markets as envisioned by the Kansas and Federal Telecommunications Acts, we believe the price deregulation provisions of this bill are still problematic. The Commission is also concerned with the provisions of this bill that pertain to depreciation rates, the price cap formula, and the calculation of KUSF support.

Depreciation Rates

At page 2, lines 2-4, the language of K.S.A. 66-2005(b) is amended to state:

Carriers that elect price cap regulation shall be exempt from: rate base, rate of return and earnings regulations; and regulation of depreciation rates of assets for all regulatory purposes.

While changes in the depreciation rates of a price cap company (SWBT and Sprint) do not have an impact on the rates for local service paid by their customers, this language would prohibit the Commission from examining the appropriate depreciation rate applicable for determination of KUSF support. It would also prohibit the Commission from examining depreciation rates to be used in determination of rates for unbundled network elements (UNEs) that Sprint and SWBT provide to competitors. It is important for the Commission to determine the reasonableness of depreciation rates in these contexts. The Commission could support this language if it did not limit its review of KUSF support and UNE rates.

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Price Deregulation of Bundled Offerings

Beginning at page 5, line 23, the language of K.S.A. 66-2005(f) is amended to exclude services included in bundled offerings from the price cap baskets and price cap regulation. After August 1, 2005, any bundled offerings would be price deregulated. The amended language provides for the specific services contained in the bundles to be available to consumers on an individual basis under the traditional price cap applied to each service.

The Commission understands that price cap companies facing some level of competition would like to have greater flexibility in responding to customer desires. This provision would price deregulate bundled offerings even in those areas served by SWBT or Sprint for which there is minimal competition to discipline the price of the bundle. However, the proposed language still offers some protection for those consumers in such areas. If customers in those areas with little competition were dissatisfied with the price of the bundled offering, those customers could purchase the services individually at rates disciplined by the price cap mechanism. The level of protection offered to consumers in less competitive areas is then dictated by the price cap formula. It should be noted that changes to the price cap formula are proposed on page 6 of this bill. The Commission believes that at least one of the changes to the formula weaken the protections offered by price cap regulation in those areas served by SWBT and Sprint that have little or no competition. While, the reasonableness of the proposed changes will be discussed more fully later, it is pertinent to this discussion to indicate that the Commission finds the proposal of increases of up to 6% for Basket 3 or miscellaneous services to be unreasonable given either the performance of the telecommunications industry or the economy as a whole. This rate of increase is much greater than recent measures of inflation. By permitting the rates for services in Basket 3, such as caller ID, call waiting, etc., to increase by as much as 6%, it is possible that this may also lead to higher bundle prices in those areas with minimal competition. Thus, consumers in these areas may ultimately face increases for discretionary services.

We would also suggest that if this amendment is approved, it be made clear that when services in bundles are removed from Basket 1 or Basket 3, it should be done in a manner that does not have an impact on the existing rates of the services remaining in the respective baskets.

Price Deregulation of New Services

At page 5, line 28, the proposed legislation also excludes new services from rate regulation through price caps. It is unclear what is meant by "new services". However, regardless of the definition, it appears that new services will not be offered individually under price cap as is intended for other services. Therefore, the rates for such services will depend upon the degree of competition. Consumers will not have the opportunity to purchase new services individually under price cap regulated rates. Thus, the protections discussed above will not be extended to new services.

Price Cap Formula

SB 120 amends the language requiring the Commission to develop a price cap formula and examine the formula every five years. At page 6, lines 20-25 the proposed language alters the

formula applied to services in Basket 1 and the proposed language at lines 32-36 alters the formula applied to services in Basket 3.

