BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of INVESTIGATION INTO PRICING OF UNBUNDLED NETWORK ELEMENTS.	DOCKET NO. 990649-TP

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VOLUME 1

Pages 1 through 155

PROCEEDINGS:	HEARING
BEFORE:	CHAIRMAN J. TERRY DEASON COMMISSIONER E. LEON JACOBS, JR. COMMISSIONER LILA A. JABER
DATE:	Monday, July 17, 2000
TIME:	Commenced at 9:30 a.m.
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	JANE FAUROT, RPR FPSC Division of Records & Reporting Chief, Bureau of Reporting (850) 413-6732

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APPEARANCES:

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DONNA McNULTY, MCI WorldCom, 325 John Knox Road, Tallahassee, Florida 32303, appearing on behalf of MCI WorldCom.

RICHARD MELSON, Hopping, Boyd, Green & Sams, 123 South Calhoun Street, Tallahassee, Florida 32301, appearing on behalf of MCI WorldCom and Rhythms Links.

JOSEPH McGLOTHLIN, McWhirter Law Offices, 117 South Gadsden Street, Tallahassee, Florida 32301, appearing on behalf of Florida Competitive Carriers Association (FCCA) and Z-Tel.

NANCY B. WHITE and BENNETT ROSS, BellSouth Telecommunications, Inc., c/o Nancy Sims, 150 South Monroe Street, Suite 400, Tallahassee, Florida 32301, appearing on behalf of BellSouth Telecommunications, Inc.

KIMBERLY CASWELL, GTE Florida Incorporated, P.O. Box 110, FLTC0007, Tampa, Florida 33601-0110, appearing on behalf of GTE Florida Incorporated.

JEFFRY WAHLEN, Ausley & McMullen, 227 South Calhoun Street, Tallahassee, Florida 32302, appearing on behalf of ALLTEL.

APPEARANCES CONTINUED:

JOHN FONS and CHARLES REHWINKEL, P.O. Box 2214, Tallahassee, Florida 32316-2214, appearing on behalf of Sprint-Florida, Incorporated.

SCOTT SAPPERSTEIN, 3625 Queen Palm Drive, Tampa, Florida 33619-1309, appearing on behalf of Intermedia Communications, Inc.

MICHAEL A. GROSS, 310 North Monroe Street, Tallahassee, Florida 32301, appearing on behalf of Florida Cable Telecommunications Association, Inc.

MICHAEL HAZZARD, Kelley, Drye & Warren, LLP, 1200 19th Street, NW, Fifth Floor, Washington, D. C. 20036, appearing on behalf of Z-Tel Communications, Inc.

MARK BUECHELE, Koger Center, Ellis Building, Suite 200, 1311 Executive Center Drive, Tallahassee, Florida appearing on behalf of Supra Telecommunications.

KAREN CAMECHIS and PETER DUNBAR, 214 South Monroe Street, 2nd Floor, Tallahassee, Florida appearing on behalf of Time Warner, LP.

APPEARANCES:

BETH KEATING, DIANA CALDWELL and WAYNE KNIGHT, FPSC Division of Legal Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, appearing on behalf of the Commission Staff.

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P R O C E E D I N G S

CHAIRMAN DEASON: Call the hearing to order. Could I have the notice read, please.

MS. KEATING: By notice issued June 27th, 2000, this time and place have been set for a hearing in Docket 990649. The purpose is as set forth in the notice.

CHAIRMAN DEASON: Thank you. Take appearances.

MS. WHITE: Nancy White and Bennett Ross for BellSouth Telecommunications.

MS. CASWELL: Kim Caswell for GTE Florida, Incorporated.

MR. FONS: John "Indiana" Fons for Sprint-Florida, and Charles Rehwinkel.

MR. GROSS: Michael Gross for FCTA.

MR. LAMOUREUX: Jim Lamoureux for AT&T Communications of the Southern States, Inc.

MR. MELSON: Rick Melson for MCI WorldCom and Rhythms Links, Inc., and I would also like to enter an appearance for MCI WorldCom on behalf of Donna McNulty.

MR. McGLOTHLIN: Joseph A. McGlothlin appearing today for the FCCA and also for Z-Tel Communications, Inc.

MR. WAHLEN: Jeff Wahlen on behalf of ALLTEL Communications, Inc.

MS. CAMECHIS: Karen Camechis and Pete Dunbar for Time Warner Telecom LP of Florida.

MR. SAPPERSTEIN: Scott Sapperstein on behalf of Intermedia Communications.

MR. BUECHELE: And Mark Buechele on behalf of Supra Telecommunications.

MS. KEATING: And Beth Keating, Wayne Knight, and Diana Caldwell for Commission staff.

CHAIRMAN DEASON: Just give me a second, I'm trying to keep track. Did someone make an appearance for Covad? No one did? All right. Are they not a party anymore to this case?

MS. KEATING: They have not withdrawn.

CHAIRMAN DEASON: Okay.

MR. MELSON: Commissioner Deason, they have sponsored some testimony jointly with Rhythms. With your permission, I would enter an appearance on behalf of Covad then this morning?

CHAIRMAN DEASON: Very well.

MR. McGLOTHLIN: Commissioner Deason, may I also enter an appearance for Michael Hazzard of the Kelley Drye and Warren law firm on behalf of Z-Tel Communications.

CHAIRMAN DEASON: We were going fairly fast, but did someone make an appearance for Intermedia?

MR. SAPPERSTEIN: Yes, sir. Scott Sapperstein.

CHAIRMAN DEASON: Okay. And we had two appearances for Supra, is that correct?

MR. BUECHELE: No, just mine.

CHAIRMAN DEASON: I'm sorry.

MR. BUECHELE: Mark Buechele.

CHAIRMAN DEASON: Thank you. Okay. I believe that is everything.

Staff, preliminary matters.

MS. KEATING: Yes, Commissioner. There are two outstanding motions; one is a motion to compel filed by BellSouth on July 11th. The second is a motion to compel filed by GTE-Florida on July 14th. On Friday, the prehearing officer issued orders requiring expedited responses to those motions to compel. The parties are required to be prepared to address those at this time.

CHAIRMAN DEASON: Okay. Have there been written responses or are we going to hear oral responses today?

MS. KEATING: There has been one written response, and I believe the remainder of the parties prepared with oral responses. And it is also my understanding that these may have been resolved between the parties.

CHAIRMAN DEASON: Okay. Let's start with BellSouth. Can you give me an update as to where we stand on your motion?

MR. ROSS: Yes, sir, Chairman Deason. Bennett Ross on behalf of BellSouth. I am pleased to report that

all of the parties have provided information in response to BellSouth's discovery requests with the exception of Supra. Supra had advised BellSouth that it was going to provide the information that had been requested this past Friday. But as of today, BellSouth has not received that information.

But all the parties to whom the motion to compel was actually directed have either responded or have withdrawn from this proceeding. So I believe that BellSouth's motion to compel is moot provided that Supra does, in fact, provide the information that has been requested.

CHAIRMAN DEASON: Mr. Buechele. Can you come to a microphone, please.

MR. BUECHELE: It is my understanding that we weren't even a part of that motion to compel, but we did voluntarily make an agreement with them. It was my understanding that it went out on Friday. If it didn't, we will get it to them posthaste.

CHAIRMAN DEASON: So you are agreeing to provide the information?

MR. BUECHELE: Responses as we did -- we agreed with them.

CHAIRMAN DEASON: Very well. Mr. Ross, you have gotten a commitment that the information will be provided,

is that correct, you have not actually received the information?

MR. ROSS: No, we actually have received information from all the parties except for Supra. And it is our intent to go ahead and introduce those responses into the record as evidence.

CHAIRMAN DEASON: Into the record for this proceeding that we are --

MR. ROSS: Yes, sir.

CHAIRMAN DEASON: Very well. Ms. Caswell.

MS. CASWELL: Yes. GTE has agreed to accept the responses to BellSouth's discovery as sufficient responses for our discovery, as well. I believe all of the parties have either given us that information or promised to give it to us. Florida Digital Networks and Broadslate are the only parties from which I haven't actually received the information. I don't think there is anyone there from those companies, but I don't expect there will be a problem in eventually getting that. So our motion would be moot, as well.

CHAIRMAN DEASON: Very well. So there is no need to have argument on those motions. That's a pleasant surprise. Okay.

Other preliminary matters?

MS. KEATING: The only other thing we have is

there are a number of stipulated exhibits. And I would suggest that we have those numbered for the record at this time.

CHAIRMAN DEASON: Okay. I am going to rely on you to go through that list, and we will identify those and admit those into the record. And if anyone has any objection or question about anything, please get to a microphone and let me know, because we are going to move fairly rapidly, I anticipate.

MS. KEATING: The first exhibit is the official recognition list for this proceeding. Staff recommends that it be marked as Hearing Exhibit 1 in lieu of reading this rather extensive list into the record.

CHAIRMAN DEASON: It will be identified as Exhibit 1 and without objection shall be admitted.

MS. KEATING: The next one is Stip 1, which contains AT&T and MCI WorldCom's responses to discovery.

CHAIRMAN DEASON: That will be Exhibit 2. Without objection Exhibit 1 is admitted.

MS. KEATING: The third one is Stip 2, which contains BellSouth's responses to discovery.

CHAIRMAN DEASON: It will be identified as Exhibit 3, and without objection shall be admitted.

MS. KEATING: The fourth one is Stip 3, which contains GTE-Florida's responses to discovery.

CHAIRMAN DEASON: It will be identified as Exhibit 4, and without objection shall be admitted.

MS. KEATING: The fifth one is Stip 4, which contains Sprint's responses to discovery.

CHAIRMAN DEASON: That will be identified as Exhibit 5, and without objection shall be admitted.

MS. KEATING: The sixth one is Stip 5, which contains Supra's responses to discovery.

CHAIRMAN DEASON: That will be identified as Exhibit 6, and without objection shall be admitted.

MS. KEATING: The seventh one is Stip 6, which is a confidential exhibit that contains BellSouth's responses to discovery.

CHAIRMAN DEASON: That will be identified as Exhibit 7, and without objection shall be admitted.

COMMISSIONER JACOBS: I'm sorry, I skipped over one. I apologize.

MS. KEATING: The eighth one is Stip 7, which is also a confidential exhibit, and it contains Sprint's responses to discovery.

CHAIRMAN DEASON: That will be identified as Exhibit 8, and without objection shall be admitted.

MS. KEATING: And the ninth one is Stip 8, which is also a confidential exhibit, and it contains GTE-Florida's responses to discovery.

CHAIRMAN DEASON: It will be identified as Exhibit 9, and without objection shall be admitted.

MS. KEATING: Next are all the deposition transcripts and exhibits that the parties have agreed may be entered into the record at this time.

CHAIRMAN DEASON: That will be identified as Exhibit 10, and without objection shall be admitted.

(Exhibits 1 through 9 marked for identification and admitted into evidence.)

MS. KEATING: Would you like for me to go through -- do you want to make this a composite exhibit that contains all of the deposition transcripts?

CHAIRMAN DEASON: No, let's go through each one of those individually.

MR. MELSON: Mr. Chairman, the next item in my stack was Confidential Stip 9.

MS. KEATING: I'm sorry, he is correct. There is one more, Stip 9, that should be the tenth exhibit. And it is a confidential exhibit of MCI Worldcom's supplemental responses to discovery.

CHAIRMAN DEASON: Okay. And that is Exhibit 10, correct?

MS. KEATING: Correct.

CHAIRMAN DEASON: And without objection it is admitted.

(Exhibit 10 marked for identification and admitted into the record.)

MS. KEATING: Then moving to 11, which is the deposition transcripts. That would be KWD-D, which is Witness Dickerson's deposition transcript and exhibits.

CHAIRMAN DEASON: That would be Exhibit 11, and without objection shall be admitted.

MS. KEATING: Exhibit 12 is GDJ-D, which is Witness Jacobson's deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 12 will be admitted without objection.

MS. KEATING: Thirteen is CB-D, which are Witness Bentley's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection Exhibit 13 shall be admitted.

MS. KEATING: Number 14 will be DDC-D, which is Witness Caldwell's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection Exhibit 14 shall be admitted.

MS. KEATING: Fifteen is RSB-D, which is Witness Billingsley's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection Exhibit 15 shall be admitted.

MS. KEATING: Sixteen is WJB-D, which is Witness Barta's deposition transcript.

CHAIRMAN DEASON: Without objection Exhibit 16 shall be admitted.

MS. KEATING: Seventeen is AJV-D, which is Witness Varner's deposition transcript and exhibit.

CHAIRMAN DEASON: Exhibit 17 shall be admitted without objection.

MS. KEATING: Eighteen is DAN-D, which is Witness Nilson's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection Exhibit 18 shall be admitted.

