SOUTH CAROLINA TELEPHONE COMPANIES

DIRECT TESTIMONY OF EMMANUEL STAURULAKIS

BEFORE THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

DOCKET NO. 97-239-C

Q. Please state your name and business address.

A. My name is Emmanuel Staurulakis. My business address is 6315 Seabrook Road, Seabrook, Maryland 20706.

Q. By whom and in what capacity are you employed?

A. I am President of John Staurulakis, Inc. (JSI) a telecommunications consulting firm providing a full range of financial, regulatory and management consulting services to independent telecommunications providers throughout the nation.

Q. Please briefly outline your education, training and experience in the telephone industry.

A. In 1980, I received a Bachelor's degree in Business Administration from the American University, Washington, D.C. From May 1980 until December 1984, I worked at JSI as a Cost Separations Consultant. My responsibilities

included preparing jurisdictional toll cost separations studies for clients in several states.

In December 1983, I earned a Masters degree in Accounting from the George Washington University, Washington D.C. In January 1985, I became a Supervisory Consultant responsible for the overall preparation and submission of numerous jurisdictional toll cost separations studies, rate case work, and intrastate tariff filings for a number of JSI clients.

In November 1987, I was promoted to Director of the Separations Department. In October 1992, I was promoted to Vice President of Operations and given day to day responsibility for all financial and regulatory matters affecting our clients. I am also a member of the National Exchange Carrier Association's (NECA) Universal Service Fund Committee.

In July of 1997, I was promoted to my current position of President of JSI.

Q. On whose behalf are you testifying in this case?

A. I have been requested to testify on behalf of five incumbent local exchange carriers (five Companies) that have filed for reductions in the price of certain

services and seek recovery of the lost revenue from the state USF (SC USF). The Companies are listed in Exhibit A.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to describe the cost methodology utilized in determining the level of implicit support contained in the rates of the services proposed for reduction by the five Companies. In addition, I will describe recent developments in the federal arena with regard to universal service funding.

Q. What role does the SC USF play in ensuring that consumers have access to state of the art telecommunications services at affordable rates?

A. In establishing a State USF, the Public Service Commission of South Carolina (Commission) responded to a legislative mandate that recognized the fact that implicit support for basic local telephone service built into rates for other services cannot be sustained in a competitive environment. Market forces will eventually cause a decrease in the prices for telecommunications services priced above their underlying cost thereby reducing the level of implicit support, or subsidy that is available to maintain affordable basic local service rates in high-cost areas. Accordingly, the SC USF is the mechanism by which

implicit support is identified and removed from existing rates and made explicit, thereby ensuring the continuation of universal service to telecommunications consumers in South Carolina.

Q. Have there been any recent actions at the federal level relating to universal service issues?

A. Yes. On October 27, 2003, the Federal Communications Commission (FCC) released an Order on Remand (Order) and a Further Notice Of Proposed Rulemaking (FNPRM) addressing universal service issues affecting rural areas served by non-rural carriers. In the Order, the FCC was responding to a decision of the United States Court of Appeals for the Tenth Circuit (Tenth Circuit) and recommendations of the Federal-State Joint Board on Universal Service.

Q. What issues were at the center of the Tenth Circuit's decision and the need for the FCC to issue their Order?

A. The Telecommunications Act of 1996 (Act) codified the historical commitment of the FCC and state regulators to promote universal service by ensuring that consumers in all regions of the nation have access to affordable, quality telecommunications services. Under Section 254(b) of the Act, consumers in

rural, insular and high-cost areas should have access to telecommunications services at rates that are reasonably comparable to rates charged for similar services in urban areas. Moreover, Section 254(e) of the Act provides that federal universal service support should be explicit and sufficient to achieve the intended purposes.

In 1999, the FCC issued its Ninth Report and Order in a proceeding involving a new methodology for the determination of universal support for non-rural carriers based on forward-looking economic costs. The new methodology was challenged in court by Qwest and as a result, the Tenth Circuit issued a decision that remanded certain aspects of the Ninth Report and Order back to the FCC. Specifically, the Tenth Circuit required the FCC to define more precisely the statutory terms "reasonably comparable" and "sufficient" and then to assess whether the new non-rural mechanism adopted would be sufficient to achieve the statutory principle of making rural and urban rates reasonably comparable. In addition, the Tenth Circuit required the FCC to develop mechanisms to induce state action in order to preserve universal service.

Q. In your opinion, has South Carolina made the effort to preserve universal service in South Carolina as described in the FCC Order?