The Kansas Act established price cap regulation as an option for carriers to adopt. The Act states that Basket 1 would be comprised of residential and single-line business service while Basket 3 would contain multi-line business and discretionary services. Discretionary services are products such as call waiting, caller ID, call forwarding, etc. The Kansas Act required that the initial price cap be set at the rate levels existing when the local exchange carrier applied to elect price cap regulation and at K.S.A. 66-2005(g), required the Commission to determine a formula for adjusting the level of the cap. In developing the formula, the Commission was directed to "balance the public policy goals of encouraging efficiency and promoting investment in a quality, advanced telecommunications network in the state." The Commission opened a generic proceeding to determine a price cap formula. All interested parties were invited to participate. Ultimately, the Commission determined that the price cap should be adjusted according to the following formula:

$$\text{Price Cap Index} = \text{Inflation} - \text{Productivity Offset} + \text{Extraordinary Event Adjustment}$$

Rates would be allowed to increase as costs of the local exchange carrier increase and would be decreased to reflect the effects of increases in productivity. The extraordinary event adjustment would permit adjustment to the price cap to reflect events that changed costs or cost recovery that were beyond the control of the local exchange carrier. After considering the positions of all parties, the Commission found that inflation would be determined by percent change in the Gross Domestic Product Price Index (GDP-PI)(chain-weighted). This index (or the similar Gross National Product Price Index) was utilized by most states and by the FCC at the time. The GDP-PI measures the price level, incorporating all final goods produced within the boundaries of the United States. However, it was generally recognized that the costs in the telecommunications market were rising more slowly than for the economy in general and that the productivity level of the telecommunications market differed from that of the economy in general. Therefore, the productivity offset was established to account for such differences. The Commission determined that the productivity offset should initially be set at 2.3%. K.S.A. 66-2005(g) requires the Commission to review the price cap formula every five years. The Commission reviewed the formula in 2002 and approved a Stipulation and Agreement presented by the parties. The parties agreed to retain the GDP-PI (chain weighted) as the measure for inflation. The parties agreed that the productivity offset for Basket 1 should be set at 3.15% and for Basket 3 it should be set at 1.4%. The price floor is set out in K.S.A. 66-2005(k) as the long-run incremental cost of a service.

The proposed language would replace this system for adjusting the price cap level each year. For Basket 1, the language would apply the change in the telephone service component of the consumer price index (CPI-TS). There are four individual indices relating to telecommunications services – local service, intrastate long distance service, interstate long distance service, and wireless service – and there is an index that combines these individual service categories with certain weights applied. It is not clear if CPI-TS is meant to represent the local service index or if it is the index that is a weighted combination of all telecommunications services. During the Commission's last review of the price cap formula, Sprint's own witness

recommended continued use of the GDP-PI. Dr. Brian Staihr stated that “[u]sing the GDPPI has met the needs of the price cap formula in Kansas, and Sprint can discern no compelling reasons at this point in time to make a change.”¹ However, Dr. Staihr did develop a productivity offset recommendation based on the CPI-TS. In his testimony, Dr. Staihr questioned the ability of the CPI for local services to reflect industry performance. He testified that the CPI for local service has “. . . reflected significant price increases in most recent years, quite possibly due to rate rebalancing that has occurred both here in Kansas and across the U.S. since the passage of the 1996 Telecom Act. As such, those price changes do not, on a stand-alone basis accurately reflect changes in LEC productivity.”² Rate rebalancing, increasing local rates to compensate for reductions in access rates, leads to rates for local services that are higher than would have otherwise been in place in the market absent regulatory actions. Dr. Staihr did indicate that if one examined the CPIs for interstate and intrastate long distance calling, the effect of rate rebalancing may be neutralized. The Commission is concerned that if the CPI-TS referred to in the legislation is index that examines only rates for local service, it will not be reflective of the industry’s performance in the future because the FCC has indicated that it will examine intercarrier compensation in the near future. If the FCC addresses intercarrier compensation then it is likely that rate rebalancing will occur again and a CPI based on local service rates will not reflect the productivity of the industry. However the Commission’s concerns may be alleviated if the CPI-TS contemplated in this bill also includes long distance and wireless rates because the impact of rate rebalancing may be reduced. The following is a comparison of the change in rates permitted under the formula that has been used and what changes would have been permitted had the CPI-TS (for all telecommunications services) had been in place.

