William E. Taylor

Subscribed and sworn to before me
this 23rd day of October 1995.

Notary Public

My Commission Expires July 7, 2000

Attachment 1

WILLIAM E. TAYLOR

BUSINESS ADDRESS

National Economic Research Associates, Inc.
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Cambridge, Massachusetts 02142
(617) 621-2615

Dr. Taylor received a B.A. *magna cum laude* in Economics from Harvard College, an M.A. in Statistics and a Ph.D. in Economics from the University of California at Berkeley. He has taught economics, statistics, and econometrics at Cornell and the Massachusetts Institute of Technology and was a Research Fellow at the Center for Operations Research and Econometrics at the University of Louvain, Belgium.

At NERA, Dr. Taylor heads the Cambridge office and is Director of the Telecommunications Practice. He has worked primarily in the field of telecommunications economics on problems of state and federal regulatory reform, competition policy, economic issues concerning broadband network architectures, quantitative analyses of state and federal price cap and incentive regulation proposals, and antitrust and contract litigation in telecommunications markets. He has applied the economic theories of price squeezes and cross-subsidization to long distance telephone, Centrex, and public telephone markets. In the area of environmental regulation, Dr. Taylor has worked on statistical issues in the measurement of emissions levels from coal-fired electric power generators and municipal waste-to-energy facilities.

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EMPLOYMENT

NATIONAL ECONOMIC RESEARCH ASSOCIATES, INC. (NERA)

1988- Senior Vice President, Vice President, Office Head, Telecommunictions Practice Director. Dr. Taylor has directed many studies applying economic and statistical reasoning to regulatory, antitrust and competitive issues in telecommunications markets. In the area of environmental regulation, he has studied statistical problems associated with measuring the level and rate of change of emissions.

BELL COMMUNICATIONS RESEARCH, INC. (Bellcore)

TESTIMONIES

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Arkansas Public Service Commission (Docket No. 83-042-U) on behalf of Southwestern Bell Telephone Company: economic analysis of non-traffic sensitive cost recovery proposals. Filed October 7, 1985.

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October, 1995

Exhibit B

DECLARATION OF ROBERT J. RIDER

I, Robert J. Rider, declare the following:

1. I am Director of Broadband Multimedia Products and New Business Planning. I am responsible for business development for broadband network based products and services on our video dialtone platforms, including Dover Township, New Jersey. In this capacity, I am familiar with the price levels in the tariff at issue. I am also familiar with the demand characteristics for video dialtone service in general, and for the video dialtone project in Dover Township in particular. I submit this declaration in support of Bell Atlantic's direct case and to respond to Commission questions concerning the impact of various price increases on demand for video dialtone service in Dover.

2. As explained more fully below, there is an inverse relationship between the price Bell Atlantic charges for video dialtone service and the demand for that service. Consistent with the Commission's new service rules, Bell Atlantic has set rates that cover the appropriate costs and still are sufficiently low to stimulate demand for the service. Any significant increase in those rates, however, will have a significant negative effect on demand. The result would be to undermine Bell Atlantic's ability to recover its video dialtone investment, and hinder the ability of competing programmers to enter the market in competition with the cable incumbents.

Programmer-customers face market pressure.

3. Video dialtone customers purchase transport of channel capacity from Bell Atlantic in order to provide video programming to end user subscribers. In Dover, these programmer-customers will enter the market and compete against two entrenched incumbents -- Adelphia Communications Corp. ("Adelphia") and Monmouth Cablevision Associates ("Monmouth"). These cable companies today enjoy a penetration rate of approximately 80% of the Dover market. As newcomers to this market, Bell Atlantic's programmer-customers will have to attract subscribers through a combination of superior service and product offerings, as well as a competitive price. Regardless of the quality of their offerings, price will remain a key component of their ability to compete and survive in this market.

4. At the same time, programmer-customers must also cover their own costs, a substantial portion of which consists of the cost to obtain transport on Bell Atlantic's video dialtone system. Unlike Adelphia's and Monmouth's systems in Dover Township, the video dialtone system, which is based on digital technology, requires a set top converter for every television that is to receive the programming. In setting price attractive enough to entice potential subscribers to switch video service providers, programmer-customers must factor in the costs for any inside wire installation and set top converters. In short, programmer-customers are presented with a market-based ceiling for the rates they can charge their subscribers, yet still need to cover their costs to stay in business. This puts a limit on the proportion of

their total costs that they can afford to pay for video transport, i.e., video dialtone service, and thus makes them particularly price sensitive.

Bell Atlantic's current rates are reasonable.