MS. KEATING: Nineteen is AES-D, which is Witness Sovereign's deposition transcript and exhibits.

CHAIRMAN DEASON: And Exhibit 19, without objection, shall be admitted.

MS. KEATING: 20 is MRN-D, which is Witness Norris' deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 20 without objection shall be admitted.

MS. KEATING: 21 is MJM-D, which is Witness Majoros' deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 21 without objection shall be admitted.

MS. KEATING: 22 is JAH-D, which is Witness Holmes' deposition transcript.

CHAIRMAN DEASON: And without objection Exhibit

22 shall be admitted.

MS. KEATING: Twenty-three is JIH-D, which is Witness Hirshleifer's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection Exhibit 23 shall be admitted.

MS. KEATING: Twenty-four is GDC-D, which is Witness Cunningham's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection, Exhibit 24 shall be admitted.

MS. KEATING: Twenty-five is JDQ-D, which is Witness Quackenbush's deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 25 shall be admitted without objection.

MS. KEATING: Twenty-six is JK-D, which is Witness King's deposition transcript and exhibits.

CHAIRMAN DEASON: Without objection, Exhibit 26 shall be admitted.

MS. KEATING: Twenty-seven is GSF-D, which is Witness Ford's deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 27 without objection shall be admitted.

MS. KEATING: Twenty-eight is JWS-D, which is Witness Sichter's deposition transcript and exhibits.

CHAIRMAN DEASON: Exhibit 28, without objection shall be admitted.

MS. KEATING: And 29 is DBT-D, which is Witness Trimble's deposition transcript and exhibits.

CHAIRMAN DEASON: And without objection, Exhibit 29 shall be admitted.

(Exhibit Number 11 through 29 marked for identification and entered into the record.)

MS. KEATING: Those are all the stipulated exhibits that we have at this time. As I understand it, however, BellSouth would like to take up the responses to its discovery.

CHAIRMAN DEASON: Very well.

MR. ROSS: Mr. Chairman, BellSouth would like to put into the record the following discovery responses from the following parties: The responses of ALLTEL, dated July 14, 2000.

CHAIRMAN DEASON: Those responses will be identified as Exhibit 30. Without objection? Hearing none, show Exhibit 30 admitted.

(Exhibit Number 30 marked for identification and entered into the record.)

MR. ROSS: The discovery responses of AT&T as set forth in a letter from Mr. Jim Lamoureux dated July 14, 2000.

CHAIRMAN DEASON: That will be identified as Exhibit 31.

MR. LAMOUREUX: Chairman Deason, I don't have any objection to making it a part of the record, but that response was produced to BellSouth by AT&T as a proprietary document pursuant to a protective agreement that we have with BellSouth in this proceeding.

CHAIRMAN DEASON: Has there been a request of the Commission to have that information deemed confidential?

MR. LAMOUREUX: Well, it was produced in discovery to BellSouth, and it was produced to BellSouth pursuant to the protective agreement we have. AT&T did not make any effort to make it a part of this proceeding, that is what BellSouth is doing right now.

CHAIRMAN DEASON: BellSouth, what procedures have you followed to ensure the confidentiality of this information?

MR. ROSS: We received the information on Friday, and BellSouth has agreed to treat it as confidential. However, BellSouth does not agree that this information is in any way confidential. And, in fact, AT&T reports its depreciation lives in its annual report.

However, if this information is going to be provided to the staff and included in the record, I suspect AT&T will have to make a request for confidential classification at some point in time in which case we

could argue whether or not it is, in fact, entitled to protection as proprietary information at a later date.

CHAIRMAN DEASON: Staff, can we accept this information as confidential until the matter can be resolved, if it has to be resolved?

MS. KEATING: I believe if AT&T notes for the record that they intend to file a notice of intent to request confidential treatment today then that would be sufficient.

CHAIRMAN DEASON: Very well.

MR. LAMOUREUX: We will do that.

CHAIRMAN DEASON: With that understanding, then, Exhibit 31 is admitted.

(Exhibit Number 31 marked for identification and entered into the record.)

MR. ROSS: The next response, Mr. Chairman, is from Covad Communications dated July 10, 2000.

CHAIRMAN DEASON: That will be identified as Exhibit 32. Without objection, Exhibit 32 shall be admitted.

(Exhibit Number 32 marked for identification and entered into the record.)

MR. ROSS: The next discovery response is Florida Digital Network's discovery responses dated July 13, 2000.

CHAIRMAN DEASON: That will be identified as Exhibit 33, and without objection, Exhibit 33 shall be admitted.

(Exhibit Number 33 marked for identification and entered into the record.)

MR. ROSS: The next responses are from MCI WorldCom dated July 14, 2000, which also includes a clarifying e-mail sent to me from Greg Darnell with MCI WorldCom explaining their discovery responses.

CHAIRMAN DEASON: The responses with the e-mail will be identified as Exhibit 34.

(Exhibit Number 34 marked for identification and entered into the record.)

MR. MELSON: Commissioner, again, these were provided to BellSouth on a confidential basis. Part of this is the staff's confidential stipulated Exhibit Number 9, I believe. We did file a copy with the staff. We did file a notice of a claim of confidentiality with the Commission, so at this point I believe this information is properly protected.

CHAIRMAN DEASON: Very well. And with that understanding and without objection, Exhibit 34 shall be admitted.

MR. ROSS: The next responses are from Intermedia Communications.

CHAIRMAN DEASON: That will be identified as Exhibit 35. Without objection, Exhibit 35 shall be admitted.

(Exhibit Number 35 marked for identification and entered into the record.)

MR. ROSS: The next one are responses from Rhythms Links, Inc. dated July 7, 2000.

CHAIRMAN DEASON: That will be identified as Exhibit 36. Without objection, Exhibit 36 shall be admitted.

(Exhibit Number 36 marked for identification and entered into the record.)

MR. ROSS: Mr. Chairman, the last one is the amended responses of Time Warner Telecom of Florida LP, dated July 17, 2000.

CHAIRMAN DEASON: That will be identified as Exhibit 37, and without objection, Exhibit 37 shall be admitted.

(Exhibit Number 37 marked for identification and entered into the record.)

MR. MELSON: Mr. Chairman, I know many of these were served on BellSouth very late in the game. I would ask if BellSouth could provide at least my clients with a copy of the exhibits as they are being introduced just so we are sure we have got what officially is going into the

record.

MR. ROSS: Mr. Chairman, I have copies for all the parties and for the staff.

CHAIRMAN DEASON: Very well.

MR. MELSON: Thank you.

CHAIRMAN DEASON: Other preliminary matters?

MR. WAHLEN: Chairman Deason, this is Jeff Wahlen for ALLTEL. ALLTEL has not taken a position on the depreciation issues that are going to be heard in this part of the hearing, so I would like to be excused from the hearing.

CHAIRMAN DEASON: I started to say something, but I won't. You certainly may be excused.

MR. WAHLEN: Thank you very much.

CHAIRMAN DEASON: Anybody else want to follow Mr. Wahlen's lead? It may be tempting, right?

Other preliminary matters? Are we prepared then to -- I did not find anything in the prehearing order indicating there was going to be opening statements, so I assume there will not be.

MS. KEATING: That's correct.

CHAIRMAN DEASON: And we can proceed then to hearing witnesses. We have three scheduled for this phase of the hearing. I will ask all three witnesses -- hopefully they are present -- to please stand and raise

your right hand.

(Witnesses sworn collectively.)

CHAIRMAN DEASON: Thank you. Please be seated.

MS. KEATING: Mr. Chairman, may I suggest before we move to the witnesses that are actually here today that we go ahead and take up the testimony and exhibits of the witnesses that have been excused.

CHAIRMAN DEASON: Yes. I think that would be preferable.

MS. KEATING: I believe the first one is Witness Varner.

CHAIRMAN DEASON: Okay. Staff moves that the prefiled testimony of Witness Varner -- are we doing direct and rebuttal at the same time?

MS. KEATING: That is correct.

CHAIRMAN DEASON: Okay. Witness Varner's testimony without objection shall be inserted into the record. And we need to identify any exhibits?

MS. KEATING: He has Exhibits AJV-1, AJV-1R, and AJV-2R.

CHAIRMAN DEASON: They will be identified as Composite Exhibit Number 38, and without objection shall be admitted.

(Exhibit Number 38 marked for identification and entered into the record.)

BELLSOUTH TELECOMMUNICATIONS, INC.

DIRECT TESTIMONY OF ALPHONSO J. VARNER

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 990649-TP

MAY 1, 2000

Q. PLEASE STATE YOUR NAME, YOUR POSITION WITH BELLSOUTH TELECOMMUNICATIONS, INC. ("BELLSOUTH") AND YOUR BUSINESS ADDRESS.

A. My name is Alphonso J. Varner. I am employed by BellSouth as Senior Director for State Regulatory for the nine-state BellSouth region. My business address is 675 West Peachtree Street, Atlanta, Georgia 30375.

Q. PLEASE GIVE A BRIEF DESCRIPTION OF YOUR BACKGROUND AND EXPERIENCE.

A. I graduated from Florida State University in 1972 with a Bachelor of Engineering Science degree in systems design engineering. I immediately joined Southern Bell in the division of revenues organization with the responsibility for preparation of all Florida investment separations studies for division of revenues and for reviewing interstate settlements.

Subsequently, I accepted an assignment in the rates and tariffs organization with responsibilities for administering selected rates and tariffs including

preparation of tariff filings. In January 1994, I was appointed Senior Director of Pricing for the nine-state region. I was named Senior Director for Regulatory Policy and Planning in August 1994, and I accepted my current position as Senior Director of Regulatory in April 1997.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony addresses the policy issues related to the cost studies and price development for unbundled network elements ("UNEs") and interconnection that BellSouth offers to Alternative Local Exchange Carriers ("ALECs"). The following areas are discussed in my testimony: 1) the policy foundations underlying the proposed rates; 2) effect of the proposed rates on implementation of those policies; and, 3) development of the proposed rates. Specifically, I address issues 1, 2a, 2b, 4a, 4b, 5, 6, and 9 through 13 as identified by the Florida Public Service Commission's ("Commission's") Tentative List of Issues contained in its Second Revised Order on Procedure dated March 16, 2000 (PSC-00-0540-PCO-TP).

Q. PLEASE IDENTIFY THE OTHER BELLSOUTH WITNESSES FILING DIRECT TESTIMONY AND BRIEFLY DESCRIBE THE PURPOSE OF THEIR TESTIMONY.

A. In addition to my testimony, BellSouth presents the direct testimony of the following witnesses and the topics covered:

Ms. Daonne Caldwell	BellSouth's cost methodology for recurring and nonrecurring costs
Mr. Walter Reid	Appropriate methodology for including shared and common costs in cost studies
Mr. David Cunningham	Appropriate economic lives for use in cost studies
Dr. Randall Billingsley	Appropriate cost of capital in cost studies
Mr. Joe Page	Appropriate switching costs assumptions in cost studies
Mr. Keith Milner	Network issues
Mr. Jim Stegeman	Loop Model development

Q. GENERALLY, WHAT IS THE PURPOSE OF THIS PROCEEDING?

A. The primary goal of this proceeding is to establish rates for UNEs and interconnection that are just and reasonable, under the Telecommunications Act of 1996 ("Act"). The Commission previously established rates for several UNEs and interconnection services in arbitration proceedings. BellSouth has developed updated cost studies for those UNEs and interconnection services. The rates the Commission establishes is this proceeding will replace the rates established by the Commission in those arbitration proceedings. In addition, several new UNEs, including UNE combinations, and geographic deaveraging have been required since the Commission previously established permanent rates. Permanent rates for those new requirements are also being established in this proceeding.

Issue 1: What factors should the Commission consider in establishing rates and

charges for UNEs (including deaveraged UNEs and UNE combinations)?

Q. HOW WILL THE RATES ESTABLISHED IN THIS PROCEEDING AFFECT THE DEVELOPMENT OF LOCAL COMPETITION IN FLORIDA?

A. The rates established in this proceeding will have profound effects on the continued development of competition in Florida. The outcome of this docket will affect:

- the nature and extent of competition
- how local competition will continue to develop
- which companies will choose to participate
- which customers will benefit from local competition
- economic development and the availability of advanced technologies.

All of these issues will be significantly impacted by the Commission's decision in this proceeding.

Q. PLEASE BRIEFLY COMMENT ON HOW PRICES FOR UNES AND INTERCONNECTION AFFECT THE ISSUES IDENTIFIED ABOVE.

A. In order to maintain an environment in which efficient competition will occur and provide the maximum benefit to consumers, local competition must be implemented in a fair and balanced manner. If prices for UNEs and interconnection services are set either too high or too low, then the

development of efficient competition in the local market, as intended by Congress, will not occur. Prices that are set either too high or too low will not, in the long run, benefit the consumer. If prices are set incorrectly, new investment won't materialize, and economic development will be thwarted. In addition, the market entry and investment decisions of competitors, including BellSouth, will be distorted.