Basket 1

Year	% Change Permitted		% Change Using
	SWBT	Sprint	CPI-TS
2004	-1.42%	-1.53%	-2.54%
2003	-1.55%	-1.81%	-1.40%
2002	-0.93%	-0.43%	0.40%
2001	-0.04%	0.02%	0.81%
2000	-0.46%	-0.70%	-1.60%
1999	-1.02%	-0.24% **	-0.60%

** This represents the prorated change permitted for the 2 months affected by the plan

Basket 3

Year	% Change Permitted		% Change Using
	SWBT	Sprint	CPI-TS
2004	0.33%	0.22%	-2.54%

¹ *In the Matter of a General Investigation Into the Price Cap Formula in Compliance with K.S.A. 2000 Supp. 66-2005(f)*, Docket Number 02-GIMT-272-MIS, Direct Testimony of Brian K. Staihr on Behalf of Sprint, filed April 1, 2002, page 5.

² *Id.*, page 10.

2003	0.20%	-0.06%	-1.40%
2002	-0.93%	-0.43%	0.40%
2001	-0.04%	0.02%	0.81%
2000	-0.46%	-0.70%	-1.60%
1999	-1.02%	-0.24% **	-0.60%

** This represents the prorated change permitted for the 2 months affected by the plan

Overall, the formula currently in place and the CPI-TS (for all telecommunications services) would have resulted in similar changes in the price cap. In discussions with Sprint, representatives for the company have indicated that the intent of bill is to apply the CPI-TS that is a combination of all telecommunications services. The language of the bill should be modified to indicate this intent.

For Basket 3 services, the bill proposes that the total basket be adjusted at the discretion of the price cap carrier by an amount that does not exceed 6%. In reviewing the history of price cap adjustments for the two price cap companies we have found that for Sprint the greatest change in the GDP-PI (chain weighted) was 2.32% in 2001; for SWBT, the greatest change in GDP-PI (chain weighted) was 2.26% in 2001. Even before applying the productivity offset, this is somewhat less than the proposed 6%. It is unclear whether this 6% increase includes any adjustment for exogenous events. If it is the intent of this language to include exogenous adjustments within the allowable increase, then it would be appropriate to permit changes greater than the change in inflation; however, 6% is likely to be more accommodating than necessary.

While the Commission understands that carriers under price cap regulation might desire the certainty provided by a fixed method of determining the price cap, it may be prudent to include language to permit the Commission to continue to have jurisdiction to review these measures for reasonableness and propose adjustments as the industry changes if prices appear to be increasing unreasonably.

Price Deregulation

At page 8, beginning on line 1, the bill proposes new language to determine when price deregulation is appropriate. The new language provides for price deregulation when the carrier demonstrates that there is a single carrier providing two-way voice service that can be originated and terminated in the relevant exchange, regardless of technology.

Current Kansas law provides a process for price deregulation of services when the Commission finds that competitive activity can protect consumers by disciplining the pricing of those services. The Commission has permitted price deregulation of services under this statutory process. The Commission has also established a process for achieving greater pricing flexibility, which Sprint has recently taken advantage of for its Garner exchange, which still provides for consumer protection when it is uncertain whether the presence of one competitor is sufficient to discipline the prices of a dominant carrier. This legislation seeks to restrict the discretion of the Commission in determining whether market conditions exist to permit price deregulation through the review of factual evidence. The Commission is concerned that this bill eliminates any discretion of the Commission to determine whether a substitutable service is available to consumers and whether the presence of one competitor is sufficient to discipline prices. It also

eliminates the discretion of the Commission to evaluate if the market has matured sufficiently to assuage concerns regarding "destructive competition." Destructive competition is competition that leads to lower prices for consumers in the short-term but that eliminates competitors from the market and creates the potential for price increases in the long-term.