5. The rates that Bell Atlantic charges for video dialtone channels are based on the number of potential subscribers in the Dover Township area. Thus, from the programmer-customer's perspective, the costs for video dialtone broadcast service under the current tariff vary only with the number of channels ordered. In order to cover these costs, a programmer-customer's first recourse is to add subscribers since, for each subscriber added, the transport cost per subscriber declines. It is sensible for programmer-customers to focus on cost recovery on a per subscriber basis, because that is how programmer-customers will collect their revenues.

6. For example, if a programmer-customer were to purchase 60 channels at the most favorable rate options (maximizing 5 year term, 24 channel packages), that programmer-customer would pay $90,440 per month for video dialtone broadcast service (including the cost of an access link), assuming 38,000 potential subscribers. While the programmer-customer's per-month cost for transport is fixed, cost varies on a per subscriber basis depending upon the number of subscribers the programmer-customer has. Assuming various levels of penetration, the programmer-customers' video dialtone transport costs are as follows:

Penetration	Number of Subscribers	VDT Cost Per Subscriber
10%	3800	$23.80
20%	7600	11.90
30%	11400	7.93
40%	15200	5.95

To the extent a programmer-customer cannot increase penetration, the only way to reduce its costs is to limit the number of channels purchased.

7. Currently, Adelphia -- the primary incumbent in the Dover area -- charges its subscribers approximately $25.00 for a package of about 60 channels. Assuming, for example, that a new entrant offered its service initially at a 20 % discount compared to the price charged by the incumbent, a competitive offering would be priced at $20. In order to price at that level, a programmer-customer must cover not only the price it pays Bell Atlantic, but its other costs including equipment, programming, and marketing. In previous filings, Adelphia has estimated that total costs of providing programming services are two and a half to three times the cost of transport.[1] Assuming Adelphia is correct, this would mean that a market penetration of 30 to 40 percent would be needed to allow a programmer-customer to cover its total costs, and

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[1] ***Application of New Jersey Bell Telephone Company For Authority Pursuant to Section 214 of the Communications Act***, File No W-P-C-6840, Reply of Adelphia Communications Corp. at 22 (filed Feb. 17, 1993).

even then with little margin for error.[2] But even assuming that total costs are a more reasonable two times the cost of transport, a programmer-customer would still need a market penetration of over 20 percent to cover its costs at this price.

<u>An increase in Bell Atlantic rates will reduce demand.</u>

8. The result of this type of cost and market pressure is that if Bell Atlantic were to increase its channel charges, the market response would be a drop in the number of channels purchased. We have confirmed this evaluation of the economics of the market place in discussions with existing and potential programmer customers. As a result, it is possible to make a reasonable estimate of the impact of potential price changes on demand.

9. As an initial matter, any increase in price would discourage any new purchases of capacity, either from existing programmer-customers or from new programmer-customers that have not yet made any investment to provide video dialtone service in Dover. A price increase also would produce a reduction in existing demand with resulting revenue losses.

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[2] For example, at 30% penetration, two and half times the transport cost is $19.83. This calculation does not include other optional tariffed charges (i.e. messaging ports and additional channel charges), so the total cost is potentially higher. This means that even assuming a lower multiple, such as 2 times transport, programmer-customers operate on thin margins. This is especially true in the early years of service, when penetration numbers are likely to be lower.

10. If video dialtone rates were increased, programmer-customers would order fewer channels. For example, in response to market price increases, those customers ordering more than 72 channels (the approximate current capacity of Adelphia's system) would quickly drop channels in excess of 72 to maintain their per subscriber margins. As prices are further increased, programmer-customers would drop additional channels, which places them in a "Catch-22" situation: as channels are dropped to reduce transport costs, the programmer-customer's ability to offer attractive programming packages is reduced. The result of offering a less attractive package, however, will be to lower their subscriber penetration, which in turn further increases their per subscriber costs. This spiral partly accounts for the significant drop

12. Based on the foregoing, a conservative projection of the demand and revenue changes in response to various price increases is as follows:

Price Change	**Demand Change**	**Revenue Change**
+ 10 %	- 16 %	- 9 %
+ 20 %	- 32 %	- 23 %
+30 %	- 48 %	- 36 %
+ 40 %	- 74 %	- 65 %
+ 50 %	-100 %	-100%

13. These figures indicate the high demand elasticity of this service. As a result, any increase in per channel revenues from a price increase would be more than offset by revenue losses from a reduction in demand. Thus, a price increase in video dialtone service will have the net effect of decreasing its revenue contribution.