STATE OF VERMONT
PUBLIC UTILITY COMMISSION

Petition of the Vermont Department of Public Service for an investigation into the service quality provided by Telephone Operating Company of Vermont, Inc., d/b/a Consolidated Communications, Inc.	)	Case No. 18-3231-PET

REDACTED

DIRECT TESTIMONY OF MICHAEL SHULTZ ON BEHALF OF CONSOLIDATED COMMUNICATIONS

June 12, 2019

SUMMARY OF TESTIMONY

Mr. Shultz describes: 1) Consolidated Communications Inc.'s overview of the company and operating entities; 2) changes in corporate structure since July 2017; 3) spending commitment and network improvements since July 2017; 4) commitment to the NE states; and 5) changes in operations structure.

**REDACTED DIRECT TESTIMONY OF
MICHAEL SHULTZ
ON BEHALF OF CONSOLIDATED COMMUNICATIONS**

1. Q. Please state your name, position, and business address.

A. My name is Michael Shultz, Vice President Regulatory & Public Policy, Consolidated Communications ("Consolidated" or the "Company"), 770 Elm Street, Manchester, NH 03110.

2. Q. On whose behalf are you testifying?

A. I provide testimony on behalf of Consolidated Communications of Vermont Company, LLC (formerly Telephone Operating Company of Vermont, LLC) d/b/a Consolidated Communications ("Consolidated Vermont").

3. Q. Please describe your professional and educational background.

A. I have over 30 years of telecommunications experience in regulatory, external relations, billing, tariffs and compliance. I have held the position of Vice President, Regulatory & Public Policy with Consolidated since April 2004. Prior to that date, I held the role of Senior Director, Regulatory and Industry Affairs with TXU Communications from November 2002 to April 2004.

From 1991 to 1992, I held positions of increasing responsibility with Citizens Communications (now Frontier Communications). The last position I held was Director, Federal Regulatory & Compliance. Prior to joining Citizens Communications, I was with the consulting firm John Staurulakis, Inc. from 1985 to 1991.

I received a Bachelor of Arts degree in Economics from the University of Pittsburgh and a Masters of Business Administration from the University of Dallas.

4. Q. What are your duties as Consolidated's Vice President, Regulatory & Public Policy?

A. I am responsible for Federal and State regulatory and legislative strategy, advocacy, and regulatory compliance. In addition, I have responsibility for tariffs, interconnection, industry relations, settlements, and billing operations.

5. Q. Have you previously testified before the Vermont Public Utility Commission (the "Commission" or "PUC") or another state public utility commission?

A. Yes, in Vermont I testified in Docket 8881. I have also testified in various dockets in California, Maine, Nebraska, New Hampshire, Pennsylvania, and Texas.

6. Q. What is the purpose of your testimony?

A. First, I will introduce the other witnesses in this Case. I will discuss service quality issues experienced by the Company in Vermont in the summer and fall of 2018, and how Consolidated has taken steps to improve service quality. I will then give an update on the Company's organizational changes, and accomplishments since the merger, as well as addressing our merger commitments and status to date. To provide context, I will also discuss technology and industry changes since the Docket 5903 metrics were implemented. Last, I discuss the financial aspects of the provider of last resort obligations.

7. Q. Please identify the witnesses offered by Consolidated in this Case.

A. In addition to myself, Consolidated offers testimony of Gabe Waggoner, Executive Vice President of Operations; Ryan Whitlock, Senior Vice President of Operations; and Jeffrey Austin, Director, Government Relations, State of Vermont.

8. Q. Please describe what caused the service delivery delays and consumer complaints to increase in summer and fall of 2018.

A. Mr. Waggoner discusses this is detail, but let me summarize. There were a combination of factors that caused the service quality challenges. First several OPT's (Outside Plant Technicians) and SST's (Splice Service Technicians) retired in late 2017 and during the first half of 2018. Finding people to fill those job vacancies took longer than expected. Also in 2018, we began the process of negotiating a labor agreement, which was finalized in August 2018. This new labor agreement allowed for contractor resources to be utilized, providing management flexibility to fill in resources when needed, something that was not permitted under the prior agreement. During this same time period, there was also an increase in service installation and upgrade requests based on marketing and rebranding efforts, as well as our broadband upgrade announcement in late February 2018. Summer and fall is a time that we often experience higher levels of customer troubles related to storms causing increased demand on resources. Finally, our action plan to resolve resource issues caused by the previous factors took longer to implement due in part to hurricanes in North Carolina and Florida limiting contractor resources during this time.