Sprint has indicated to us that its intent is to apply this new language only in those areas where it faces competition from a cable provider or other facilities-based land line company. However, the proposed language is broad and would permit price deregulation, for example, in the presence of one wireless provider. Even if the intent of the bill is to permit price deregulation if a cable or other facilities-based land line provider is present in an exchange, the Commission has several concerns. The bill strikes the language requiring that the service provided by the competitor be comparable in function and price to the service of the incumbent. Thus, price deregulation can occur without regard to whether the services of the competitor can be a substitute for those of the incumbent. For example, a competitor may provide basic single line business services but not multi-line business services but the bill language would still permit the price deregulation of multi-line business services even though there is not a substitute for such service. Additionally, there is no requirement that competition be present in the entire service area for which price deregulation is sought. Many cable providers do not have service territories that follow the exchange boundaries of Sprint or SWBT. If the presence of a cable provider is used to demonstrate that there is at least one competitor in the exchange, it is possible that there are some customers not served by the cable provider or other land-line competitor. These customers will not have a substitute for the service of Sprint or SWBT and there will be no competition to discipline the price charged to those consumers. One may also question whether sufficient competition exists if the competitor offers only bundled services. Some customers desire only to purchase the basic local service with no discretionary services added on. In some cases, the cable provider utilizes Voice Over Internet Protocol to provide voice services and this requires the customer to also subscribe to broadband services. If price deregulation is permitted to occur in this instance, these customers may have to purchase bundles they do not desire or, since no substitute exists, Sprint or SWBT may increase the rate applied to basic local service.

The bill asserts that carriers providing only "prepaid telecommunications service" will not be considered entities providing two-way voice service. However, "prepaid telecommunications service" is not defined. While the Commission is aware that it is intended to exclude carriers who provide service only to the credit challenged market, technically, all customers prepay for local telecommunications services. The term should be better defined to avoid any future confusion.

KUSF

At page 10, the bill amends K.S.A. 66-2008(c) to state that the Commission should review costs specific to the carrier, including costs associated with the carrier of last resort designation, when reviewing KUSF support. K.S.A. 66-2008(e) requires the Commission to examine embedded costs for rate of return regulated carriers. For price-cap carriers, the Commission has employed a model for determining the costs of an efficient provider to serve customers.

Sprint has stated that its intent is to require the Commission to utilize Sprint specific inputs into the model used for determining its KUSF support. The Commission understands that Sprint

believes its service territory and customers are sufficiently different from SWBT's to warrant a company specific model. Under the current statutes, Sprint can request that the Commission recognize its distinguishing characteristics that impact its cost of providing service. Therefore, the Commission believes the proposed language is unnecessary to achieve Sprint's goal or could be modified to more accurately reflect Sprint's intent.

Also in this section of the bill at lines 22-23, language is included to require the Commission to examine "costs arising from fulfilling carrier of last resort obligations" in the determination of high cost KUSF support. This issue is being addressed before the Court of Appeals. Oral arguments were heard last week. While carrier of last resort costs are separately addressed in K.S.A. 66-2009, there is no indication anywhere in the current statutory framework regarding how such costs should be determined. If carriers are simply required to be ready to serve customers while it is quite possible that the obligation to actually serve may never materialize, this could greatly increase costs for carriers (no matter how such cost is determined) and thus, the size of the fund. For price cap companies whose KUSF support is based on a model, inclusion of such carrier of last resort cost may be particularly speculative without an audit. Additionally, funding for carrier of last resort costs may be in conflict with the requirement that distributions from the KUSF be made in a competitively neutral manner unless that support is also portable to competitive carriers.

Thank you for the opportunity to appear today to express the Commission's concerns regarding SB 120. I am willing to answer questions at the appropriate time.

Citizens' Utility Ratepayer Board

Board Members:

Gene Merry, Chair
 A.W. Dirks, Vice-Chair
 Francis X. Thorne, Member
 Nancy Wilkens, Member
 Carol I. Faucher, Member
 David Springe, Consumer Counsel



State of Kansas
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Testimony on Behalf of the Citizens' Utility Ratepayer Board
 By Steve Rarrick, Staff Attorney
 Before the Senate Utility Committee
 Re: Senate Bill 120
 February 16, 2005

Chairman Emler and Members of the Committee:

Thank you for the opportunity to offer testimony on behalf of the Citizens' Utility Ratepayer Board (CURB) in opposition to Senate Bill 120. My name is Steve Rarrick and I am a Staff Attorney with CURB.

