

MINUTES OF THE SENATE UTILITIES COMMITTEE

The meeting was called to order by Chairman Pat Apple at 9:30 A.M. on February 19, 2008 in Room 526-S of the Capitol.

Committee members absent: Sen. Emler (excused)

Committee staff present: Raney Gilliland, Kansas Legislative Research Department
Cindy Lash, Kansas Legislative Research Department
Mike Corrigan, Revisor of Statutes
Ann McMorris, Committee Secretary

Conferees appearing before the committee:

Mike Murray, Embarq Corporation
Don Low, KCC
Steve Rarrick, CURB

Others in attendance: See attached list

Chair opened the hearing on

SB 570 - Kansas universal service fund, exemptions for certain local exchange carriers.

Proponent:

Michael R. Murray, Embarq Corporation, stated **SB 570** would facilitate potential mergers and acquisitions by allowing transactions involving price cap regulated companies to proceed without KCC approval. **SB 570** will not affect KCC's current authority to monitor the service quality of price cap regulated companies. (Attachment 1)

Questions concerning non-competitive areas and portions under regulation.

Opponents:

Don Low, Kansas Corporation Commission, testified that **SB 570** basically would exempt price-cap local exchange companies from Commission review of acquisitions of utilities under two statutes, K.S.A. 66-127 and 66-136. He voiced concern about the consequences for competition that need to be reviewed. (Attachment 2)

Questioned whether companies seeking financial gain only had been in Kansas. Also questioned time period involved in mergers and acquisition. KCC accountant indicated 3 months for some and 10 months for others.

Steve Rarrick, staff attorney, Citizens' Utility Ratepayer Board, CURB opposes **SB 570** because eliminating KCC review and approval of acquisitions and mergers will leave Kansas ratepayers at risk for: (1) significant local rate increases; (2) loss of extended area service (EAS) calling and the associated additional long distance charges; and (3) decreased or inadequate service quality. (Attachment 3)

Questions regarding FCC involvement. Senator Lee requested of KCC a list of communities with competitors and who the competitors are and a list of non-competitive communities. KCC will compile.

Chair closed the hearing on **SB 570**.

Adjournment.

Respectfully submitted,

Ann McMorris, Secretary

Attachments -3

SENATE UTILITIES COMMITTEE GUEST LIST

DATE: FEBRUARY 19, 2008

Name	Representing
Linda Yonon	RTS
Shawn Atkins	Nex-Tech
Kari Presley	Hearney & Associates
Mike Murray	Embarg
Mark Harper	Embarg
Sam Foreman	Embarg
Steve Karauk	Emb
Colleen Jensen	Cox
Tom Gantner	AT&T
Nelson Krueger	LEL
Dean Hays	Praga, Smith
Emily Guir	Hein Law Firm

Before the Senate Utilities Committee
SB 570
Michael R. Murray, Embarq Corporation
Tuesday, February 19, 2008



Mr. Chairman and Members of the Committee:

Thank you for the opportunity to discuss the provisions of SB 570 which would no longer require the Kansas Corporation Commission (KCC) to approve mergers and acquisitions of price cap telecommunications companies. In Kansas this would cover Embarq and AT&T.

In today's competitive telecommunication's environment consolidation of telecommunications companies will both continue and likely increase. Only through increased effectiveness and efficiency can telecommunications companies deliver the quality customer service and an increasingly broad set of services that customer's demand.

SB 570 would facilitate potential mergers and acquisitions by allowing transactions involving price cap regulated companies to proceed without KCC approval and thus facilitate the benefits to Kansas consumers without the risk of undue delay that can potentially increase financing and acquisition costs. Numerous states have taken, or are taking, similar actions. Kentucky recently acted on this issue and there is pending legislation in Tennessee. Other states Embarq serve don't require commission approval. They include North Carolina, Texas, Indiana and Oregon.