Optimizing competitive development would require prices to be set, at a minimum, to cover the actual costs incurred by the Incumbent Local Exchange Carrier ("ILEC"). However, the FCC has adopted rules that require prices for UNEs and interconnection services to be set below an ILEC's actual cost, so a bias toward artificially low prices has already been created. The validity of the FCC's rules is currently being addressed by the United States Court of Appeals for the Eighth Circuit and a decision in that case could impact the prices established in this proceeding.

Q. WHAT DOES THE ACT SAY ABOUT PRICES FOR UNEs AND INTERCONNECTION SERVICES?

A. Congress established the obligation for ILECs to provide UNEs and interconnection, and established a pricing standard for those UNEs and interconnection services. That standard requires prices to be just and reasonable. Section 251(c)(3) of the Act establishes the pricing standard for unbundled network elements, by stating that the ILEC has "the duty to provide, to any requesting telecommunications carrier for the provision of a

telecommunications service, nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms and conditions that are just, reasonable, and nondiscriminatory in accordance with the terms and conditions of the agreement and the requirements of this section and section 252." (emphasis added)

Further, section 252(d)(1) of the Act provides guidelines for determining just and reasonable rates for UNEs and interconnection, stating that "determinations by a state commission of the just and reasonable rate for the interconnection of facilities and equipment for purposes of subsection (c)(2) of section 251, and the just and reasonable rate for network elements for purposes of subsection (c)(3) of such section -

(A) shall be--

(i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable); and,

(ii) nondiscriminatory, and

(B) may include a reasonable profit." (emphasis added)

Q. HOW DOES THE FCC REQUIRE PRICES TO BE SET?

A. The FCC's rules limit prices for UNEs and interconnection to the forward looking economic cost of the element. Economic cost is defined as the sum of the long run incremental cost plus a reasonable allocation of forward-looking

common costs.

The FCC's rules do not permit full cost recovery. However, these rules are currently effective and must be followed, which will result in prices being established below the appropriate level. Even though the Commission is bound to follow the FCC's rules at present, the Commission should consider when establishing prices that those rules already mandate that rates will be below the appropriate level. Any further reductions will only exacerbate the negative consequences that I will discuss later.

Q. HOW DO THE PRICES ESTABLISHED IN THIS PROCEEDING AFFECT UNIVERSAL SERVICE?

A. As discussed in more detail later in my testimony, if rates are set incorrectly, BellSouth's revenues are marginalized, and enormous pressure is created to substantially increase local rates, particularly in the rural areas where costs are higher. Obviously, these pressures could jeopardize universal service. Even if prices are set to recover all costs permitted by FCC rules, the prices in this proceeding will generate additional pressure on universal service.

Also, geographically deaveraged pricing places an additional burden on universal service. BellSouth has consistently maintained that geographic deaveraging should not precede the implementation of an appropriate universal service support mechanism and/or the implementation of adequate rate rebalancing. Both are necessary to accommodate the impact of deaveraging

UNEs for ALECs. The Commission will establish permanent deaveraged UNE prices in this proceeding. Such deaveraging will accelerate the erosion of subsidy from low cost urban customers to support high cost rural customers. As long as ILECs such as BellSouth have a continuing universal service obligation, there must be a mechanism in place to permit ILECs to recover costs for providing service in high cost areas.

Q. DOESN'T PRICE REGULATION PERMIT BELLSOUTH TO ADDRESS THIS UNIVERSAL SERVICE ISSUE?

A. Not to the extent that is needed. BellSouth currently is operating under a price regulation plan outlined in Florida Statutes. Under price regulation, BellSouth is precluded from raising certain rates for a specified period, and limitations apply to increases on other rates. Because of these restrictions, in addition to competitive pressures, BellSouth's ability to rebalance rates is severely constrained.

BellSouth's price regulation plan, while allowing some flexibility to meet competition as it develops in Florida, does not provide the flexibility necessary to timely move basic local exchange rates more toward the cost of providing the service. Until BellSouth can adjust these retail rates to better match their underlying costs, deaveraging simply increases an ALECs' profit margins in urban areas without increasing the level of competition in rural or other areas of Florida. Because geographic deaveraging will be implemented before an appropriate universal service fund is implemented and before a sufficient

degree of rate rebalancing can be accomplished, ALECs will have an unreasonable advantage created by regulatory fiat. ALEC's ability to attract high revenue, low cost customers will be unnecessarily increased in urban areas. ILECs like BellSouth will be left with an increased percentage of the low revenue, high cost customers who ultimately will bear the majority of BellSouth's network costs. Though BellSouth believes rate rebalancing should happen concurrent with or before deaveraging, the most important issue is to immediately address the implementation of an appropriate state universal service fund.

Q. HOW DO FLORIDA STATUTES AFFECT IMPLEMENTATION OF A UNIVERSAL SERVICE FUND?

A. The Florida Statutes permit this Commission to establish an interim universal service fund, but only the Legislature can establish a permanent fund. Presently, Florida Statutes allow the Legislature until January 1, 2001 to establish a permanent universal service fund. However, the Legislature is presently considering amendments to the current statute that would defer any requirement to address the permanent universal service fund until 2004. As such, based on the FCC's current timetable, which calls for geographic deaveraging of UNEs to be available by May 1, 2000, a universal service fund will not be in place in Florida when the federal requirement for geographic deaveraging goes into effect. We urge the Commission to establish an appropriate interim fund quickly.

Q. HOW WILL INCENTIVES TO INVEST IN NEW TECHNOLOGY BE AFFECTED BY PRICES THAT ARE NOT JUST AND REASONABLE?

A. Generally, incentives to invest in new technology are reduced by prices for UNEs and interconnection services that are not just and reasonable. As explained further below, both ALEC's and ILEC's incentives are reduced.

One consequence of establishing prices that are not just and reasonable is that such pricing creates inefficiency. Prices that are understated deter the ILEC from undertaking investments because it guarantees that the costs of those investments will not be recovered. An ILEC only has an obligation to unbundle its existing network. If UNE prices are too low, investments to expand or upgrade that network become much more speculative. Accordingly, incentives to expand that network into new areas and upgrade it with new technology are reduced. Where UNEs are available, ALECs will over-consume the ILEC's facilities and under-invest in their own facilities, even when investing in their own facilities is the efficient choice.

A consequence of pricing that insufficiently recovers shared cost is that it inappropriately encourages the ILEC to invest in technology that involves low shared cost (which reduces economies of scope) and high incremental costs, even if that is not the lowest cost technology. If shared costs are not fully recovered, the fact that shared cost technology is cheaper becomes irrelevant, since there will be no incentive for the ILEC to invest in the lower cost technology if it knows it will not be allowed to fully recover those shared

costs.

A third consequence of inadequate UNE prices is that it invites inefficient entry of ALECs by placing all of the risks of building and maintaining a network on the ILEC. The ALECs in effect get a "free ride" on BellSouth's network without the ALECs having to make any substantial investment. While ALECs have the option to use the ILEC's facilities for the economic life of those facilities, ALECs don't have to make any long-term commitments to use those facilities. The ALEC can utilize BellSouth facilities for a limited period, e.g., until it builds its own facilities to serve a customer. However, since BellSouth established the facilities, BellSouth must recover its costs whether an ALEC uses the facilities or not. Any costs not recovered from the ALEC who caused the costs, becomes a burden upon end users. If prices are not set to cover costs, then ALECs don't bring to the marketplace anything more than an arbitrage mechanism. This arbitrage allows them to avoid paying the costs they would otherwise have to pay in a competitive marketplace. End user customers are the losers in this arrangement.

Q. PLEASE COMMENT ON THE IMPORTANCE OF SHARED COST RECOVERY IN UNE PRICES.

A. As part of the cost of providing UNEs and interconnection services for the use of BellSouth's ubiquitous network, there are shared costs that benefit multiple network elements as well as common costs that benefit all elements. An appropriate portion of all of the costs of doing business must be included in the

prices for UNEs and interconnection. These shared and common costs do not "go away" if rates are set too low to recover them. Indeed, these costs remain and must be recovered by other services. Therefore, ALECs would directly benefit from the use of these facilities by enjoying lower rates which are being subsidized, in part, by BellSouth's retail end users. Since ALECs benefit from the use of the facilities that generate the costs in question, those ALECs should contribute to the recovery of the shared and common costs that result from economically efficient provisioning of those facilities.

Further aggravating this problem is the fact that technology is driving toward networks that have higher shared and lower direct costs. If shared costs are understated in UNE prices, the shortfall in recovery will grow as the network is upgraded. This condition merely exacerbates the previously discussed negative consequences of setting prices too low. The importance of adequate shared cost recovery has increased and will continue to increase in the future.

Q. ARE THERE ANY OTHER ASPECTS TO THIS RATE-SETTING PROCEEDING OF WHICH THE COMMISSION SHOULD BE AWARE?

A. Yes. Another troublesome outcome of setting prices too low would be the marginalization of the ILEC. Setting UNE and interconnection services prices at unreasonably low levels will hinder BellSouth's ability to compete because the ALECs will have an artificial pricing advantage over BellSouth. The ALEC will, therefore, be in a better position to "cherry pick" the more profitable, mainly business customers, and the ILEC will lose the low cost,

high margin, urban customers to competition. The ILEC will be left to serve the high cost, low margin, rural customers. Ultimately, since only the low margin customers will be left to cover the full cost of the network, prices for these predominantly rural customers would have to increase.

Q. PLEASE EXPLAIN FURTHER HOW INADEQUATE UNE PRICES AFFECT RETAIL PRICES.

A. Setting prices that do not cover actual costs establishes a vicious cycle that ultimately harms consumers. If the prices of the services provided to competitors do not cover the costs of providing the services, BellSouth will end up subsidizing its competitors. In that event, BellSouth must attempt to recover this revenue shortfall through its retail prices. Unfortunately, however, attempts to recover the shortfall in this manner will be unsuccessful. The competitor who is using the subsidized facilities will not have to recover this shortfall through its retail prices - prices which will remain lower than the incumbent's retail prices. Therefore, the competitor can undercut BellSouth's retail prices utilizing a subsidy provided by BellSouth's end users. The result is that this subsidy to competitors would ultimately be borne by those end users that have the fewest competitive options, e.g., rural residential customers.

In addition, by creating a high price umbrella for the competitor, all retail customers would pay higher prices than they would otherwise. The competitors benefit, but the end user loses. This does not seem fair when both the end-user and the ALEC are benefiting from, and share in, the use of

BellSouth's network. BellSouth must recover all of its costs to continue to be a viable concern, and all of the users of the network should contribute toward that recovery.

The Commission agreed that contribution above TSLRIC is appropriate, stating in Order No. PSC-96-1579-FOF-TP, that "[t]he rates cover BellSouth's TSLRIC costs and provide some contribution toward joint and common costs." (Order, page 33).

Q. WHAT ARE SOME CONSEQUENCES IF PRICES ARE SET TOO HIGH?

A. Since the FCC's pricing rules require prices to be understated, setting prices too high is not currently a condition the Commission will encounter. Nonetheless, setting UNE and interconnection prices too high will discourage ALECs from purchasing those elements from the ILEC. Of course, setting prices too high will give ALECs the maximum incentive to construct their own facilities and, in the long run, infrastructure competition will develop sooner. However, the incentive for the ALEC to compete by purchasing UNEs from the ILEC will be lessened.

The ultimate goal is to establish prices that are neither too low nor too high; to do otherwise will result in inefficient decisions, and, ultimately, it is the consumer who will suffer the consequences. However, given the current pricing rules, the Commission can only minimize the extent to which prices are set too low.

Q. ARE THERE ANY UNIQUE CONCERNS SURROUNDING NON-RECURRING PRICES?

A. Yes. All of the issues previously discussed apply both to recurring and non-recurring prices. However, the impact of inappropriate non-recurring prices is felt immediately. Non-recurring prices principally recover labor cost and direct expenses. These expenses are paid immediately by the ILEC. Thus, setting non-recurring prices too low will immediately begin to create the negative consequences that I previously discussed. Consequently, the Commission should be very careful to ensure that non-recurring prices fully recover the ILEC's costs that an ILEC is expected to incur.

In particular, the Commission should ensure that the costs allowed to be recovered matches the ILEC's obligations. For example, assume the costs for installing a UNE are based on providing it in seven days. The Commission should not then adopt performance measurements that require a shorter installation interval. Such action would increase the cost without providing for recovery. Order processing costs are another example. BellSouth incurs costs to process ALEC orders for UNEs and interconnection services. Those costs should be recovered in UNE prices.

Finally, non-recurring costs should recover the activities actually undertaken to provide the element. For example, a new technology that could reduce non-recurring costs should only be used as a basis for prices to the extent that it is

actually used by BellSouth to provide the element.