CURB is opposed to Senate Bill 120 in its entirety. As written, this bill would completely price deregulate Southwestern Bell and Sprint in every exchange they operate in the State of Kansas, leaving the vast majority of Kansans without any protection against price increases for basic local telephone service.

Basic local service, sometimes called "POTS" (plain old telephone service), is the cornerstone of the telecommunications industry and is the service that the poor, the elderly, and most Kansans use for contacting doctors, schools, and friends and family. Basic local service is the primary service in the definition of universal service in K.S.A. 66-1,187 (p), and is a service that must not be price deregulated.

The public policy of the State of Kansas regarding telecommunications was stated by the Legislature in K.S.A. 66-2001:

"It is hereby declared to be the public policy of the state to:

- (a) Ensure that every Kansan will have access to a first class telecommunications infrastructure that provides **excellent services at an affordable price;**
- (b) ensure that consumers throughout the state realize the benefits of competition through increased services and improved telecommunications facilities and infrastructure **at reduced rates;...**"
 (emphasis added)

The Kansas legislature recognized the importance of universal service by ordering the Commission to initiate a proceeding to adopt guidelines to "ensure that all telecommunications carriers and local exchange carriers *preserve and enhance universal*

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service, protect the public safety and welfare, ensure the continued quality of telecommunications services and *safeguard the rights of consumers*” K.S.A. 66-2002 (c) (emphasis added). As testament to the importance of universal service, Kansans currently fund the Kansas Universal Service Fund (KUSF) by over \$60,000,000 annually primarily to “preserve and enhance” universal service in Kansas.

The price deregulation proposed in Senate Bill 120 is contrary to the public policy set forth in K.S.A. 66-2001 and the mandates set forth in K.S.A. 66-2002 (c). Without price cap regulation of basic local service, the State will not be ensuring that (1) every Kansan will have access to *excellent services at affordable prices*, (2) consumers throughout the State will realize the benefits of competition through increased services and improved facilities and infrastructure *at reduced rates*, or (3) that local exchange carriers *preserve and enhance universal service and safeguard the rights of consumers*. These public policies and priorities simply cannot be met with the wholesale price deregulation proposed in Senate Bill 120.

I will address the proposed changes to K.S.A. 66-2005 and K.S.A. 66-2008 separately below, in order of importance:

66-2005 (p), page 8, lines 1-28 (total price deregulation)

- This proposed amendment *requires* the Commission to price deregulate Southwestern Bell and Sprint in any exchange in which there is “at least one” other carrier or “entity” providing basic local telephone service (broadly defined) to residential or business customers in the exchange. Under this proposal, all Southwestern Bell and Sprint exchanges will be price deregulated, since there is currently a wireless, cable, or VOIP provider in portions of every exchange in which they operate.
- The single carrier or entity triggering price deregulation under this section can be a cable, VOIP, or wireless provider that does not provide ubiquitous service throughout the exchange in question. This amendment would remove price caps protecting Kansans from unreasonable price increases in basic local service simply because a VOIP or cable company provides service to a limited number of customers in the exchange, even though these providers do not offer basic service to many or perhaps even most customers in the exchange. If passed, this bill will leave thousands of Kansans with price deregulated local service in Southwestern Bell and Sprint exchanges, even though they may have no alternative provider.
- The single carrier or entity triggering price deregulation in this section (cable or wireless) typically charges substantially more than the basic service offered under the current price capped services, resulting in price deregulation that would allow Southwestern Bell and Sprint to raise prices rather than lower them to meet competition.
- Once deregulated, Southwestern Bell and Sprint may adjust their rates for any of their

services *upward* or downward as they deem fit. This means they can lower their rates for those fortunate ratepayers within the exchange where a competitor actually provides service at lower prices, and increase rates for those outside that area but within the same exchange, regardless of the reasonableness or affordability of those rates, since price discrimination will not be prohibited in this price deregulated environment.