While we recognize the KCC has a valid and important role to assure consumers are protected from absorbing expenses associated with mergers and acquisitions that role is simply not necessary under price cap regulation. Under price cap regulation, telecommunication's consumers are protected from increasing rates due to transactions because of the price cap on rates.

Another appropriate role of KCC is to assure that quality telecommunications services are available to Kansas consumers. SB 570 will not affect the KCC's current authority to monitor the service quality of price cap regulated companies and mandating improvement where necessary. The KCC's involvement in mergers and acquisitions is another example of regulatory policy written in the age of monopoly telephone companies when consumers needed protections.

The pace and impact of competition from wireless carriers and VoIP service over cable systems is significant and increasing. Recognizing the impact competition has on the need for less regulation, Kansas statutes have recently been changed, and may change again this year, to allow greater freedom to telephone companies to respond. Correspondingly, Kansas price cap regulated telecommunications companies which have multi-state operations, should have the discretion to conduct these types of transactions quickly and without the risk of increased costs and delay due to unneeded regulatory oversight.

Respectfully, we ask that the Committee act favorably on SB 570.

I'd be pleased to respond to questions.

Senate Utilities Committee
February 19, 2008
Attachment 1-1

Before The Senate Utilities Committee
Presentation of the Kansas Corporation Commission
February 19, 2008
SB 570

Thank you, Chairman and members of the Committee. I am Don Low, Director of the Utilities Division for the Kansas Corporation Commission. I appreciate the opportunity to testify for the Commission on SB 570. This bill basically would exempt price-cap local exchange companies from Commission review of acquisitions of utilities under two statutes: K.S.A. 66-127, dealing with acquisition of stocks or indebtedness by a competing utility, and K.S.A. 66-136, concerning transfers of certificates of convenience or agreements affecting such certificates. It's unclear whether the bill would totally exempt a transaction from KCC review if a price-cap company were either the seller or buyer. In any event, the Commission opposes the bill.

Commission review of acquisitions and mergers is necessary and desirable to ensure that such transactions do not have an adverse impact on the utilities' services or rates. There is a possibility that an acquiring entity may not have a goal of providing sufficient and efficient service, as required by Kansas statutes, but be primarily interested in short term profits from deal-making. Additionally, the acquiring entity may very well not have the technical, managerial or financial ability to provide the needed services. Certainly, without the prospect of Commission review, the selling utility has the incentive to screen prospective buyers primarily for their size of their purchase bids and not whether they are motivated and competent to provide service.

Commission review is also needed because there could be concerns about the consequences for competition that need to be reviewed. The Commission has not attempted to do a rigorous review of competitive impacts when the Kansas piece is part of a national transaction subject to federal review. However, if the transaction is a local rather than national transaction, KCC review of competitive impacts may be necessary. I should also note that the Commission frequently uses acquisitions as an opportunity to review service or other needs or to address other issues. For instance, the acquiring company may agree that new services such as broadband service should be made available in the area.

There is no evident reason why local exchange companies that have chosen price-cap regulation should be exempt from KCC review, either as the seller or buyer. The fact that individual rates of the company are not regulated does not affect potential impacts on the financial, technical, managerial and other aspects of a company's operations and services.

Thank you for your attention. I will be happy to answer questions. Jeff McClanahan, Chief of the Division's Accounting and Financial Analysis Section, is also here if you have questions about prior transactions involving Sprint and Embarq since I did not participate in such cases.

Citizens' Utility Ratepayer Board

Board Members:
Gene Merry, Chair
Randy Brown, Vice-Chair
Carol I. Faucher, Member
Laura L. McClure, Member
A. W. Dirks, Member



State of Kansas
Kathleen Sebelius, Governor

David Springe, Consumer Counsel
1500 S.W. Arrowhead Road
Topeka, Kansas 66604-4027
Phone: (785) 271-3200
Fax: (785) 271-3116
<http://curb.kansas.gov>

Testimony on Behalf of the Citizens' Utility Ratepayer Board
By Steve Rarrick, Staff Attorney
Before the Senate Utility Committee
Re: Senate Bill 570
February 19, 2008

Chairman Emler and Members of the Committee:

Thank you for the opportunity to appear before you this morning on behalf of the Citizens' Utility Ratepayer Board (CURB) to testify in opposition to Senate Bill 570. My name is Steve Rarrick and I am an attorney with CURB.