Q. BRIEFLY DESCRIBE THE COST STUDIES BELLSOUTH IS SUPPORTING IN THIS PROCEEDING.

A. The studies BellSouth filed on April 17, 2000 are based on forward-looking economic costs. The most voluminous part of the study is the development of Total Element Long Run Incremental Cost ("TELRIC") as defined by the FCC in its First Report and Order in CC Docket No. 96-98 released August 8, 1996 ("FCC Order"). These TELRIC results, for both recurring and non-recurring costs are the subject of Ms. Caldwell's testimony. Several other witnesses support specific inputs for the TELRIC study. The other component of economic cost is an allocation of common costs as discussed in Mr. Reid's testimony. The prices proposed are the sum of TELRIC and common costs.

Q. HAS THE FLORIDA COMMISSION ADOPTED A COST METHODOLOGY?

A. Yes. In Order No. PSC-96-1531-FOF-TP, issued December 16, 1996 (BellSouth/MFS arbitration), the Commission stated ". . . the appropriate cost methodology to determine prices for unbundled elements should approximate TSLRIC. This is the pricing policy we adopted in our state proceeding on unbundling and resale." Order at p. 6. Additionally, in establishing permanent rates in the AT&T/MCI/ACSI consolidated arbitration proceedings, the Commission stated in Order No. PSC-96-1579-FOF-TP dated December 31,

1996 "[W]e find it appropriate to set permanent rates based on BellSouth's TSLRIC cost studies." [Emphasis added] Order at p. 33.

Q. WHAT EFFECT SHOULD EXISTING FCC PRICING RULES HAVE ON THIS COMMISSION'S POLICY FOR UNE AND INTERCONNECTION SERVICES PRICES?

A. Unless and until the FCC's pricing rules are invalidated, this Commission is obviously bound to follow them. However, this Commission should develop its pricing policy for UNEs and interconnection services to enhance the development of facilities-based competition with its attendant benefits for economic development. If the Commission follows this course, it will be positioned to establish appropriate prices in the event the Eighth Circuit Court rejects the FCC's pricing rules. Such a policy requires, at a minimum, that UNE prices cover the full actual costs of the elements and that prices for preexisting combinations of UNEs be set at full market value.

Limitations of existing rules should not deter this Commission from establishing the appropriate policy. Implementation of that policy may be delayed by the Eighth Circuit Court's review of the FCC's rules. But this Commission should ensure that it has a clear identification of the appropriate objective so that it can achieve that objective when the rules permit it to do so.

Q. SHOULD THE COMMISSION ADOPT A POLICY OF LIMITING PRICES TO ECONOMIC COSTS?

A. No, even though that is what the FCC's rules currently require. First, pricing should account for the cost of the element plus the market, regulatory and competitive conditions that exist. Further, pricing is not so simplistic that it can be narrowed to an exact numerical exercise. Prices for UNEs should be based on cost, but that is not the only factor that should be considered. Another consideration is that prices should also be functional in the marketplace and be consistent with prices for similar services.

Second, prices should be set so that sellers and buyers make correct economic choices. Prices should cover total costs. This requirement is necessary for a firm to remain in business and to make efficient investment decisions.

Third, BellSouth as well as any multiservice company, must recover its actual costs in prices. Although BellSouth acknowledges that competition will appropriately drive prices toward cost, BellSouth does not believe that the level of cost would be economic cost as defined by the FCC. BellSouth submits that prices will move toward a point where all valid costs are recovered. Those costs include shared costs, common costs and historical costs.

Q. DOES PRICING AT ECONOMIC COST PROVIDE FOR A REASONABLE PROFIT AS PERMITTED BY THE ACT?

A. It certainly does not. Proponents of this theory equate economic profit with cost of capital, which is not an appropriate comparison. Cost of capital is a

cost of doing business. It is well accepted that an economic profit cannot be realized until all costs, including cost of capital, have been recovered. Although pricing at TELRIC would provide for the cost of capital attributable to the investments directly related to the specific element involved, it would not provide for any contribution to shared or common costs or any cost of capital on investment not related to a specific service. Until BellSouth recovers all of its costs, and cost of capital on its total operations is a cost, BellSouth does not make a profit. BellSouth witness Mr. Randall Billingsley addresses cost of capital in his testimony.

Issue 2(a): What is the appropriate methodology to deaverage UNEs and what is the appropriate rate structure for deaveraged UNEs?

Q. PLEASE DISCUSS THE GENERAL POLICY CONSIDERATIONS ASSOCIATED WITH GEOGRAPHIC DEAVERAGING OF UNEs.

A. UNEs are generally used by ALECs to compete with services offered at retail rates by ILECs. Consequently, the relationship between UNE and retail rates affects competitive development. Historically, it has been the intent and practice of regulators to deaverage rates for basic service in an inverse relationship to costs. Such pricing practices served both regulatory and political purposes and incorporated implicit subsidies to ensure affordable local service for all urban and rural customers. Conversely, UNE prices are based on costs and will be deaveraged in a direct relationship to cost.

Deaveraging of UNEs will result in a rate structure that is inconsistent with the existing pricing practices for retail rates for basic local exchange service as established by this Commission. The present rate structure in Florida incorporates long standing policies of purposefully pricing some services markedly above costs in order to price other services, such as residential basic local exchange service, at or below cost. Further, basic local exchange service rates have been established with a direct relationship to the number of lines in an exchange's local calling area – the greater the number of lines in a particular exchange's local call area, the higher the price for the basic service. Deaveraging will create loop prices that vary in the opposite direction from the prices for retail services.

Q. WHAT SHOULD THE COMMISSION DO TO ADDRESS THE PROBLEMS DISCUSSED ABOVE?

A. The Commission should encourage rate rebalancing and establish a universal service fund as quickly as possible. This is important because the unbundled loop will be used by ALECs to compete for these retail customers. Deaveraging loop prices would result in lower rates in the urban area where retail prices are currently the highest. In rural areas, the reverse would be true. However, in rural area, deaveraged unbundled loop prices set high enough to cover costs would be irrelevant because the ALEC could simply resell the low priced retail service to rural customers. As a result, deaveraging, without concomitant rate rebalancing or creation of a state universal service fund, simply creates another opportunity for ALECs to engage in inappropriate

arbitrage of the pricing schedule. This arbitrage will ultimately lead to higher prices for rural customers as ALECs usurp the contribution contained in the prices charged in urban areas that currently make lower rural prices possible.

It is very important to recognize that ALECs use unbundled loops to compete with residence and business retail local exchange services. As such, the pricing implications of deaveraging the loop cannot be divorced from the price of local exchange services.

Q. WHAT OBLIGATION DOES THIS COMMISSION HAVE TO ESTABLISH DEAVERAGED RATES FOR UNBUNDLED NETWORK ELEMENTS?

A. The FCC's Rule 51.507 (f) requires state commissions to establish different rates (prices) for elements in at least three cost-related rate zones within the state to reflect geographic cost differences. With the November 2, 1999 release of the FCC's Order in CC Docket No. 96-46, the stay of section 51.507(f) was lifted effective May 1, 2000. As such, state commissions are required to establish rates for applicable UNEs in at least three geographic areas pursuant to rule 51.507(f) by May 1, 2000.

Q. PLEASE EXPLAIN HOW BELLSOUTH PROPOSES THAT THE DEAVERAGED ZONES FOR LOOPS AND LOCAL CHANNELS BE ESTABLISHED IN FLORIDA.

A. Rate group costs tend to follow the zoning methodology. Existing local

exchange rate groups were mapped into one of three zones. BellSouth witness Ms. Caldwell addresses in her testimony the compilation of the cost data and further explains the methodology BellSouth used to establish the three deaveraged rate zones. The proposed deaveraged rates are contained in Exhibit AJV-1 to my testimony.

Q. PLEASE EXPLAIN WHY IT IS APPROPRIATE TO "MAP" THE EXISTING RATE GROUPS TO THREE DEAVERAGED RATE ZONES.

A. "Rate group-to-zone" mapping best represents the competitive market environment in Florida, thereby promoting competition in all areas of Florida. Utilizing local exchange rate groups to define deaveraged zones for UNEs meets the requirements set forth by the FCC and provides consistency between the structure of BellSouth's retail, resale and UNE rates. Further, it is more understandable to customers because customers with similar calling areas and located in the same geographic region will be in the same deaveraged zone for UNE pricing.

Q. IS USING RATE GROUPS TO DEFINE THE ZONES COMPLIANT WITH FCC RULES?

A. Yes. BellSouth proposes deaveraging UNE prices to reflect the forward-looking economic cost differences in three geographic areas. BellSouth's deaveraged prices will be the forward-looking economic cost for the zone where that price applies. Utilizing existing rate groups to define the

geographic area is consistent with the FCC's rules. In fact, the rules specifically permit using the same zones developed for other services as one means of defining the area. The FCC's Rule 51.507(f) in part states, "state commissions may use existing density-related zone pricing plans described in § 69.123 of this chapter, or other such cost-related zone plans established pursuant to state law."

Q. WHY SHOULD ZONES FOR UNBUNDLED LOOPS AND LOCAL CHANNELS BE DEFINED BASED ON RATE GROUPS INSTEAD OF WIRE CENTERS?

A. Defining such zones by rate groups applies a consistent method that recognizes the proximity of customers to each other. BellSouth's proposed prices equal TELRIC to reflect geographic differences. The existing local exchange rate groups were grouped into three zones in Florida. The proposed price is the average TELRIC cost in that zone. Utilizing local exchange rate groups to deaverage UNEs provides consistency between the structure of BellSouth's retail, resale and UNE prices. Further, customers who are located in the same geographic area and who have similar calling areas will be in the same deaveraged zone for UNE pricing. Simply using existing rate groups as the basis for establishing pricing zones results in consistent prices for customers within the same geographic markets.

Q. PLEASE PROVIDE AN EXAMPLE OF HOW DEAVERAGED RATES BASED ON WIRE CENTERS ARE NOT CONSISTENT WITHIN THE

SAME GEOGRAPHIC MARKETS.

A. A simple example can be found by looking at the Commission's February 22, 2000 Order approving the stipulation establishing interim deaveraged rates. (Order No. PSC-00-0380-TP, in Docket No. 990649-TP) This stipulation contains three deaveraged rate zones that were based on wire center costs. The stipulated interim rate for an unbundled 2-wire voice grade analog loop in zone 1 is $13.75, zone 2 is $20.13 and zone 3 is $44.40. In the stipulation, two wire centers located in Sebastain, Florida are assigned to two different deaveraged pricing zones. The loops served by the Sebastain Main wire center are priced at zone 2 rates while the loops served by the neighboring Sebastain Fellsmere wire center are priced at in zone 3 rates. As such, ALECs choosing to serve end users in Sebastain would most likely charge rates that could vary by over $20 per month to end users that reside in close proximity to one another. Such inconsistency is less likely to occur when deaveraged pricing zones are established based on rate groups.

Issue 2(b): For which of the following UNEs should the Commission set deaveraged rates?

(1) loops (all);

(2) local switching;

(3) interoffice transport (dedicated and shared);

(4) other (including combinations).

Q. WHICH UNEs SHOULD BE DEAVERAGED?

A. There is no dispute that the recurring cost of an unbundled loop and local channel varies by geographic location. These prices are required to be deaveraged. However, other unbundled network elements either do not display a significant level of cost variation by geographic location or have price structures that already account for geographic cost differences. Thus, BellSouth believes that the recurring cost of the local loop and local channel are the only network elements that should be deaveraged in this proceeding. This issue is addressed in greater detail in the testimony of Ms. Caldwell.

Q. WHY SHOULDN'T SWITCHING PRICES BE DEAVERAGED?

A. Switching costs do not vary significantly by geographic location. None of the factors that make the loop cost vary are present with respect to switching cost calculations. The physical characteristics of the loop and the placement costs associated with that loop vary by geographic location due to weather, and distance. However, these factors do not impact switching costs to any great degree.

Q. WHY SHOULDN'T OTHER UNE PRICES BE DEAVERAGED?

A. The cost of other unbundled network elements may vary by geographic location, but these cost differences are reflected in the rate structures without the need for further deaveraging. An example is interoffice transport. The rate structure for interoffice transport is on a per mile basis. Facility length is the

principal driver of cost differences in different geographic areas. Since the price of interoffice transport will vary according to facility length, the price structure for interoffice transport already accounts for geographic differences. Thus, there is no reason to include interoffice transport in a separate deaveraging scheme.