We at Consolidated take very seriously the problems that customers experienced in the summer and fall of 2018, in particular the time it took to clear troubles. As I discuss below and as detailed in Mr. Waggoner's and Mr. Whitlock's testimony, we have undertaken many and diverse actions to attempt to improve service quality. That said, I would like to note that meeting the C24 standard has been a chronic problem for our predecessors as well, particular in the summer months when there is more rain. The Company strongly believes that the existing service quality metrics from Docket 5903, that became effective in 1999, should be modified because the Company's competitors are not subject to the Docket 5903 reporting at all, and it is no longer a realistic and accurate measurement of customer satisfaction. However, we do recognize our duty to try to meet the metrics under Docket 5903, and continue to work to do so.

9. Q. When service levels began to decline in mid-2018 and continued to decline over several months, what steps did you take to correct the situation?

A. Our immediate response was to bring in additional technicians from other Consolidated markets within New England and other areas of the company. Once we had the additional flexibility under the new collective bargaining agreement, we also engaged outside contractors. This process took longer than expected as I noted above due to other weather events around the country. The many other steps we have taken to work on improving service quality are detailed in the testimony of Mr. Whitlock and Mr. Waggoner. A few of the most noteworthy changes include greater flexibility gained in technician and support functions to improve service to our customers through the new collective bargaining agreement. We have also cross-trained resources in other parts of the country to provide support to our technicians and call center representatives. We have also made a number of structural changes within the organization to add resources to support technicians and to increase visibility of problems throughout the management structure.

From an administrative standpoint, we are in the process of reducing the number of legal entities to streamline our various back office functions such as accounting, tax, sales, and regulatory, among others. We eliminated several FairPoint holding companies, merged FairPoint non-regulated entities into Consolidated Communications Enterprise Services, Inc., collapsed, where possible, ILEC entities to have one per state, and changed all entities names to a Consolidated Communications based name.

10. Q. Have you reviewed the Memorandum of Understanding ("MOU") between Consolidated and the Department of Public Service ("Department") in Docket 8881, and which was incorporated into the Commission's Final Order in that Docket?

A. Yes, I have.

11. Q. What are the specific commitments made by Consolidated in the Docket 8881 MOU regarding VT plant/infrastructure upgrades?

A. There are 27 merger commitments Consolidated agreed to as part of the merger, the following seven are in regards to Vermont's network plant and infrastructure:

1. Consolidated shall maintain a minimum level of capital investment in Vermont for network improvements at an average level of at least 14% of total Vermont revenue for a period of three (3) years after completion of the merger.

2. Consolidated has agreed to invest another $1M, on an average annual basis, for a period of three (3) years after completion of the merger, in capital investments specifically to target areas with on-going service quality concerns, as identified in collaboration with the Department.
3. Consolidated shall annually file with the Commission and the Department a report detailing its compliance with the capital investment requirements from bullets 1 and 2 above.
4. Within six months after closing, Consolidated shall prepare a three-year plan for capital investment in the Vermont network.
5. Consolidated agrees that within three months of assuming responsibility for the network operations of FairPoint, it will utilize the Consolidated escalation process for aging trouble tickets.
6. Consolidated agrees to provide a staffing plan for the SS7/STP functional network expertise within three months after approval of the merger and file it with the Commission and Department under seal.
7. For the first two (2) years after completion of the merger, Consolidated also agrees to provide notice to the Commission and the Department at least three months prior to any transition of the Vermont SS7/STP service to a third-party. This requirement only applies for a period of two (2) years after the completion of the merger, and in no event after June 30, 2019.

12. Q. Has Consolidated met those obligations you list above?

A. Yes, we have met all requirements to date and are committed to fulfilling the remaining commitments as required. In this respect, I disagree with the Department's statements in its testimony filed in this Case that Consolidated has failed to meet its commitments. As discussed more below, Consolidated met or will meet its obligations from Docket 8881.