Senate Bill 570 proposes to eliminate the authority of the Kansas Corporation Commission (KCC) to review and approve acquisitions and mergers involving price-cap local exchange carriers under K.S.A. 66-127 and K.S.A. 66-136. K.S.A. 66-127 addresses the acquisition of stocks or indebtedness by a competing utility/carrier, and K.S.A. 66-136 addresses the assignment or transfers of certificates of convenience or agreements affecting such certificates.

CURB opposes Senate Bill 570 because eliminating KCC review and approval of these transactions will leave Kansas ratepayers at risk to potential rate increases, loss of extended area service (EAS) calling and associated additional long distance charges, and poor service quality and customer service. Continued oversight by the KCC over these transactions is necessary to ensure consumers aren't negatively affected by an acquisition or merger.

Under the existing provisions of K.S.A. 66-127 and K.S.A. 66-136, the KCC is authorized to review acquisitions and mergers involving local exchange carriers, including price cap regulated carriers. Typically, Commission review of these transactions involves consideration of the public policy requirements of K.S.A. 66-2001. The KCC also determines whether the transaction is in the public interest by examining the competitive impact of the transaction, the impact on customers, continuity of service, the financial viability of the companies, and the companies' managerial, technical, and financial qualifications.

Removing KCC oversight of these transactions will place consumers at risk for the following:

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Attachment 3-1

- **Significant local rate increases** for customers in the acquired exchange and in the acquiring company's existing exchanges. Rate increases can result from numerous issues involved in acquisitions and mergers, including but not limited to the following:
 - The company acquiring the exchange has higher rates in its existing exchanges and the company wishes to implement its rate structure in the acquired exchange.
 - The company acquiring the exchange pays an acquisition premium (the amount paid in excess of the net book value for the plant acquired) and wishes to recover the acquisition premium in rates. For example, if a company pays three times net book value for an exchange, the company will record the actual plant in an assets account and put the amount in excess of plant in a deferred charge account that it seeks to recover via increased rates. The company may seek to recover the goodwill amounts in price caps or via an "exogenous" adjustment, or in the company's next rate case if the acquiring company is rate of return regulated.
 - The company acquiring the exchange may be taking on more debt than it can afford or put its credit rating at risk, which may result in rate increases because the acquiring company could not afford the acquisition.
- **Loss of extended area service (EAS) calling and the associated additional long distance charges** for customers in an acquired exchange when the purchasing company does not wish to honor EAS calling for the acquired exchange. Customers would then face increased and additional long distance charges instead of paying local rates for these calls.
- **Decreased or inadequate service quality** provided by the new company, which may not be financially able to maintain existing service quality for customers in the acquired exchange. A sale of an exchange may even put the acquiring company's existing customers in jeopardy regarding service quality if the acquisition requires more capital than the company can afford, which may require internal capital budget cuts in maintenance and repairs and related plant. While decreasing expenses and replacement of plant may allow the acquiring company to pay the cost of the acquisition, it can lead to increased complaints and service quality problems for its new and existing customers.

CURB is unaware of any rational reason that would justify exempting local exchange companies electing price cap regulation from KCC review of acquisition and merger transactions. Price cap carriers are not statutorily precluded from returning to rate of return regulation, so a carrier's current price-cap status provides insufficient rationale to eliminate the important consumer protections provided by KCC review of these transactions.

On behalf of CURB, I urge the Committee to vote against passage of Senate Bill 570 in its entirety.