

# Case Closed

## Verizon, Inc., BellSouth Telecommunications, Inc., and Sprint-Florida Inc.

Verizon Inc. (Verizon), BellSouth Telecommunications, Inc. (BellSouth), and Sprint-Florida Inc. (Sprint-Florida), asked the Florida Public Service Commission (Commission) to restructure their rates for access services and basic local telecommunications services. The Commission subsequently approved the telecommunication providers' "rate rebalancing" petitions, but was challenged by numerous intervenors. The Florida Supreme Court issued a ruling in July 2005 affirming the Commission's original decision to allow the three local telephone companies to rebalance their rates.

### NERA's Role

NERA Special Consultant Dr. Kenneth Gordon and Senior Vice President Dr. William Taylor filed direct testimony before the Florida Commission in August 2003. Dr. Gordon filed rebuttal testimony in November 2003 and was cross-examined in hearings before the Commission. Dr. Gordon was asked to provide an economic and policy analysis of the rate plans and to determine if those plans met the public policy criteria laid out in Florida's public utility statutes. As an economist and former Chairman of regulatory commissions in Massachusetts and Maine, Dr. Gordon reviewed the applicable statutes, companies' plans, and the cost evidence submitted by the companies' witnesses. Dr. Taylor discussed economic issues arising from the then newly-created statutes on competitive market enhancements, price floors, and reduction of intrastate switched access prices to parity with interstate price levels.

NERA witnesses have testified on telecommunication competition issues—such as rate rebalancing—on numerous occasions and published their findings. For example, Dr. Agustin Ros and Dr. Karl McDermott wrote a chapter of a book entitled "Are Residential Local Exchange Prices Too Low?: Drivers to Competition in the Local Exchange Market and the Impact of Inefficient Prices," which examines and empirically tests the impact that unique, regulatory induced features of local exchange markets may have on the development of local exchange competition.<sup>1</sup>

### The Expert Evidence

In Florida, Dr. Gordon presented evidence that demonstrated that basic local prices were receiving a subsidy from other services. Good policy requires weighing and balancing the costs and benefits of particular actions. Maintaining the current prices of incumbent local telephone companies can have real effects on the emergence of competition at the local level. Thus, there is a real cost to continuing the status quo. Dr. Gordon explained that the deployment of next-generation advanced networks depends crucially on providing all market participants with sound economic signals that encourage efficient investment and innovation. Cost-based prices provide the incentives needed to bring to market the new services that customers demand. Dr. Gordon explained that the companies' plans would not result in the "rate shock" as some of the intervenors had predicted.

Dr. Taylor presented economic evidence on the need for rebalancing rates in order to encourage greater competitive entry and to reduce the persistent unevenness of entry into Florida's local exchange markets. Rate rebalancing of the form envisioned by Florida's newly-enacted "rate rebalancing" statutes would improve incentives for competitive entry into these markets and lead to more efficient prices for residential basic telephone services and switched access services. Dr. Taylor concluded that this would greatly benefit consumers and local exchange competition alike.

<sup>1</sup> See: *Expanding Competition in Regulated Industries*, pp 149–168, edited by Michael Crew, Kluwer Academic Publishers (2000).

### Favorable Ruling for NERA's Clients

The Florida Supreme Court agreed with the findings of Dr. Gordon and Dr. Taylor, ruling in favor of Verizon, BellSouth, and Sprint-Florida.

The Florida Supreme Court decision, dated July 7, 2005, states:

Dr. Kenneth Gordon, an economist and former chairman of the Maine Public Utilities Commission and the Massachusetts Department of [Public] Utilities, testified that the outcomes sought by the petitions will result in increased economic activity, enhanced service offerings, including new, more affordable technologies, and decreased long distance rates.

The Supreme Court of Florida agreed with Dr. Gordon's findings, stating that:

In light of the foregoing evidence cited by the Commission and present in the record of the proceedings below, we conclude that the Commission's determination that its grant of the petitions will create competition to the benefit of residential consumers ... is supported by competent, substantial evidence....

We further conclude that the Commission's determination that its grant of the petitions will "[i]nduce enhanced market entry," is supported by competent, substantial theoretical and empirical evidence.... For example, Drs. Gordon,

Mayo, and Andy Banerjee, an economist, testified that the removal of support for basic local telecommunications rates will induce market entry. Dr. Gordon explained that new competitors entered the market in response to similar basic local telecommunications rate changes in Maine and Massachusetts.

The Court agreed that local subscribership was not adversely affected by local telephone rate increases comparable to those proposed by the instant petitions, explaining that:

Dr. Gordon's opinion that "basic residential local rates ... will be just as affordable to Florida customers as before," was based on his observations that the ILECs' (incumbent local exchange carriers) current basic local telecommunications rates are well below the national average and that the local rate increases will be offset by decreases in long distance rates.

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## About NERA

Founded in 1961 as National Economic Research Associates, NERA Economic Consulting is an international firm of economists with practical experience creating strategies, studies, reports, expert testimony, and policy recommendations reflecting our specialisation in industrial and financial economics. Our global team of more than 500 professionals operates in offices across North and South America, Europe, Asia, and Australia.

For a complete listing of offices and practice areas, please visit [www.nera.com](http://www.nera.com).

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## Our Experts Involved in the Case

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