Every state commission in BellSouth's region that to date has established deaveraged rates for unbundled network elements has done so only with respect to loops (and certain combinations involving the loop). *See, e.g.*, Order Adopting Joint Stipulation for Deaveraged UNE Rates, *In re: Review of Cost Studies, Methodologies, and Cost-Based Rates for Interconnection and Unbundling of BellSouth Telecommunications Services,* Docket No. 7061-U (Ga. Public Service Comm'n April 4, 2000) (approving stipulation to deaverage recurring rates for unbundled loops and certain UNE combinations involving the loop); Order, *In re: An Inquiry Into the Development of Deaveraged Rates For Unbundled Network Elements*, Administrative Case No. 382 (Ky. Public Service Comm'n March 24, 2000) (same).

Q. WHAT IS BELLSOUTH'S OBLIGATION TO PROVIDE UNE COMBINATIONS TO ALECs?

A. Consistent with the reinstatement of FCC Rule 51.315(b), ALECs may request access to network elements that BellSouth currently combines in its network, which BellSouth may not separate except upon request. According to the FCC, "currently combines" mean that such elements are in fact combined by

BellSouth in BellSouth's network to provide service to a particular customer at a particular location. The FCC further confirmed that BellSouth presently has no obligation to combine network elements for ALECs, when those elements are not currently combined in BellSouth's network.

Q. WHICH UNE COMBINATIONS SHOULD BE DEAVERAGED?

A. Because many UNE combinations involve the use of the loop or local channel, it is appropriate for the Commission to establish deaveraged prices for currently combined UNE combinations that include the loop or local channel. As explained in greater detail in Ms. Caldwell's testimony, when it comes to UNE combinations, there may be cost differences in both recurring and nonrecurring rates when an ALEC orders and BellSouth provisions certain combinations of network elements that are currently combined in BellSouth's network.

Q. IS BELLSOUTH PROPOSING RATES FOR ALL COMBINATIONS OF NETWORK ELEMENTS THAT ARE CURRENTLY COMBINED IN BELLSOUTH'S NETWORK?

A. No. As set forth in AJV-1, BellSouth is proposing recurring and nonrecurring rates for 24 UNE combinations, which represent the types of loop-port and loop or local channel-transport combinations that ALECs have most frequently requested from BellSouth. BellSouth makes available other combinations of network elements consistent with its obligations under Rule 51.315(b). Once

the Commission establishes rates for these most frequently requested combinations, BellSouth believes that the rates for other combinations an ALEC may request can be handled on a negotiated basis between the parties. Of course, to the extent the parties cannot reach agreement on appropriate rates, either party could ask the Commission to arbitrate the issue.

Issue 4(a): Which subloop elements, if any, should be unbundled in this proceeding, and how should prices be set?

Issue 4(b): How should access to such subloop elements be provided, and how should prices be set?

Q. WHICH SUBLOOP ELEMENTS IS BELLSOUTH OBLIGATED TO UNBUNDLE?

A. The FCC's Third Report and Order in CC Docket No. 96-98, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996 ("319 Order"), defines the subloop network element as any portion of the loop that is technically feasible to access at terminals in the ILEC's outside plant, including inside wire. Consistent with the FCC's 319 Order, BellSouth makes the following subloop elements available to ALECs on an unbundled basis:

The *Network Interface Device* ("NID") provides a single line termination device or that portion of a multiple line termination device required to terminate a single line or circuit. The NID, located on the customer's premises, establishes the official network demarcation point

between a telecommunications company and its end user customer. BellSouth provides access to the NID on an unbundled basis, therefore, an ALEC may order a stand alone NID from BellSouth. However, when an ALEC orders an unbundled loop, BellSouth provides the NID also. In all cases where BellSouth provisions a loop, it must be properly grounded.

Loop feeder provides a transmission path between the feeder distribution interface and the telephone company central office.

Loop distribution or distribution media provides a transmission path between a feeder distribution interface and the NID at the customer's premises. If the ALEC were to take loop distribution as an unbundled element, then the ALEC would presumably provide its own feeder facilities to its own switch.

Loop concentration enables ALECs to concentrate up to 96 sub-loops on 2 DS1s for the purpose of connecting the sub-loops (at a concentrated level) to BellSouth's feeder system.

Inside Wire, as described by the FCC in its 319 Order, includes wire owned and controlled by the ILEC on or near an end user customer premises. Such inside wire would include access to BellSouth's Network Terminating Wire ("NTW") and Intrabuilding Network Cable

("INC"). Inside wire on the customer's side of the demarcation point (typically the NID) is owned and controlled by the customer.

Q. DOES BELLSOUTH'S PETITION FOR RECONSIDERATION ON THE DEFINITION OF INSIDE WIRE AFFECT THE RATES PROPOSED IN THIS PROCEEDING?

A. No. On February 17, 2000 BellSouth petitioned the FCC to reconsider its definition of inside wire adopted in the 319 Order. Specifically, BellSouth has requested the FCC to continue to use its historic definition of inside wire and not expand it to include Network Terminating Wire and Intrabuilding Network Cable. However, regardless of the outcome of BellSouth's Petition, the rates proposed for NTW and INC comply with the FCC's rules.

Q. SHOULD THE COMMISSION EXPAND THE LIST OF SUBLOOP ELEMENTS BEYOND THOSE IDENTIFIED BY THE FCC IN ITS 319 ORDER?

A. No. The subloop elements that BellSouth currently provides to ALECs are more than sufficient to allow an efficient carrier a meaningful opportunity to compete. BellSouth believes it is not necessary for this Commission to require BellSouth to provide any additional subloop elements beyond those currently required by the FCC. In the 319 Order, the FCC determined which UNEs are "necessary" and where failure to provide such UNEs "impairs" the ability of an

efficient ALEC to provide telecommunications services. To my knowledge there are no elements that the FCC did not examine in that proceeding.

The FCC concluded that Section 251(d)(3) of the Act grants state commissions the authority to impose additional obligations upon incumbent LECs beyond those imposed by the national list, as long as they meet the requirements of section 251 of the Act and Section 51.317 of the FCC's Rules. Should this Commission wish to consider imposing additional unbundling obligations on BellSouth, the requirements of Rule 51.317 obligate the Commission to apply the "necessary and impair" standard in its analysis and consideration.

Q. HOW SHOULD THE PRICES FOR UNBUNDLED SUBLOOP ELEMENTS BE SET?

A. The prices for unbundled subloop elements should be established using the same cost methodology used for other unbundled network elements. BellSouth witness, Ms. Daonne Caldwell, filed cost studies and testimony in support of the appropriate cost methodology for establishing UNE prices. Prices for the subloop elements that BellSouth makes available to ALECs on an unbundled basis are contained in Exhibit AJV-1 attached to my testimony.

Issue 5: For which signaling networks and call-related databases should rates be set?

Q. PLEASE DESCRIBE BELLSOUTH'S OBLIGATIONS RELATIVE TO PROVIDING ALECS WITH ACCESS TO ITS SIGNALING NETWORKS AND CALL-RELATED DATABASES.

A. The FCC's Rule 51.319 requires BellSouth to provide nondiscriminatory access to signaling networks and call-related databases. When an ALEC purchases unbundled switching, BellSouth provides access to its signaling network from that switch in the same manner in which BellSouth obtains such access itself. When an ALEC provides its own switching facilities, BellSouth also provides access to its signaling network for each of the ALEC's switches in the same manner as BellSouth connects one of its own switches. For query and call-related database response, BellSouth provides access to its call-related databases.

Q. WHAT ARE THE RATES BELLSOUTH PROPOSES FOR ACCESS TO ITS SIGNALING NETWORK AND CALL-RELATED DATABASES?

A. BellSouth proposes the rates contained in Exhibit AJV-1, attached to my testimony, for access to CCS7 Signaling Transport and the following call-related databases:

- 800 Access Ten Digit Screening
- Line Information Database Access (LIDB)
- BellSouth Calling Name Database Service (CNAM)
- BellSouth Access to E911 Service
- Local Number Portability (LNP) Query Service

Issue 6: Under what circumstances, if any, is it appropriate to recover non-recurring costs through recurring rates?

Q. WHAT IS BELLSOUTH'S POSITION ON THIS ISSUE?

A. Several factors must be considered in order to determine if it is appropriate to price a particular service such that its recurring rates recover non-recurring costs. One such factor is how long will the service be installed or remain in service? This factor is important to ensure that the non-recurring costs can be recovered and will not be foregone if the service is removed or disconnected too soon. In a competitive environment, a provider's ability to predict how long a customer will remain on the provider's network is limited. Absent some type of volume and term agreement or termination liability, the risk of not recovering nonrecurring costs increases.

Another factor to consider is the impact that the recovery of the non-recurring costs will have on the recurring rate. Depending on the amount of costs to be recovered, spreading the non-recurring costs over a recurring rate could cause the recurring rate to be inappropriately high.

Issue 9(a): What are the appropriate recurring rates (averaged or deaveraged as the case may be) and non-recurring charges for each of the following UNEs?

(1) 2-wire voice grade loop;

(2) 4-wire analog loop;

(3) 2-wire ISDN/IDSL loop;

(4) 2-wire xDSL-capable loop;

(5) 4-wire xDSL-capable loop;

(6) 4-wire 56 kbps loop;

(7) 4-wire 64 kbps loop;

(8) DS-1 loop;

(9) high capacity loops (DS3 and above);

(10) dark fiber loop;

(11) subloop elements (to the extent required by the Commission in Issue 4);

(12) network interface devices;

(13) circuit switching (where required);

(14) packet switching (where required);

(15) shared interoffice transmission;

(16) dedicated interoffice transmission;

(17) dark fiber interoffice facilities;

(18) signaling networks and call-related databases;

(19) OS/DA (where required).

Q. WHAT RATES (RECURRING AND NON-RECURRING) DOES BELLSOUTH PROPOSE FOR EACH UNE LISTED ABOVE?

A. The rates BellSouth proposes are contained in Exhibit AJV-1 attached to my testimony. This exhibit provides an overall summary of the proposed rates and their associated costs. The cost study reference number is provided with the

description of the corresponding rate element. As required by the FCC's pricing rules, these rates equal the forward-looking economic costs of the UNE.

Q. HOW SHOULD THESE UNE PRICES RELATE TO PRICES FOR INTERCONNECTION?

A. Prices for local interconnection facilities should equal the UNE prices for the type of interconnection facility provided. For example, the price for an OC3 interconnection facility should equal the price for the relevant OC3 dedicated transport UNE. Likewise, prices for transport and termination of local traffic should equal the price for the equivalent UNE functions used to transport and terminate the traffic. For example, the prices for tandem switching used to transport and terminate local traffic should equal the UNE price for tandem switching. The Commission should not create an inconsistency between the prices for the same functionality or facility. Regardless of whether the facility or functionality is provisioned as a UNE or interconnection service, prices must be consistent.

Issue 9(b): Subject to the standards of the FCC's Third Report and Order, should the Commission require ILECs to unbundle any other elements or combinations of elements? If so, what are they and how should they be priced?

Q. WHAT IS BELLSOUTH'S POSITION ON THIS ISSUE?

A. As I discussed earlier in response to Issue 4, the UNEs which BellSouth currently makes available to ALECs are those required by the FCC's 319 Order. Absent a showing that access to a UNE is "necessary" and where failure to provide such access "impairs" the ability of an efficient ALEC to provide telecommunications services, BellSouth believes it is not necessary for this Commission to impose additional unbundling obligations beyond those UNEs identified in the FCC's national list. Since the FCC recently completed its exhaustive review of UNEs, BellSouth is not aware of any additional elements that need to be examined.

Issue 10: What is the appropriate rate, if any, for customized routing?

Q. WHAT RATES DOES BELLSOUTH PROPOSE FOR CUSTOMIZED ROUTING, WHICH IS ALSO REFERRED TO AS "SELECTIVE ROUTING"?

A. BellSouth offers ALECs two methods for selective routing: selective routing using line class codes, or selective routing utilizing BellSouth's Advanced Intelligent Network solution. The rates for each of these methods of selective routing are contained in Exhibit AJV-1. These proposed rates are based on BellSouth's filed cost studies which are supported and addressed in the testimony of Ms. Daonne Caldwell.

Issue 11: What is the appropriate rate, if any, for line conditioning, and in what situations should the rate apply?

Q. PLEASE DESCRIBE THE SITUATIONS WHEN CHARGES FOR LINE CONDITIONING, ALSO REFERRED TO AS LOOP MODIFICATION, WOULD APPLY.

A. Unbundled loop modification (line conditioning) charges are applicable when an ALEC requests BellSouth to remove equipment that has been placed on copper loops (i.e., load coils, low-pass filters, range extenders, etc.) and/or by removing bridged tap attached to the copper loop. The FCC permits BellSouth to charge ALECs for loop conditioning. The FCC's UNE Remand Order in CC Docket No. 96-98 states, "We agree that networks built today normally should not require voice-transmission enhancing devices on loops of 18,000 feet or shorter. Nevertheless, the devices are sometimes present on such loops, and the incumbent LEC may incur costs in removing them. Thus, under our rules, the incumbent should be able to charge for conditioning such loops." [See Paragraph 193, Footnote deleted] Obviously, because the FCC allows the recovery of costs for conditioning loops under 18kf, rates for conditioning loops greater than 18kf are also appropriate. An ALEC may use BellSouth's unbundled loop modification offering to remove bridge tap and/or equipment from any copper loop within BellSouth's network for the purposes of providing advanced data services.

