Other Provisions

Q. Let's move to the next section of your testimony. Could you please briefly discuss the provision in the Joint Stipulation that calls for the creation of a new basket and the transfer of certain services between baskets?

A. Yes. The market for telecommunications services is gradually becoming more competitive. Price cap regulation is designed to provide carriers with the flexibility to adapt to this changing environment, while continuing to provide customers with protection from potential abuse of the carrier's remaining market power. This balance between pricing flexibility and protection from monopoly power is achieved by grouping services into categories or "baskets," and providing an appropriate degree of pricing flexibility within each basket. As markets evolve, it is reasonable to move services between baskets, or to create new baskets, in order to ensure that the carrier is given sufficient (but not excessive) pricing flexibility.

The Joint Stipulation calls for a new Non-Basic1.5 Service Category comprised of services that would be moved from the existing Non-Basic1 basket. These services are considered to be more competitive than those that would remain in Non-Basic1 but less competitive than those in Non-Basic2. This group includes services like data communications equipment, PathLink, and intraLATA message toll service. If this change is approved, the new Non-Basic1.5 basket will include services that accounted for 50% of the 1998 annual revenues from the existing Non-Basic1 basket.

The Joint Stipulation also calls for moving a sub-group of services from Basic to Non-Basic1. These services accounted for approximately 11% of 1998 Basic revenues. When the existing Plan was adopted in 1996, prices for this sub-group of services were not constrained to the same degree as the remainder of the services in the Basic category. Moving these services to Non-Basic1 is a further step toward providing BellSouth with additional flexibility in pricing these services. Finally, I would note that while the Joint

Stipulation calls for moving some services to other baskets, the rate element constraints within the baskets will remain unchanged.

Q. Are the proposed reclassifications reasonable?

A. Yes. These changes will provide BellSouth with additional pricing flexibility, without giving it complete pricing freedom. This is a reasonable step to take, given the trend towards increased competition, particularly since it will provide an opportunity to observe how BellSouth uses this additional flexibility prior to the time when the entire plan is reviewed.

Q. Could you please briefly discuss the infrastructure improvements BellSouth will make as a part of the Joint Stipulation?

A. Yes. BellSouth has agreed to invest $97.5 million towards deployment of Asymmetrical Digital Subscriber Line ("ADSL") technology in North Carolina. This represents an addition of $60 million to BellSouth's previous investment plans and a net additional cost to BellSouth of $15 million annually over ten years. ADSL will be installed in 93 central offices and over 2,100 remote sites across the state. Although the additional investment will undoubtedly generate additional revenues, this commitment ensures that this advanced technology is rapidly deployed throughout BellSouth's North Carolina service area, regardless of whether or not it is fully profitable in a particular area.

Q. Will consumers benefit from more rapid deployment of ADSL?

A. Yes. North Carolina consumers will benefit in three ways. First, the infrastructure improvements will be widely spread across the state, including areas where the potential revenues alone wouldn't necessarily be sufficient to encourage BellSouth to invest in this advanced technology. For example, the Joint Stipulation provides for deployment of ADSL in 93 central offices; eleven of these have been identified as being in economically disadvantaged areas. [Joint Stipulation, p. 9] Individuals, families, and businesses that might not have otherwise gotten access to high speed services will gain this opportunity as a result of the Joint Stipulation.

Second, rapid deployment of ADSL will help meet the ever-growing demand for bandwidth by both business and residential consumers. The Internet is revolutionizing the way consumers stay in touch with each other, obtain information, and do business. For downloading software, graphics and other data-intensive files from the Internet, a typical 56K dial-up modem is often far from optimal. Customers are increasingly seeking faster alternatives; ADSL provides an inexpensive, efficient alternative. While the transmission speeds vary depending upon the specific DSL technology, and the distance from the customer's location to the nearest wire center or fiber optic connection, ADSL will typically provide download speeds of 1.5 to 6.1 Mbs. Even the low end of this range provides downstream transmission that is more than 25 times faster than 56K dial up modems.

Third, the investment which is mandated by the Joint Stipulation may ultimately lead to additional investments in DSL-type technology by other carriers (both incumbents and competitors), as well as additional investments by BellSouth in other parts of the state. DSL technology provides enormous amounts of bandwidth at very reasonable cost, while relying to a great extent on the existing infrastructure (e.g. copper cable). However, the benefit of this technology may be delayed by a "chicken and egg" dilemma: costs will remain relatively high until a substantial level of market penetration is achieved, but a high level of penetration is difficult to achieve while costs and prices remain high. By mandating a substantial "up front" investment by the dominant carrier in this new technology, the Joint Stipulation will help overcome this dilemma. As experience is gained in the marketplace with this technology, all carriers in North Carolina will be encouraged to rapidly deploy this and other types of broadband technology.

Q. You also mentioned that BellSouth would absorb some of lost access revenues. Would you please discuss this aspect of the Joint Stipulation?

A. Yes. As I stated earlier, BellSouth will experience revenues losses of $83 million as a result of charging lower switched access rates. It will recoup some of these lost revenues through increases to other rates, and by reducing the number of free DA calls. The cumulative gain from these tariff changes amounts to approximately $50 million, or less than two-thirds of the lost access revenues. The remaining portion will be absorbed by BellSouth. Together with the commitment to additional investment in advanced technology, this provision helps guarantee that consumers in North Carolina will benefit from the Joint Stipulation.