13. Q. Please describe changes and improvements to the Vermont network since July 2017.

A. Consolidated has increased fiber and broadband deployment and increased available speeds to approximately 100,000 consumers. Consolidated has deployed many fiber fed remote terminal supporting voice and data services which reduces Central Office copper facilities. Mr. Waggoner and Mr. Whitlock describe in detail the organizational and process changes that have been made, as well as the additional training and tools for technicians we have implemented and they describe the many additional technicians brought to Vermont.

14. Q. Please describe the changes in the broadband services available in VT.

A. Since the July 3, 2017 merger we have increased broadband availability and speed in Vermont. Consolidated accepted FairPoint's CAF II obligations as part of the merger commitment in Docket 8881 and 99% of our CAF II commitment is completed, significantly ahead of schedule. In 2018 we set and met an internal goal to increase broadband speeds to 100,000 homes and businesses in Vermont. This initiative represents increased speeds to one third of the total homes passed in the Vermont. We have applied for and have been granted VT connectivity grants to continue to build and expand broadband in Vermont's rural communities.

15. Q. In Docket 8881, you stated in testimony that Consolidated was committed to reducing customer pain points and that Consolidated was committed to improving service. Has Consolidated been successful?

A. Consolidated continues to focus on our commitment of reducing customer pain points and improving service. We had some significant challenges in the summer and fall of 2018 when we experienced difficulty providing installation and repair intervals that were in line with customer expectations and the Docket 5903 service quality metrics. Since January 2019, our service repair and installation intervals have returned to normal levels and we continue to improve service quality, along with meeting our broadband buildout commitments.

16. Q. Did you review Department witness Scott Wheeler's pre-filed testimony submitted in this Case?

A. Yes, I did.

17. Q. Do you agree with Mr. Wheeler's analyses of the financial statements of the Vermont operating entity and Consolidated's parent company?

A. No, his analysis is incomplete, is an oversimplification of free cash flow, and ignores the extensive capital investment already being made in Vermont, both to grow our high speed broadband reach and to improve service quality. Mr. Wheeler's analysis also ignores the cost to finance operations, integration costs, and pension obligations. We do agree with one part of Mr. Wheeler's testimony which states that dividend payments to equity shareholders is at the discretion of our Board of Directors. For reasons not specifically related to Mr. Wheeler's testimony, Vermont, or this service quality proceeding, on April 25, 2019, Consolidated's Board of Directors and Management Team, after careful study and analysis, announced: 1) we would eliminate our dividend after the May 1, 2019 dividend payment, and 2) would be repurposing the annual $110.0 million in dividends to focus on debt reduction and potentially accelerated investment in our network. As equity values for all wireline companies have come under pressure in recent months, our Board felt that we were no longer getting the appropriate value in our stock price as compared to our peer group to warrant continuing to pay it. With that said, we would also note that at the time we acquired Fairpoint, given the dividend policy at the time, we were able to purchase Fairpoint in a 100% stock consideration and assumption of their debt. We were able to refinance the assumed debt at very attractive interest rates and rates significantly better than rates Fairpoint were carrying the debt at. In the future, this will also enable us to invest in broadband fiber expansion projects, but initially, that will be a small portion of funds formerly set aside for a dividend payment.

18. Q. Please describe how Mr. Wheeler's financial analysis deviates from standard accounting principles.

A. Mr. Wheeler's testimony proposes to remove depreciation and amortization from the earnings calculation to come up with cash flow, which he asserts could then be used to improve service quality. However, his calculations are incomplete as they do not account for capital already being invested in Vermont, interest expense of the debt associated with Vermont, or pension obligations associated with Vermont based employees. This calculation seems in conflict with traditional utility ratemaking in which depreciation rates are included in retail and wholesale rate development. In addition, his calculation is flawed in that it assumes only non-cash expenses, it does not reflect the corporate activities that are necessary to keep Consolidated Vermont running. To have any validity from an accounting standard, his proposed calculation must include corporate benefits paid on behalf of Consolidated Vermont. Such benefits would include: capital expenditures, dividend payments, and interest on the debt. These items are booked at the holding company level and not allocated to each legal entity. Consolidated is adequately invested and committed to expanding broadband speeds and to honor our existing investment commitments in Vermont.