Q. WHAT ARE THE APPROPRIATE RATES FOR LOOP MODIFICATION?

A. The rates for unbundled loop modification are contained in Exhibit AJV-1. These proposed rates are supported by the cost studies filed on April 17, 2000 and addressed in the testimony of Ms. Daonne Caldwell.

Issue 12: Without deciding the situations in which such combinations are required, what are the appropriate recurring and non-recurring rates for the following UNE combinations:

(a) "UNE platform" consisting of: loop (all), local (including packet, where required) switching (with signaling), and dedicated and shared transport (through and including local termination);

(b) "extended links", consisting of:

(1) loop, DS0/1 multiplexing, DS1 interoffice transport;

(2) DS1 loop, DS1 interoffice transport;

(3) DS1 loop, DS1/3 multiplexing, DS3 interoffice transport.

Q. WHAT RATES (RECURRING AND NON-RECURRING) DOES BELLSOUTH PROPOSE FOR EACH UNE COMBINATION LISTED ABOVE?

A. The rates BellSouth proposes for the currently combined UNE combinations listed above are contained in Exhibit AJV-1 attached to my testimony. These proposed rates are supported by the cost studies filed on April 17, 2000 and addressed in the testimony of Ms. Daonne Caldwell.

Q. WHAT PRICES HAS BELLSOUTH PROPOSED TO COMBINE UNEs FOR ALECs?

A. BellSouth has only proposed prices for new combinations of UNEs that are necessary to enable BellSouth to receive the exemption from providing local switching as a UNE in accordance with the FCC's Rule 51.319. Specifically, BellSouth proposes rates for providing new Enhanced Extended Link ("EEL") combinations where BellSouth avails itself of the exemption from providing unbundled local switching to customers with four or more lines in density zone 1 in the top 50 metropolitan statistical areas ("MSAs"). The specific MSAs in Florida where BellSouth will offer new EEL combinations are Miami, Orlando, and Fort Lauderdale. Areas served by BellSouth in density zone 1 in the top 50 MSAs are the only locations where BellSouth is required to combine UNEs at cost based prices. As such, the proposed prices for providing new EEL combinations equal economic cost and are reflected in Exhibit AJV- 1.

Issue 13: When should the recurring and non-recurring rates and charges take effect?

Q. WHAT IS BELLSOUTH'S POSITION ON THIS ISSUE?

A. The recurring and non-recurring rates and charges established in this proceeding will take effect after the Commission issues an effective order and when existing interconnection agreements are properly amended to incorporate the ordered rates. The rates BellSouth charges ALECs for UNEs and

interconnection services are governed by an approved interconnection agreement.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

#202932

BELLSOUTH TELECOMMUNICATIONS, INC.

REBUTTAL TESTIMONY OF ALPHONSO J. VARNER

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 990649-TP

JUNE 29, 2000

Q. PLEASE STATE YOUR NAME, YOUR POSITION WITH BELLSOUTH TELECOMMUNICATIONS, INC. ("BELLSOUTH") AND YOUR BUSINESS ADDRESS.

A. My name is Alphonso J. Varner. I am employed by BellSouth as Senior Director for State Regulatory for the nine-state BellSouth region. My business address is 675 West Peachtree Street, Atlanta, Georgia 30375.

Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?

A. Yes. I filed direct testimony in this proceeding on May 1, 2000.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to policy issues addressed in the direct testimony filed on behalf of various intervenors. Specifically, I will respond to Issues 6, 9(b), and 13 as they are addressed in the testimony of AT&T and MCIWorldCom's witness Mr. Jeff King, Florida Cable Television Association's ("FCTA's") witness Mr. William Barta, Bluestar, Covad and Rhythms Link's

witness Ms. Terry Murray, and Supra's witness Mr. David Nilson filed with the Florida Public Service Commission ("Commission") on June 8, 2000.

Issue 6: Under what circumstances, if any, is it appropriate to recover non-recurring costs through recurring rates?

Q. ON PAGE 4, MS. MURRAY CONTENDS THAT NON-RECURRING CHARGES ARE A BARRIER TO ENTRY FOR NEW ENTRANTS. PLEASE RESPOND.

A. Ms. Murray's contention that the higher the nonrecurring charges the more difficult it is for ALECs to offer competitive local exchange services is not necessarily true. Ms. Murray presumes that end users are not charged nonrecurring charges for the retail services they purchase. Also, Ms. Murray disregards the fact that properly structured nonrecurring charges reduce recurring prices charged to the ALEC. Consequently, the ALEC can offer lower prices to its end users than they would otherwise. In fact, the aggregate cost to an ALEC is probably lower with properly structured nonrecurring charges because including nonrecurring costs in recurring rates would require the addition of a cost of money component. If the nonrecurring costs are paid up front, the ALEC avoids this cost of money component.

Q. ALSO ON PAGE 4, MS. MURRAY STATES THAT THE FCC HAS REQUIRED BELL ATLANTIC, AS A CONDITION FOR ITS MERGER WITH GTE, TO IMPLEMENT AN OPTIONAL PAYMENT PLAN IN AN ATTEMPT TO MITIGATE THE EFFECT OF NONRECURRING COSTS ON NEW

ENTRANTS. DOES BELLSOUTH OFFER ALECs AN OPTIONAL PAYMENT PLAN?

A. While BellSouth does not have a standard offering for an optional payment plan, BellSouth is willing to consider any such requests through negotiations with ALECs. To the best of my knowledge, none of the ALECs on whose behalf Ms. Murray is testifying have made such a request. Furthermore, the fact that the FCC may have required Bell Atlantic to implement such a plan as part of the condition for its merger with GTE is of no relevance in this proceeding.

Q. ON PAGE 5, MS. MURRAY STATES THAT A NEW ENTRANT CANNOT OBTAIN A REFUND OR REPAYMENT FOR NONRECURRING CHARGES IF IT LOSES THE RETAIL CUSTOMER OR GOES OUT OF BUSINESS. PLEASE COMMENT.

A. Ms. Murray's comment is true but irrelevant. When BellSouth incurs nonrecurring costs necessary to provide a service or functionality to an ALEC, those costs cannot be "unincurred" and should be paid for by the ALEC that requested the service or functionality. Regardless of whether the ALEC chooses to serve its end user by purchasing unbundled network elements or using its own facilities, non-recurring costs would be incurred by the ILEC to provide service to the ALEC's end user. Since the ILEC does not realize a nonrecurring cost reduction when the ALEC's end user disconnects or the ALEC goes out of business, "refunds" of the type proposed by Ms. Murray would be inappropriate. Ms. Murray wants ALEC's business risk to be transferred to BellSouth, which makes no sense. Why should

BellSouth assume the risk of the ALEC's failure in the marketplace? If BellSouth were burdened with such risk, then it would be appropriate for BellSouth to share in the ALEC's success as well.

Q. ON PAGE 6, MS. MURRAY CONTENDS THAT "THERE ARE NO NONRECURRING COSTS OR CHARGES WHEN AN EXISTING CUSTOMER OF AN INCUMBENT LOCAL EXCHANGE CARRIER CHOOSES TO STAY WITH THAT INCUMBENT" AND THAT NEW ENTRANTS MUST "FOREGO OR MINIMIZE" UP-FRONT CHARGES TO PERSUADE CONSUMERS TO SWITCH CARRIERS. PLEASE RESPOND.

A. Ms. Murray is mistaken on both contentions. First, any BellSouth existing customer would have already paid nonrecurring charges to cover the nonrecurring costs when the service was established with BellSouth. Second, the interLATA and Internet markets demonstrate the fallacy of Ms. Murray's contention that ALECs would have difficulty recovering nonrecurring costs in the recurring rates they charge their customers. Despite the application of nonrecurring charges, the number of competitors in the interLATA and Internet markets has skyrocketed. When Internet providers and long distance carriers started to frank or "waive" nonrecurring charges, most other carriers or providers followed suit, so they were all competing with prices that incorporated nonrecurring costs in recurring rates. Furthermore, any concern regarding recovery of nonrecurring costs in recurring rates to end users due to "frequency of customer churn" is mitigated by the fact that when a customer needs new service or moves they have to incur nonrecurring

charges whether they buy from an ILEC or ALEC. The fact that the customer has already paid nonrecurring charges is, at best, a temporary concern.

Q. ON PAGE 6, MR. BARTA CONTENDS THAT THE COST TO DEVELOP OPERATIONAL SUPPORT SYSTEMS ("OSS") AND THE ELECTRONIC INTERFACES SHOULD BE RECOVERED THROUGH RECURRING RATES IN LIEU OF NONRECURRING CHARGES. DID BELLSOUTH PROPOSE RATES FOR THE RECOVERY OF ITS OSS AND ELECTRONIC INTERFACE DEVELOPMENT COSTS?

A. No. Consistent with the Stipulation of Certain Issues and Schedule of Events, filed December 7, 1999, of which the Florida Cable Telecommunications Association was a party to, the issue of recovery of the development and the ongoing maintenance associated with providing ALEC's with access to BellSouth's OSS and electronic interfaces will be addressed in a separate proceeding. As such, any discussion of cost recovery or pricing for access to OSS should not be addressed in the immediate proceeding.

Issue 9(b): Subject to the standards of the FCC's Third Report and Order, should the Commission require ILECs to unbundle any other elements or combinations of elements? If so, what are they and how should they be priced?

Q. MR. NILSON (PAGE 13) AND MS. MURRAY (PAGE 13) DISCUSS THE TOPIC OF UNBUNDLED ACCESS TO DIGITAL SUBSCRIBER LINE ACCESS MULTIPLEXERS (DSLAMs) AND IMPLY THAT BELLSOUTH SHOULD

PROVIDE SUCH UNBUNDLED ACCESS. HASN'T THE FCC ALREADY ADDRESSED THIS VERY ISSUE?

A Yes. The FCC has made clear the cases where BellSouth must unbundle DSLAMs. As I understand the FCC's requirements, BellSouth must provide unbundled DSLAMs only in specific instances where BellSouth has installed its own DSLAMs but will not or cannot accommodate a request for an ALEC such as Supra Telecom to collocate its own DSLAMs. Basically, in its Rule 51.319(c)(5), the FCC identified four conditions that, only where all four conditions are present, would an ILEC have to unbundle packet switching, which would include DSLAMs. All of these conditions do not exist in BellSouth's network, as BellSouth has taken the necessary measures to ensure that ALECs have access to necessary facilities so that BellSouth is not required to unbundle packet switching.

Q. WHAT DID THE FCC FIND IN ITS DETERMINATION OF WHETHER ACCESS TO UNBUNDLED PACKET SWITCHING MET THE FCC's "IMPAIR" STANDARD?

A. The FCC determined that competing carriers would not be impaired without unbundled access to the incumbent LEC's packet switching functionality. (Para. 306) The FCC recognized that there are numerous carriers providing service with their own packet switches, and that "competitors are actively deploying facilities used to provide advanced services to serve certain segments of the market - namely, medium and large business - and hence they cannot be said to be impaired in their ability to offer service." *Id.*

Q. DID THE FCC EMPOWER STATE COMMISSIONS TO REQUIRE INCUMBENT LECs TO UNBUNDLE SPECIFIC NETWORK ELEMENTS USED TO PROVIDE FRAME RELAY SERVICE?

A. Yes, but only to the extent that a competing carrier can demonstrate to the state commission that it is impaired without access to such unbundled network elements - a showing the FCC found that commenters failed to make. (UNE Remand Order, Para. 312) In its UNE Remand Order, the FCC established the "impair" standards by which it would determine if a network element should be unbundled. The FCC concluded that

> "the failure to provide access to a network element would 'impair' the ability of a requesting carrier to provide the services it seeks to offer if, taking into consideration the availability of alternative elements outside the incumbent's network, including self-provisioning by a requesting carrier or acquiring an alternative from a third-party supplier, lack of access to that element materially diminishes a requesting carrier's ability to provide the services it seeks to offer." (Para. 51)

The FCC went on to say that a materiality component "requires that there be substantive differences between the alternative outside the incumbent LEC's network and the incumbent LEC's network element that, collectively, 'impair' a competitive LEC's ability to provide service within the meaning of section 251(d)(2)." *Id.*

Even assuming a state commission is authorized to alter the conditions established by the FCC for the unbundling of packet switching (which BellSouth does not believe is the case), Supra still would have the burden of proving that it is impaired by not having access to BellSouth's packet switching functionality on an unbundled basis. The very arguments Mr. Nilson makes here are the same that the FCC considered and rejected. Mr. Nilson has offered nothing new and certainly has not provided anything substantive that would meet the FCC's "necessary and impair" standards for requiring BellSouth to provide DSLAMs on an unbundled basis. For the Commission's convenience, I have attached to my testimony as Rebuttal Exhibits AJV-1 and AJV-2 the pertinent excerpts from BellSouth's Comments and Reply Comments filed with the FCC in CC Docket No. 96-98 on this subject.