- There is no need for price deregulation to allow Southwestern Bell and Sprint to lower prices to meet competition. The current regulatory environment allows carriers to seek approval to create Competitive Sub-Baskets for pricing flexibility required by actual competition. Sprint recently filed an Application for a Competitive Sub-Basket for its Gardner Exchange on December 22, 2004, and the Commission approved the Competitive Sub-Basket on January 27, 2005, in KCC Docket No. 05-UTDT-542-MIS. This swift approval of Sprint's request for a Competitive Sub-Basket demonstrates that the price deregulation proposed in Senate Bill 120 is simply unnecessary, as the current regulatory scheme accommodates the needs of the local carrier while protecting ratepayers and competitors alike. Sprint's application was not opposed by CURB and the application was approved 36 days after the application was filed.

The Competitive Sub-Baskets were established and authorized by the Commission in Docket No. 94-GIMT-478-GIT to:

“provide greater flexibility to the LEC while simultaneously providing protection against cross-subsidization of competitive service losses or price reductions. This plan allows effective responses by competing firms within the telecommunications industry without disturbing the balance between consumer interests and competing providers. In determining this [sub-basket plan], the Commission has balanced the public policy goals of encouraging efficiency and promoting investment in a quality, advanced telecommunications network in the state of Kansas.”¹

This process allows local carriers to lower prices to compete with other carriers, while maintaining the price cap to assure affordable rates for basic telephone service and ensuring that rates in other exchanges cannot be increased to offset revenue losses in the competitive exchange. Competitive carriers are likewise protected by Commission regulation that prohibits the local exchange carrier from charging rates below the long-run incremental cost. Eliminating these regulatory protections would cause both immediate and long-term harm to consumers and competitors.

- CURB urges the Committee to reject this proposal to completely price deregulate basic phone service in Kansas.

¹ *In the Matter of a General Investigation Into Competition within the Telecommunications Industry in the State of Kansas*, Order, ¶ 140 (December 27, 1996).

66-2005(f), page 5, lines 23-30 (price deregulation for new or bundled services)

- This proposed amendment price deregulates any new telecommunications service or bundled offerings offered after August 1, 2005. If the proposed amendment to 66-2005(p) discussed above is passed, this provision would have no application, since all price capped basic local service would be price deregulated without this amendment.
- The proposed amendment contains no definition for “new telecommunications service.” This could result in existing basic local service being redefined and introduced as a new service, resulting in price deregulated basic local service.
- There is no need for price deregulation to allow Southwestern Bell and Sprint to lower prices to meet competition, as current regulatory procedures allow price cap carriers to seek approval to create Competitive Sub-Baskets for pricing flexibility required by actual competition.
- CURB urges the Committee to reject this proposal.

66-2005(g), page 5, lines 41-43, page 6, lines 1-25 (removal of Commission authority over price cap formula)

- This proposed amendment would replace the current price cap formula methodology utilized by the Commission, whereby they receive and weigh expert testimony and evidence on extremely technical issues related to consumer price indices and productivity factors. The amendment instead seeks to have the Legislature specify an index (CPI-TS) without any consideration of the complex issues involved with the selection of an appropriate price index. CURB would submit that this issue is best left to the expertise of the Commission.
- CURB is also somewhat perplexed by this proposal. In the last price cap docket (KCC Docket No. 02-GIMT-272-MIS), Sprint supported the use of the GDPPI consumer price index currently utilized by the Commission. Specifically, one of Sprint’s witnesses testified that, “Using GDPPI has met the needs of the price cap formula in Kansas, and Sprint can discern no compelling reasons at this point in time to make a change.”² CURB is likewise unable to discern any compelling reason at this point in time to make a change. If any such compelling reasons arise, CURB submits that the opportunity to offer evidence on the issue is available under current Commission rules, and the Commission is authorized to receive, weigh, and act upon such evidence.
- CURB urges the Committee to reject this proposal.