19. Q. Would the problems in terms of meeting service quality metrics be addressed by the imposition of additional credits as the Department has recommended?

A. No, Consolidated regularly provides credits to customers today and did so in 2018. Increasing the credit amount does not solve for the service quality metrics being missed, it only exacerbates the problem as shown in Consolidated Vermont's 2018 annual report which shows that Consolidated has already lost several million dollars to serve Vermont. We serve 110 exchanges in Vermont most of which have some form of voice alternative with Cable, CLEC, and wireless providers as described in Mr. Austin's testimony. The competitive providers have little, if any service quality reporting requirements. The additional credits proposed by the Department are punitive. Consolidated's view is consistent with that expressed in the

Department's Draft 2018 Vermont Telecommunications Plan, at p. xii, that to preserve "networks …crucial to preserving Vermont's rural way of life," ILECs like Consolidated "should be given the support they need to continue offering service in their rural markets."

20. Q. Would the problems in terms of meeting service quality metrics be addressed by simply increasing technicians in Vermont as the Department has recommended?

A. No, because the problem is broader than just adding technicians. While Consolidated did have staffing issues in 2018 due to early retirements, we have addressed those with new hires and supplemented with contractors to meet demand, seasonal or otherwise. In addition to staffing/contractor additions, we also changed dispatch and internet prequalification processes, which has helped reduce troubles reported. However, we are no longer a monopoly for voice services in many areas of the state, as we were in 1999. As Mr. Austin explains, we have lost 238,840 access lines since 1999, and the model that supported the Docket 5903 metrics 20 years ago no longer exists. Service to our customers will improve when the playing field is leveled to allow Consolidated to operate its business as most of its competitors do, i.e., without imposition of the Cleared in 24 standard.

21. Q. Please summarize the history of the service quality metrics that apply to Consolidated in Vermont.

A. The Commission, then called the Public Service Board adopted service quality metrics for Vermont telecommunications carriers in 1999. The Board said the purpose of the standards was to set the "*minimum service levels that all ratepayers should receive,*" even in the competitive marketplace.

Given its RBOC status and lagging service quality results, Verizon was placed under a different and harsher service quality (SQ) plan. FairPoint inherited Verizon's harsher SQ plan upon acquisition. The plan placed higher potential penalties upon Verizon (and therefore FairPoint, after acquisition) among other enhancements beyond the "minimum service levels" the Board set for all other carriers in 1999.

When the legacy Verizon plan expired, FairPoint successfully reduced the applicable penalty scheme and sought a mechanism to "earn out" of a harsher SQ plan by meeting performance standards for a defined period of time. At the end of the first quarter 2013, FairPoint successfully met its "earn out" requirements and became subject to the same "minimum service levels" the Board set for all other carriers in 1999 in Docket 5903.

Under the 5903 requirements, a carrier's service quality is measured against a baseline standard and an action level standard. The baseline standard represents the minimum service quality expected of a carrier in its regular course of business. If a provider triggers the Action Level Report in any quarter or in any 5 or more months in a calendar year, the provider must provide the Board with a full explanation for the failure in addition to a plan and timetable for correcting the problem giving rise to the failure.

In December 2014, the Board opened an investigation into FairPoint's service quality at the Department's request during the labor strike. The investigation looked at FairPoint's service for a period of time leading up to and during the strike. When negotiating a resolution to that investigation, FairPoint argued, among other things, that a) the Cleared in 24 metric required by the 1999 standards is outdated and unrealistic, and should be updated with a cleared in 48 metric, and b) service quality should be reported only for locations that lack an alternative voice service provider. The Department agreed FairPoint could ask the Board for these changes. While that request was pending, the Department agreed not to pursue any "remedial measures" for SQ failures and FairPoint was able to measure its performance on a calendar year basis with only one Action Plan required per year in the event it fell below benchmarks.

The Board determined that it could not allow FairPoint the requested relief without also adopting significant new penalties and restrictions sought by the Department. That result was not acceptable to FairPoint and so the Board granted FairPoint's request to dismiss its petition altogether.