Q. ON PAGE 14 OF HIS TESTIMONY, MR. NILSON STATES "THE ILEC IS THE ONE CARRIER WHO HAS DEPLOYED DSLAMs UBIQUITOUSLY THROUGHOUT ITS NETWORK IN CENTRAL OFFICES AND REMOTE TERMINALS." IS HE CORRECT?

A. Certainly not. Mr. Nilson should be fully aware that DSLAM technology is relatively new and that BellSouth has not equipped every single one of its hundreds of central offices and thousands of remote terminals in its nine-state region. Such a statement is outlandish. More to the point, BellSouth and ALECs are on equal footing regarding the provisioning of DSLAMs. BellSouth can install DSLAMs for its own use and ALECs (through collocation in BellSouth's central offices or remote terminals) can do likewise.

Q. ON PAGE 15 OF HIS TESTIMONY, MR. NILSON DISCUSSES THE TOPIC OF WAVE DIVISON MULTIPLEXING (WDM) AND ADVOCATES THAT IT BE A NEW UNBUNDLED NETWORK ELEMENT. DO YOU AGREE?

A. No. WDM is simply a new technology that allows greater transmission capacity over fiber optic cable. Similar technology evolutions in the use of fiber optic transmission systems have already occurred as Light Emitting Diode (LED) technology gave way to high-speed laser technology. I fully expect more technological advances that will allow greater and greater transmission speeds to be realized; however, whether the discussion is of fiber optic systems utilizing LEDs, lasers or even WDM, the unbundled network element involved is unbundled transport. Thus, there is simply no need to define yet another form of unbundled transport simply because WDM may be used.

Q. ON PAGE 15 OF HIS TESTIMONY, MR. NILSON SUGGESTS THAT LOOPS WITH CERTAIN CHARACTERISTICS BE CONSIDERED SEPARATE LOOPS. PLEASE COMMENT.

A. To the extent that Mr. Nilson is advocating new loop types for xDSL services, there is no need for him to do so. BellSouth has already developed and is offering a variety of unbundled loop types that BellSouth believes will meet all ALECs' needs. For example, BellSouth offers unbundled ISDN capable loops, which some ALECs use for the service sometimes referred to as IDSL (ISDN Digital Subscriber Line). BellSouth also offers HSDL capable loops (that are provisioned according to Carrier Serving Area (CSA) standards), which some ALECs use to provide HDSL

service. Additionally, BellSouth offers ADSL capable loops (that are provisioned according to Revised Resistance Design standards) and Unbundled Copper Loops (that are provisioned according to Resistance Design standards), which some ALECs use to provide ADSL service. BellSouth recently introduced a new loop type referred to as the Unbundled Copper Loop – Long, which some ALECs use to provide ADSL where the overall loop length is greater than 18,000 feet

Q. ON PAGE 17, FCTA'S WITNESS MR. BARTA STATES THAT THE COMMISSION SHOULD INITIATE PROCEEDINGS IF ACCESS TO ANY OF THE UNBUNDLED NETWORK ELEMENTS THAT HAVE BEEN REMOVED FROM THE FCC'S LIST "PROVES TO BE ONLY AVAILABLE AT NONCOMPETITIVE RATES, OR UNDER UNACCEPTABLE SERVICE QUALITY LEVELS". DOES MR. BARTA'S POSITION COMPORT WITH THE FCC'S "NECESSARY AND IMPAIR" STANDARD FOR UNBUNDLING NETWORK ELEMENTS?

A. No. Mr. Barta is attempting to establish a new standard for defining which elements should be unbundled. However, in the 319 Remand Order, the FCC determined which UNEs are "necessary" and where failure to provide such UNEs "impairs" the ability of an efficient ALEC to provide telecommunications services. The FCC defines the necessary and impair standard of Section 251 as follows:

> "A proprietary network element is considered "necessary" within the meaning of section 251(d)(2)(A) if, taking into consideration the availability of alternative elements outside the incumbent's network, including self-provisioning by a requesting carrier or acquiring an alternative from a third

party supplier, lack of access to that element would as a practical, economic, and operational matter, preclude a requesting carrier from providing the services it seeks to offer."

"The incumbent LECs failure to provide access to a non-proprietary network element "impairs" a requesting carrier within the meaning of section 251(d)(2)(B) if, taking into consideration the availability of alternative elements outside the incumbent's network, including self-provisioning by a requesting carrier or acquiring an alternative from a third-party supplier, the lack of access to an element materially diminishes a requesting carrier's ability to provide the services it seeks to offer."

Furthermore, the FCC concluded that Section 251(d)(3) of the Act grants state commissions the authority to impose additional obligations upon incumbent LECs beyond those imposed by the national list, as long as they meet the requirements of section 251 of the Act and Section 51.317 of the FCC's Rules. As I discussed in my direct testimony, should this Commission wish to consider imposing additional unbundling obligations on BellSouth, the requirements of Rule 51.317 obligate the Commission to apply the "necessary and impair" standard in its analysis and consideration, and not the standard proposed by Mr. Barta.

Q. AT&T/MCI WITNESS, MR. KING, INCLUDES DIRECTORY ASSISTANCE ("DA") DATABASE ACCESS IN HIS LIST OF UNES. IS BELLSOUTH OBLIGATED TO PROVIDE ACCESS TO THIS DATABASE?

A. No. The FCC's 319 Remand Order states "where incumbent LECs provide customized routing, lack of access to the incumbents' OS/DA service on an unbundled basis does not materially diminish a requesting carrier's ability to offer telecommunications service." (¶441, FCC Docket CC 96-98 UNE Remand Order) Since BellSouth deploys customized routing, it is not obligated to provide operator call processing and directory assistance services. The FCC also states in paragraph 442, "incumbent LECs need not provide access to its OS/DA as an unbundled network element." In fact, since the Commission will address the appropriate rates and charges for "OS/DA (where required)" under Issue 9(a) in Phase 2 of this proceeding, any discussion regarding OS/DA should be addressed at that time.

Issue 13: When should the recurring and non-recurring rates and charges take effect?

Q. ON PAGE 18, MR. BARTA STATES THAT ILECs SHOULD BE PROVIDED TIME TO CONFORM THEIR BILLING AND ADMINISTRATIVE SYSTEMS, HOWEVER HE CONTENDS THAT IT IS REASONABLE FOR THE RATES ESTABLISHED IN THIS PROCEEDING TO "BECOME EFFECTIVE 30 TO 90 DAYS AFTER THE COMMISSION ISSUES ITS ORDER". DO YOU AGREE?

A. While I do agree that BellSouth will require some amount of time to conform its billing and administrative systems to implement the rates established in this proceeding, I do not agree that a specific amount of time (e.g. 30 to 90 days) is appropriate to govern when the rates become effective. As I discussed in my direct testimony, the rates and charges established in this proceeding should take effect

when existing interconnection agreements are properly amended to incorporate the ordered rates, whether that is 30 days, 60 days or whenever.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

(#216384)

MS. KEATING: Next is BellSouth Witness Caldwell.

CHAIRMAN DEASON: Witness Caldwell's testimony without objection shall be inserted into the record.

MS. KEATING: And Witness Caldwell has Exhibits DDC-1 through DDC-5.

CHAIRMAN DEASON: Those exhibits shall be identified as Composite Exhibit 39 and without objection admitted into the record.

(Composite Exhibit 39 marked for identification and entered into the record.).

BELLSOUTH TELECOMMUNICATIONS, INC.

DIRECT TESTIMONY OF D. DAONNE CALDWELL

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 990649-TP

MAY 1, 2000

Q. PLEASE STATE YOUR NAME, ADDRESS AND OCCUPATION.

A. My name is D. Daonne Caldwell. My business address is 675 W. Peachtree St., N.E., Atlanta, Georgia. I am a Director in the Finance Department of BellSouth Telecommunications, Inc. (hereinafter referred to as "BellSouth"). My area of responsibility relates to economic costs.

Q. PLEASE PROVIDE A BRIEF DESCRIPTION OF YOUR EDUCATIONAL BACKGROUND AND WORK EXPERIENCE.

A. I attended the University of Mississippi, graduating with a Master of Science Degree in mathematics. I have attended numerous Bell Communications Research, Inc. ("Bellcore") courses and outside seminars relating to service cost studies and economic principles.

My initial employment was with South Central Bell in 1976 in the Tupelo, Mississippi, Engineering Department where I was responsible for Outside Plant Planning. In 1983, I transferred to BellSouth Services, Inc. in Birmingham, Alabama, and was responsible for the Centralized Results System Database. I

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moved to the Pricing and Economics Department in 1984 where I developed methodology for service cost studies until 1986 when I accepted a rotational assignment with Bellcore. While at Bellcore, I was responsible for development and instruction of the Service Cost Studies Curriculum including courses, such as, "Concepts of Service Cost Studies", "Network Service Costs", "Nonrecurring Costs", and "Cost Studies for New Technologies". In 1990, I returned to BellSouth and was appointed to a position in the cost organization, now a part of the Finance Department, with the responsibility of managing the development of cost studies for transport facilities, both loop and interoffice. My current responsibilities encompass testifying in cost-related dockets, cost methodology development, and the coordination of cost study filings.

Q. HAVE YOU HAD ANY PREVIOUS EXPERIENCE IN TESTIFYING?

A. Yes. I have participated in arbitration hearings, generic cost dockets, and Universal Service Fund proceedings, providing evidence on cost-related issues. Thus, I have testified before the state public service commissions in Alabama, Florida, Georgia, Kentucky, Louisiana, Mississippi, and South Carolina, the Tennessee Regulatory Authority, and the Utilities Commission in North Carolina.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to respond to the issues released March 16, 2000 by the Florida Public Service Commission ("Commission"), that concern cost development. Specifically, I discuss the requirements that should be imposed on

recurring and nonrecurring cost preparation for unbundled network elements ("UNEs"), combinations of network elements, and deaveraged offerings. In doing so, I will address the underlying cost methodology, the models, and the major inputs BellSouth utilized in the cost studies filed with this Commission on April 17, 2000.

Q. HOW IS YOUR TESTIMONY STRUCTURED?

A. In the first section of my testimony, I discuss the cost development process in general. This section is organized as follows:

- ► Cost Methodology
- ► Models
  - ▪ Loop Model
  - ▪ Switch-related Cost Models
  - ▪ BellSouth Cost Calculator©
  - ▪ Capital Cost Calculator
  - ▪ Price Calculators
  - ▪ Nonrecurring Cost Model
- ► Inputs
  - ▪ General
  - ▪ Factors and Loadings
  - ▪ Element Specific Inputs

In the second section of my testimony, I respond to the specific cost-related issues

raised by the Commission.

SECTION 1

COST METHODOLOGY

Q. HAS THIS COMMISSION PREVIOUSLY ADDRESSED COST METHODOLOGY?

A. Yes. This Commission previously conducted an exhaustive investigation into cost methodology to be used by Incumbent Local Exchange Companies in Docket No. 900633-TL. Its findings established Total Service Long Run Incremental Cost ("TSLRIC") as the appropriate methodology to be used for cost support for tariff filings. More recently, the Commission addressed the cost methodology, i.e., the underlying economic principles, for unbundled network elements in Docket Nos. 960833-TP, 960846-TP, and 960916-TP. The Commission released Order No. PSC-96-1579-FOF-TP ("Order"), on December 31, 1996, in which it first discussed the Federal Communications Commission's ("FCC's") rules and then outlined its interpretation of those cost methodology directives. In fact, the Commission recognized the similarities between the two methodologies, TSLRIC plus shared and common and Total Element Long Run Incremental Cost ("TELRIC") economic cost. On page 24 of the Order this Commission stated, "...we do not believe there is a substantial difference between the TSLRIC cost of a network element and the TELRIC cost of a network element."

Q. WHAT ARE THE ECONOMIC PRINCIPLES UNDERLYING TSLRIC PLUS SHARED AND COMMON AND TELRIC ECONOMIC COSTS?

A. Both methodologies embrace the following principles:

(1) **Efficient network configuration** – the cost should be based on the use of the most current telecommunications technology presently available and the economically efficient configuration, given the existing wire center locations.

(2) **Long run** – the studies should consider a timeframe long enough to reflect the variability of the cost components.