² *In the Matter of a General Investigation into the Price Cap Formula in Compliance with K.S.A. 2000 Supp. 66-2005(f)*, KCC Docket No. 02-GIMT-272-MIS, Direct Testimony of Brian K. Staihr, , p. 5 lines 4-6.

66-2005(i), page 6, lines 32-36, and 66-2005(f), page 5, lines 36-40 (automatic annual 6% increase in price cap for miscellaneous services)

- These proposed amendments replace the annual adjustment to the price cap established by the Commission for the miscellaneous services basket with a statutory right for Southwestern Bell and Sprint to increase the prices for these services 6% each year. The miscellaneous services basket is comprised of business lines as well as vertical services for all lines, residential and business.
- This bill is giving Southwestern Bell and Sprint the ability to raise the price of business lines and vertical services for all lines by 6% each year. While CURB has no way of knowing how the proponent of this bill arrived at 6%, the amount is excessively high and cannot be justified.
- A similar provision exists in Missouri, and local exchange providers are allowed to “bank” the guaranteed percentage provided for each year, which means if the full increase is not taken in one year it can be added to the next year’s percentage. CURB urges this Committee to reject this proposal along with all of the provisions of Senate Bill 120. However, if the Committee decides to recommend passage of any of the proposed amendments, CURB urges the Committee to treat miscellaneous services the same as the residential and single line business services. In no event should carriers be able to bank allowable increases in the price cap to enable them to use them in future years.
- CURB urges the Committee to reject this proposal.

66-2005(b), page 2, lines 3-4 (exempting regulation of depreciation rates of assets)

- This proposed amendment would remove Commission authority to regulate the depreciation rates of assets for price cap carriers. Depreciation is a major cost component for telecommunications carriers, and has a substantial impact on KUSF funding and the pricing of UNEs determined by the Commission. The elimination of the Commission’s authority to regulate depreciation with regard to KUSF and UNE pricing is likely to result in an increase in KUSF funding to these carriers as well as increased UNE pricing, without any Commission oversight.
- CURB urges the Committee to reject this proposal.

66-2008(c), page 10, lines 19-23 (KUSF review must use costs of individual carriers receiving funds from the KUSF, including costs of fulfilling carrier of last resort obligations)

- CURB sees no reason to change the existing KUSF review process and would urge the Committee to reject this proposal.

CONCLUSION

The fundamental problem with the price deregulation proposed in Senate Bill 120 is that it is premised on the assumption that the existence of one alternative carrier in an exchange constitutes competition in that exchange. This premise is simply not supportable.

Contrary to what you may have heard from the major local exchange carriers today and earlier this session, meaningful competition has not arrived for local telephone service in Kansas or elsewhere in the nation. The FCC recently acknowledged that the state of competition in the local market does not share the competitive conditions present in the wireless and long distance markets:

“The local services market does not share the competitive conditions, observed in the mobile wireless services market and long distance services market, that would support a parallel finding that the costs of unbundling outweigh the benefits. In contrast to its conclusions regarding competition in the mobile wireless services and long distance services markets, the Commission has not reached similar competitive conclusions about the core markets traditionally served by local exchange carriers.”³

The Kansas Corporation Commission likewise recently noted that competition in the local telephone market is just beginning, and that “if the Legislature’s goal of competition is realized, *eventually* the local telecommunications market *will be fully competitive*.”⁴

Price deregulation of basic local telephone service will remove the regulatory protections that ensure affordable basic local service to Kansans, including the poor and elderly, contrary to the public policy set forth in K.S.A. 66-2001 and the mandates set forth in K.S.A. 66-2002 (c). This price deregulation will also harm competition in the local market before it has the opportunity to develop, resulting in less choices and uncontrolled prices for basic local telephone services with little or no recourse for consumers.

On behalf of CURB, I urge you to vote against Senate Bill 120. I would be happy to answer any questions at the appropriate time.