As a result, Consolidated remains subject to the same 1999 "minimum service levels" as all other carriers and without any modification. This means that Consolidated has to continue to report under all of these metrics and must submit an Action Plan in any quarter the company falls below the benchmark for a reported metric. There have been modifications that allow flexibility in some areas such as pricing. However, the metrics related to repair and installation intervals are unchanged since 1999, regardless of whether there are competitive providers that are offering similar or alternative services in Consolidated's service territory without those metrics obligations.

22. Q. Please describe some of the ways in which the telecommunications industry has changed since the existing Service Quality Metrics from Docket 5903 were implemented in 1999.

A. Telecommunication technologies have changed dramatically since 1999. Networks are transitioning from legacy Time Division Multiplexing (TDM) based systems to Internet Protocol (IP) based systems and networks. Fiber services are being deployed closer to or directly to customers' homes. Voice services have declined rapidly due to social change. Many consumers today only have a wireless service with no wireline service to their homes. Texting is the new "voice" service. Internet services, cloud computing, and video streaming are driving higher broadband speeds. Speeds in 1999 were dial up, 56 Kbps at best, with very limited consumers using the internet at that time. Today, internet speeds for residential customers can reach up to 1 Gbps, with the vast majority of homes having multiple devices connected to the internet. The industry is transitioning rapidly based on consumer demand though the regulations have not been modified to keep up with these competitive trends.

23. Q. Please describe how this is different than the business Consolidated's predecessors may have been in.

A. Consolidated's predecessors had a statewide monopoly in their service territories on telephone service. This monopoly model allowed revenue from the populated urban areas to subsidize the rural areas where the cost of providing service was and continues to be significantly higher as explained in Mr. Austin's testimony. This model also provided higher revenues from commercial services to help subsidize the more expensive consumer services. In the 20 years since the service quality metrics have been implemented, the scope and nature of competition in Vermont has changed dramatically including, but not limited to, a significant loss in access lines and business services in all markets, resulting in a significant loss of revenue.

24. Q. Please explain the level of competition Consolidated experiences in Vermont.

A. There is significant competition from Cable companies, CLEC's, municipalities, and wireless providers, primarily in the most populated areas in Vermont. Companies such as Burlington Telecom, which was subsidized with taxpayer money, Comcast, and EC Fiber provide significant competition without the burden of state regulation or the requirement to provide service in a whole geographic area. These competitors do not serve all areas of the exchange, they instead choose to service locations that provide the best financial return on their investment. There are other companies, such as CenturyLink and FirstLight, that compete only in the commercial and carrier segments. These companies do not and are not required to provide service to the consumer segment. Telecommunications competition in Vermont has increased substantially in the commercial, carrier, and consumer markets. While Consolidated continues to provide service in the most rural parts of Vermont, competition from these providers that are not regulated in the same manner makes it extremely difficult for us to compete on a level playing field.

25. Q. Does Consolidated provide the same levels of service for customers in areas with more competition than areas with only Consolidated as a provider?

A. Yes. Based on our current state regulations, we do not differentiate between competitive and non-competitive exchanges.

26. Q. Does it cost the same amount of money to serve customers in all areas of the State of Vermont for basic phone service?

A. No. Our cost to serve varies by size, density, geography, and topography.

27. Q. Are there areas of the State where Consolidated is losing money to provide Plain old telephone service (POTS)?

A. Yes. POTS is a voice connection to a residence or business over TDM network. POTS service provides local calling and access to 911, long distance and operator service providers. POTS service provides line-powered dial tone to a customer's premises, which allows for service to continue, even during a commercial power outage. Rates vary by service type. A basic rate for a residential POTS in Vermont is $15.54 per month.