A. Efforts to date make it clear that the Commission has made great strides in insuring that all consumers in the state continue to have access to affordable basic local service. The second phase of the SC USF process is a clear indication of the importance of insuring that implicit support contained in existing rates is identified and made explicit so that consumers in the more rural areas of the state do not lose their access to affordable basic local service. Many other states have simply failed to take the necessary steps to address issues so long ago recognized by the Commission and South Carolina legislature.

Q. Are SC ILECs currently receiving funding from the SC USF for reductions in intrastate switched access rates?

A. Yes. Per Commission Order No. 2001-419, all SC ILECs reduced their intrastate switched access rates by 50% and began recovering the resulting revenue shortfall from the SC USF effective October 1, 2001. The reduction in access charges is referred to as the first step of the initial phase per the SCUSF Administrative Procedures. In Order No. 2001-419, the Commission refers to the access reduction as the initial step.

Q. Does the SC USF provide for the identification and recovery of implicit support contained in the rates of non-access related services provided by SC ILECs?

A. Yes. According to Commission Order No. 2001-419 and the State USF guidelines and Administrative Procedures adopted in Commission Order No. 2001-996, any SC ILEC that has been designated as a carrier of last resort by the Commission may seek recovery from the SC USF for the amount of implicit support contained in certain tariff rates. The amount of implicit support for a given service is the difference between the tariff rate and underlying cost of the service. In order to receive funding beyond the amount associated with the level of implicit support contained in intrastate access rates (first step of the initial phase), the ILEC must file detailed cost data that clearly demonstrates the existence of implicit support in the rate(s) proposed for reduction.

Q. Are any SC ILECs currently receiving funding from the SC USF for previous reductions in tariff rates?

A. Yes. Per Commission Order. No. 2003-215, the petitions of six SC ILECs for additional SC USF funding in the amount of approximately $6.6 million were approved. Payments from the SC USF to the six ILECs was to begin no later

than October 1, 2003, and would be revenue neutral as each of the six ILECs filed tariff reductions to certain end user rates totaling approximately $6.6 million that became effective upon resizing the SC USF to include the additional recovery amounts.

In an effort to maintain adequate control and oversight of the SC USF, the Commission created a phase-in approach. As such, Commission Order No. 2001-419 limited the amount that an eligible SC ILEC could withdraw from the SC USF per the first phase to no more than an amount equivalent to one-third (33.33%) of its company-specific SC USF. For each of the six Companies, the amount of funding per the first step (access reduction) of the initial phase when combined with the second (end user) step did not exceed the one-third limitation approved by the Commission.

Q. In this proceeding, are the five Companies eligible to withdraw additional support from the SC USF?

A. Yes. Each one of the five Companies has provided the detailed cost support required by the Commission in Order No. 2001-419 that demonstrates the existence of implicit support in the services identified. Accordingly, each of the five Companies has proposed reductions in the tariff rates of the services

identified and seeks recovery of the associated revenue reductions from the SC USF.

Q. What is the amount of additional SC USF support being requested by the five Companies?

A. The amount of additional annual funding requested from the SC USF is approximately $3.7 million. A breakdown of the additional funding, by Company, is shown in Exhibit B of my testimony.

Q. Are any of the five Companies seeking additional SC USF in this proceeding already receiving SC USF from previous reductions in service rates?

A. Yes. All five Companies listed in Exhibit B are currently receiving SC USF associated with end user rate reductions approved by the Commission in Order No. 2003-215. In accordance with the SC USF Administrative Procedures, total high cost support for each LEC for the second phase shall not exceed 66.67% of the LEC's maximum high cost support. For the five Companies participating in this proceeding, none is requesting additional SC USF that, when combined with SC USF support received in accordance with the first and second steps of the first (initial) phase exceed the 66.67% threshold,

Q. Does the amount of SC USF requested in the second phase by any of the five Companies cause their total SC USF to exceed the 33.33% threshold established by the Commission?

A. Yes. Three of the companies seek additional SC USF in the second phase that, when combined with the amount of SC USF received in the first phase (first and second steps) would exceed the 33.33% threshold established in Order No. 2001-419. The three companies are Bluffton Telephone Company, Home Telephone Company and PBT Telephone Company.

Q. What is a company required to do before its SC USF withdrawal can exceed the 33.33% threshold established?

A. In Order No. 2001-419, the Commission directed that any company wishing to withdraw more than one-third of its company-specific SC USF amount must first update its cost of basic local exchange service. By updating the cost of basic local exchange service, the Commission can make sure that no company's withdrawal exceeds its appropriate cost or the allowable SC USF for that specific company. The three impacted companies have filed updated cost of basic local exchange service cost studies in this proceeding, as required by the Commission. In the current proceeding, the cost per line for basic local

exchange service for the three impacted companies increased when compared with the original results calculated in the initial SC USF proceeding. For Bluffton, the cost per line increased approximately 7.4 %, from $50.07 to $53.78. For Home, the cost per line increased approximately 25.9%, from $46.14 to $58.08. For PBT, the cost per line increased approximately 8.5% from $56.49 to $61.29.