³Order on Remand, ¶38, *In the Matter of Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, WC Docket No. 04-313, CC Docket No. 01-338 (Released, February 4, 2005).

⁴Order 18, ¶ 49,56, *Establishing Policy for Win, Winback, and Retention Offerings by Incumbent Local Exchange Carriers, In the Matter of a General Investigation into Winback/Retention Promotions and Practices*, KCC Docket No. 02-GIMT-678-GIT, (April 2, 2004) (emphasis added).

Testimony of
Patrick Knorr, General Manager
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785-841-2100
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Before the Senate Utilities Committee
Regarding SB 120
February 16, 2005

Chairman Emler and Committee Members:

Thank you for the opportunity to provide written testimony on behalf of Sunflower Broadband located in Lawrence, Kansas. My name is Patrick Knorr. I am the General Manager for Sunflower Broadband. As you will recall from my testimony previously before this committee, Sunflower Broadband is a facilities-based provider of local exchange telecommunication service, cable service and high-speed Internet service. All of these services are distributed through a hybrid fiber coaxial plant owned by Sunflower Broadband.

For the past several years, legislators have listened to hours of testimony regarding ways to achieve a competitive telecommunications market. You have heard that ILECs are losing significant market share to CLECs and without price deregulation legislation they are at a competitive disadvantage. I'm not submitting testimony to debate what company or technology has a competitive advantage or disadvantage. Our company has invested its own dollars to provide quality telecommunications services and fully understands that the competitive arena is changing. As a cable company providing telecommunications services, we are not advocating more regulation. However, we strongly believe that SB 120 is a piece-meal approach to a changing telecommunications environment and therefore, stand in opposition of the bill.

SB 120 is another attempt to deregulate pricing without looking at all facets of providing competitive telecommunications services. Our concerns are as follows:

- Passage of SB 120 will deregulate pricing in all ILEC exchanges because there is at least one competitor in every exchange. Because a wireless service is available throughout the state, this criterion alone would allow SBC and Sprint to deregulate all local telephone service.
- Pricing deregulation would occur in all exchanges where competitors have introduced competitive services, but have not established sustainable competition.
- Language in this bill will allow bundled services or any new telecommunications service offered after August 1 to be price deregulated.

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This is additional language to accomplish total price deregulation. In addition, products within bundles will be funded by consumers in areas where the same bundle and/or pricing is not available.

- Deregulating telecommunications services by placing them in a bundled package does not create an effective competitive arena. For example, satellite video is not subject to the same local taxation and franchising requirements as video services provided by cable companies, therefore allowing more flexibility on promotions. Bundling satellite video with deregulated telecommunications services further widens the gap of competitors' abilities to offer consumers effective choices in communications service.

Sunflower Broadband is ready to meet the challenges of providing competitive services if all issues of competition are considered. If the goal of legislation is to structure competition so that consumers can benefit from numerous competitive choices, then passage of a bill targeted only on pricing deregulation is not the answer. Consideration needs to be given to all aspects of providing competitive services, not just the pricing aspect. The list is long of areas to study regarding a full competitive arena. The following are examples of items that need to be fully understood before changing the telecommunications environment:

- The affects of new FCC rules which were recently released regarding UNEs and access to the ILEC network
- The affects of newly announced mergers and acquisitions and what impacts they have on competitors
- Whether or not new legislation can be passed that allows competitors to stay in the market to establish sustainable long-term choices for customers
- The affects of legislation on KUSF
- Other aspects of providing competitive services, such as Interconnection to the PSTN, (current interconnection agreements with ILECs are now in arbitration with no decisions scheduled until after this legislation session adjourns) access to apartment complexes, and more.

Because of the complexities of all aspects of the competitive environment and because SB 120 is focused mainly on one – price deregulation – we oppose the bill. Unraveling a protected monopoly of 100 years cannot be achieved by price consideration only.

Because the issues include a scope larger than just pricing and bundling, we would support the development of a task group comprised of legislators, regulators and industry personnel to provide insight on the over-all goal of providing consumers choices in services, pricing and technology.

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