28. Q. Can you give an example of a situation where Consolidated is losing money to provide service?

A. The consumer Average Revenue Per Unit (ARPU) per month in Vermont is **[START CONFIDENTIAL INFORMATION]** [redacted] **[END CONFIDENTIAL INFORMATION]**. The ARPU is the average monthly spend by residential customers in

Vermont. Revenue in the calculation includes basic residential service, ancillary features, long distance, and broadband revenues. Let's compare a small, high cost exchange and a large, low cost exchange. The exchange cost numbers listed below are preliminary, but directionally correct. Island Pond is a small, rural exchange with an average cost to provide service of **[START CONFIDENTIAL INFORMATION]** [redacted] **[END CONFIDENTIAL INFORMATION]** per line, per month, which is a shortfall of **[START CONFIDENTIAL INFORMATION]** [redacted] **[END CONFIDENTIAL INFORMATION]** per month compared to the ARPU. Burlington, is our largest exchange and our most competitive, it has an average cost to serve of **[START CONFIDENTIAL INFORMATION]** [redacted] **[END CONFIDENTIAL INFORMATION]**. The point here is that our most competitive exchanges continue to support our rural, high cost exchanges, but we continue to lose customers in these larger, densely populated urban areas. Continuing to use Burlington as an example, we have experienced over 50% consumer line loss over the last five years. This is an unsustainable business model. The current regulatory framework has to change, as our competitors do not have the same restrictions.

29. Q. What options has Consolidated explored or considered to address the losses associated with serving customers in remote corners of the State?

A. We are looking at multiple avenues to address this issue: 1) Requesting to de-average local rates and rebalancing to their appropriate cost levels per service area; 2) Using fixed wireless for last mile connectivity in rural high cost exchanges; 3) Public/Private partnerships to facilitate faster broadband deployment, such as the recent joint arrangement between Consolidated and Chesterfield, NH; 4) Addressing the demand side issue with state assistance; and 5) requesting the elimination of voice obligations and potentially exiting select markets.

30. Q. In the meantime, while the service quality metrics required by Docket 5903 remain in place and have been agreed to by Consolidated in Docket 8881, please describe Consolidated's efforts to comply with those requirements.

A. We understand our obligation to meet the existing the service quality standards from Docket 5903. There are several metrics that we have continued to meet or exceed on a regular quarterly basis, for example, our network trouble report rate is well below baseline. Calls answered within 20 seconds residence, was a challenge in 2018 due to rebranding, initiation of a customer account security PIN, and increased call volumes during the summer. We have expanded call center responsibilities to have all of our call centers handle calls in NNE. We have been above baseline since that time. Cleared in 24hrs – residence is a metric that Verizon and FairPoint struggled to meet. Since 2015, FairPoint only hit baseline for two quarters and missed for 7 quarters prior to the acquisition. During 2017 and 2018 a number of SST's and OPT's retired, creating a staffing void. The new labor agreement allowed us to bring in contractors to fill the void and hire permanent technicians in Vermont and NNE. Staffing is progressing, and the compliment of contract resources have helped improve our numbers since December 2018. To date, the 2nd quarter preliminary results (April and May) are above the 60% action level. The average unaudited Cleared in 24hrs results for the last 3 months were at 60.4%, above the action level and Cleared in 48hrs was at 89%.

To reiterate, Consolidated fully understands its obligations to meet the Docket 5903 metrics and Docket 8881 commitments, and strives to do so. That said, the Docket 5903 service quality reporting requirements should be eliminated or at least changed to reflect the changes in the industry. The metrics should remove exchanges with wireline and wireless competition from the calculation, omit customer troubles that self-select their repair date beyond the metric and change the Cleared in 24hrs to Cleared in 48hrs to reflect the reality of servicing remote areas of the state.

31. Q. Please summarize Consolidated's position in this proceeding

A. Consolidated prides itself on our customer service, it is part of our Vision, Mission and Value statements. We strive to put our customer's need first, exceeding their expectations with every interaction, both internally and externally. We missed that mark in the second half of 2018. Consolidated began implementing its action plan to resolve its service quality issues in July 2018. We have added additional staff, negotiated a new bargaining agreement which gave us staffing flexibility, improved some operational processes, and changed leadership in NNE and Vermont. All of these items have helped improve and bring our service levels up toward baseline levels. The Department's recommendation here to add on further penalties for non-compliance with a broken and out-dated measurement system will not result in further improved service for Vermonters. The current metrics and requirements are outdated and should be reviewed; monopoly based regulatory structures do not work in competitive environments.

32. Q. Does this conclude your testimony?

A. Yes, this concludes my testimony.