Q. Are the annual revenue reductions associated with the proposed service rate reductions revenue-neutral to the five Companies?

A. Yes. The Commission requires that each eligible ILEC must make dollar-for-dollar reductions in rates containing implicit support before the ILEC can withdraw explicit support from the SC USF. In addition to the cost support filed in this proceeding, each Company filed revised tariff pages reflecting the proposed decrease in service rates. The Companies are not eligible to receive SC USF funding until such time as the revised tariff rates are approved by the Commission.

Q. Please describe the process that each of the five Companies utilized in order to determine which service rate(s) to reduce?

A. On an annual basis, all SC ILECs are eligible to file tariff reductions and request additional SC USF support to fund the continued removal of implicit support contained in rates, although participation is not mandatory. As such, any ILEC wishing to participate in the second phase needed to perform a review of its tariff rates for services in an effort to determine which services may contain implicit support. The five Companies participating in the instant proceeding contacted JSI and requested that the required cost analysis be conducted in order to determine the level of implicit support contained in the selected service rates.

Q. Please identify and describe the proposed service(s) reductions for the five Companies?

A. As described in the cost studies filed in this proceeding, the five Companies filed proposed rate reductions in the following areas: area calling plans, measured extended area service, private line service, special access, custom calling features, class services, landline-to-mobile optional service and mobile-to-landline termination service, and billing and collection. The existing rates for these services contain levels of implicit support that have historically allowed basic local service rates to be set at rates that are below the cost of providing the service. As competition from wireless, voice over internet protocol and other emerging technologies continues to grow, companies that

continue to set rates for services that are priced above cost will see those services migrate to competitors. To the extent that implicit support once relied upon to maintain affordable basic local service rates to rural customers dissipates, rural consumers will be faced with much higher rates for their basic telecommunications needs. Unfortunately, many of these same consumers will not have competitive choices available to them and will be forced to pay more for their basic telecommunications needs. Thus, the continued need to transition implicit support from certain rates to the SC USF is an important step to preserving universal service for all SC consumers.

Q. Are the proposed service rates for the five Companies set at a level that is above the calculated cost of each service?

A. Yes. All of the proposed service rates are set at levels above the cost of the service based on the studies performed.

Q Please describe what you mean by the cost of the service.

A. As mentioned earlier, an eligible SC ILEC seeking additional funding from the SC USF must file detailed cost data with the Commission that clearly demonstrates that implicit support exists within the rates identified for proposed reductions. The use of an embedded cost methodology by rural SC

ILECs has been approved by the Commission in Order No. 98-322 in this docket. Embedded costs represent dollars actually spent to provide services and include expenditures for plant and operating expenses as represented on the Companies' financial statements. Utilizing the Commission approved cost methodology and actual cost and demand data for the most recent year available, JSI calculated the embedded cost of service for the services identified for each of the five Companies. The embedded cost of each service was then compared to the tariff rate for the service in order to determine the existence of implicit support.

Q. Was the cost methodology utilized in the cost studies conducted and submitted in the instant proceeding consistent with the cost methodology approved by the Commission?

A. Yes. The methodology utilized to determine the level of implicit support contained in the service rates proposed for reduction by all five Companies and the updated cost of basic local exchange service for three of the five Companies is consistent with the cost methodology approved by the Commission. The same cost methodology was utilized in previous SC USF proceedings to calculate the embedded cost of basic local service and end user service rates.

Q. What would you have the Commission do in regards to this proceeding?

A. I would respectfully request that the Commission approve the petition of the five Companies and grant the reductions of rates requested in accordance with existing law and Commission orders, and resize the SC USF to recover the implicit support identified.

Q. Does this conclude your testimony?

A. Yes, it does.

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Exhibit A

List of South Carolina Companies

Bluffton Telephone Company, Inc.

Hargray Telephone Company, Inc.

Home Telephone Company, Inc.

Horry Telephone Cooperative, Inc.

PBT Telecom

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Exhibit B

Requested Universal Service Funding Associated With
The Proposed Reductions In Service Rates

Bluffton Telephone Company, Inc.	$ 250,544
Hargray Telephone Company, Inc.	$ 337,890
Home Telephone Company, Inc.	$ 721,428
Horry Telephone Cooperative, Inc.	$ 1,957,949
PBT Telecom	$ 470,622
Total Additional SC USF Requested	$ 3,738,433