(3) **Volume sensitive and volume insensitive costs are considered** – these are the costs that will be avoided by discontinuing, or incurred by offering, an entire product or service, holding all other products or services offered by the firm constant. A corollary to this directive is the principle of cost causation, i.e., the costs included in the study are those that are caused because BellSouth offers an unbundled element or a combination of network elements.

(4) **Forward-looking** – both methodologies demand a forward-looking perspective. Thus, embedded costs are excluded from consideration.

(5) **Shared and common costs** – a reasonable allocation of shared and common costs are allowed.

BellSouth agrees that the above-mentioned principles should be incorporated into any study that determines the cost of UNEs and for UNE combinations. (By necessity, TELRIC economic costs that are deaveraged also reflect these principles.)

However, implementation of these principles has often been open to dispute. In the past, the main areas of contention with respect to cost development were: network design, work time estimates and the provisioning process, and economic parameters, e.g., cost of money and depreciation.

The overall debate can be distilled into one overriding issue, "What constitutes 'forward-looking'?" Past experience has proven that opposing parties tend to ignore the FCC's statement that the "benchmark of forward-looking cost and existing network design most closely represents the incremental costs incumbents actually expect to incur in making network elements available to new entrants." (FCC Order paragraph 685) Instead they advocate network architectures, provisioning processes, and expense reductions that are unattainable within the foreseeable future.

BellSouth does not support an embedded perspective with respect to cost development. However, BellSouth recognizes that past results may be judged as an indication of future trends and thus, should provide some input into the cost analysis, at least as a starting point. For example, year-end expense and investment data are utilized as starting points in developing some cost factors.

Q. YOU MENTIONED THAT SHARED AND COMMON COSTS ARE COMPONENTS OF ECONOMIC COSTS. WHAT ARE SHARED AND COMMON COSTS?

A. Shared costs are those costs that are unaffected by a change in demand (volume) of any one service or the deletion or addition of a service. Another way to define shared costs is as the portion of incremental cost joint to two or more services offered by a firm, but not by all services offered by the firm. Common costs are costs that are incurred for the benefit of a firm as a whole, but not for the benefit of any individual product or family of products. Such costs do not change with changes in the firm's product mix or volume of output. The FCC and this Commission both recognize that shared and common costs should be considered when setting rates for UNEs and combinations of UNEs. In fact, the Commission in Order No. PSC-96-1579-FOF-TP states, "In addition, the FCC states that prices should be based on the TSLRIC of the network element, which is called the Total Element Long Run Incremental Cost (TELRIC), and includes a reasonable allocation of forward-looking joint and common costs." (Order at page 24)

Q. HOW DID BELLSOUTH CALCULATE SHARED AND COMMON COSTS?

A. BellSouth used an internally developed shared and common model. BellSouth witness, Mr. Walter Reid, provides testimony detailing the development of the shared and common costs within this model.

Q. WHAT COST METHODOLOGY DID BELLSOUTH UTILIZE IN THIS FILING FOR UNES?

A. Whether termed TELRIC economic costs or TSLRIC plus shared and common

costs, BellSouth utilized a methodology that reflects the costs BellSouth expects to incur in providing unbundled network elements to competitors on a going-forward basis in the state of Florida. These costs are based on an efficient network, designed to incorporate currently available forward-looking technology, but recognize BellSouth's provisioning practices and network guidelines, as well. Additionally, shared and common costs were considered. The shared and common costs are based on a projection of BellSouth's anticipated expenses, partitioned based on the allocation method presented in Mr. Reid's testimony.

Q. WHAT METHODOLOGY DID BELLSOUTH USE TO DEVELOP THE COSTS OF COMBINATIONS?

A. The cost methodology for combinations does not differ from the cost methodology used for unbundled elements since they will both be used to support rates for items offered to competitors. However, some of the inputs into a combination study may differ from individual UNE inputs. For example, for a combined loop and port, integrated digital loop carrier is considered in the mix of technologies providing that existing combination. In the UNE study, integration is not an option since each element is unbundled and provided separately. Thus, integrated digital loop carrier technology is not appropriate for developing the cost of individual UNEs. This distinction results from the cost object being studied rather than the underlying methodology. Additionally, depending on how a "combination" is defined, nonrecurring inputs may differ. For example, a combination of UNEs on a "switch-as-is" basis, i.e., one that currently exists in BellSouth's network, basically involves a billing change and thus has substantially shorter work times than the work times

required either to provide individual UNEs or to combine two UNEs.

Q. WHAT COST METHODOLOGY DID BELLSOUTH USE FOR GEOGRAPHIC DEAVERAGING?

A. The same cost methodology is applicable for geographic deaveraging as was used for UNEs and combinations. Geographic deaveraging is merely a finer breakdown of costs into separate subsets based on geographic differences. Some examples of these geographic differences may include distance from serving wire center and customer dispersion. BellSouth developed loop and switch-related costs on a wire center level as required by this Commission. I will discuss how BellSouth calculated the zone costs BellSouth included as part of its April 17, 2000 filing later in my testimony. However, the reasoning behind the proposed zones is discussed in Mr. Varner's testimony.

MODELS

Q. PLEASE EXPLAIN BELLSOUTH'S COST MODELS.

A. Modeling is an important step in developing both recurring and nonrecurring costs for unbundled network elements and combinations, and BellSouth has utilized several in developing UNE costs. There are different levels of complexity in the models depending on the component of the network being studied.

Following is a discussion of each of the models BellSouth utilizes in determining the cost of UNEs, combinations, and deaveraged costs.

LOOP MODEL

Q. IN ITS PREVIOUS FILINGS, BELLSOUTH UTILIZED A SAMPLE TO DETERMINE THE COST OF A LOOP. DID BELLSOUTH CONTINUE THIS PRACTICE?

A. No. BellSouth, in conjunction with INDETEC International, Inc., CostQuest Associates, and Stopwatch Maps, has developed a new BellSouth model for loop investment calculations that replaces the old loop sample approach. This new model is called the BellSouth Telecommunications Loop Model© ("BSTLM"). The new model is designed to support the cost development for both unbundled loop elements and service-specific loops. Furthermore, the BSTLM is the only model currently available that distinguishes between the different types of loops, 2-wire, 4-wire, Integrated Services Digital Network ("ISDN"), Asymmetrical Digital Subscriber Line ("ADSL")-compatible, High Bit Rate Digital Subscriber Line ("HDSL")-compatible, etc. Other proxy models are only capable of producing costs for a 2-wire local loop. Even though the model has the capability to develop costs for high capacity loops, BellSouth has currently confined the use of the BSTLM to loops with transmission rates up to DS1. BellSouth felt the limited customer demand for high capacity loops and high capacity local channels would create unrealistic results. Thus, BellSouth developed the costs for high capacity (DS3 and higher) facilities on spreadsheets outside the BSTLM.

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BellSouth's introduction of a new model should not cast doubt on the accuracy of the previous sample methodology. In fact, this Commission stated, "BellSouth's loop sample construction is appropriate." (Order at Page 75) However, the sample approach does have inherent limitations. First, the original sample was statistically valid only for the services tested, i.e., only for single line residential and single line business loops and only on a statewide average basis. Any attempt to stratify the sample into geographic areas for geographic deaveraging could not be statistically supported. Additionally, sampling is extremely labor intensive, requiring many hours to obtain, validate, input and process the data.

The BSTLM has overcome these limitations and has the ability to geographically deaverage costs for UNEs. The new model incorporates geocoded BellSouth customer serving addresses and the types and quantities of services at each location. When combined with BellSouth-specific input values, the model produces loop investments that accurately reflect the forward-looking, most efficient costs of providing service in BellSouth's territory in Florida at a more detailed level than a statewide average.

Q. PLEASE PROVIDE AN OVERVIEW OF THE BSTLM.

A. BellSouth witness, Mr. Jim Stegeman, will explain in detail the methodology underlying the model's calculations. However, I wish to discuss the fundamental process the BSTLM utilizes in developing material prices associated with the various loop offerings. The foundation of the model is customer service records, addresses, as well as services purchased. The BSTLM determines where customers

are located and "lays" cable along the roads of the wire center. A cable path can literally be traced from each customer's premises to the serving central office; a path that follows actual roads in the wire center. The model then determines serving areas for a wire center based on a Minimum Spanning Road Tree ("MSRT") algorithm. The MSRT is the shortest path that connects customer locations assuming that cables follow roads. Appropriate components, such as, digital loop carrier ("DLC") and Feeder Distribution Interfaces ("FDIs") are then located within each serving area.

Once the layout of the network is determined, the BSTLM's configuration process connects the network components. This procedure entails the determination of cable sizes, cable types (copper/fiber, aerial/buried/underground), and selection of DLC type. Once the network is configured, the BSTLM calculates the material price of each network component, not only by component type, but also by component location. Thus, the granularity required to deaverage costs is available through the model.

In order to run the BSTLM, one must establish the defining attributes of the loops and local channels under study. Exhibit DDC-1 displays the matrix used by BellSouth to accomplish this task. If we take the 2-wire analog loop (SL1) as an example, Column A contains the element number used to reference the element throughout the study, in this case A.1.1. Column B provides a description of the element, 2Wire Analog Voice Grade Loop – SL1. The next column defines the scenario run to support the loop. Three different scenarios were established by BellSouth; BST2000, Combo, and Copper. For the SL1 loop, BST2000 was used.

This scenario assumed all switched services were converted to non-switched unbundled network elements. Combo was used for loops offered in combination with other unbundled network elements (P.1.1 and P.4.1). This scenario is identical to BST2000 except that switched services remain switched. The Copper scenario was used to develop costs for those loops served on copper only. In this run, the copper to fiber crossover point was changed from the standard 12 kilofeet (kft) to 1,000,000 feet. This extreme input ensures that all loops are served by copper.

Incorporated into the customer location data utilized by the model is the type of service currently delivered by the loop. (Page 3 of Exhibit DDC-1 displays the services used in the model.) This information is used to determine which loops should be considered in the universe of loops used in the cost calculation of that loop. This is necessary since the type of loop makes certain services incompatible. For example, a digital loop, e.g., an ISDN service loop, would not be considered in the cost calculation of an analog loop, e.g., a 2-wire SL1 loop. Column D cross-references the service types applicable to each loop. For the calculation of the SL1 loop, the services considered were; Residence, Business, PBX, Centrex, Smartline, Public, 2 Wire Private Line, and 2 Wire Special Access loops provisioned to an end user's premises.

Columns E and F further define the loop. Column E should always be set to distribution and feeder (Both). If the user wants to include only certain sections of the loops, the user may do so by selecting certain Cost elements of the loop referenced in Column I. Column F merely states whether the element includes loop (end user) or local channel (carrier Point of Presence ("POP")) customer locations.

Column G outlines which medium is appropriate for the type of loop, i.e., copper, fiber, or a combination of copper and fiber (All). For an SL1 loop, both fiber and copper are appropriate. Any length limitation is contained in Column H. For an SL1 loop, there is no length limitation, thus it is set to All. The Cost Elements, i.e., the network components, considered for each loop type is shown in Column I. For example, a 2-Wire Analog Loop (SL1) would contain "All" of the network elements from the central office terminal to the Network Interface Device ("NID"). On the other hand, the Sub-loop Feeder associated with that type of loop would only reflect the network elements from the Feeder Distribution Interface ("FDI") to the Central Office Terminal ("COT").

Columns J-M detail which type of main Distributing Frame ("MDF") is applicable. For an SL1 loop, the MDF-Melded selection is appropriate. This reflects an MDF meld of copper and loop fiber non-switched loop terminations. If the loop is designed, a test point is required. Columns N-P shows the type of test point included in the cost calculation. Since an SL1 loop is not designed, no test point is chosen. Columns Q-W identify additional "Adders" applicable to certain loops/local channels. No additional adders, beyond the MDF, are required for an SL1 loop.

I will discuss the major input values entered into the BSTLM later in my testimony (in particular in response to Issue # 7), but let me mention here that it is critical that the inputs used in any model reflect the costs BellSouth will incur on a going-forward basis. Thus, the BSTLM inputs are BellSouth-specific and reflect

BellSouth's operations in the state of Florida. Exhibit DDC-2 contains the inputs BellSouth utilized in running the BSTLM.

BellSouth witness, Mr. Jim Stegeman, explains why the BSTLM is superior to the existing proxy models, provides an overview of the model, discusses the model's method of locating customers, and expands on how the inputs are utilized by the model.

SWITCH-RELATED MODELS

Q. BELLSOUTH UTILIZED TELECORDIA'S (FORMERLY KNOWN AS BELLCORE) SWITCHING COST INFORMATION SYSTEM ("SCIS") MODEL IN PAST UNE FILINGS. DID BELLSOUTH CONTINUE TO USE SCIS IN THIS FILING?

A. Yes. BellSouth used the model office module out of the SCIS program, ("SCIS/MO"), in order to determine the fundamental investments. The switch is a multi-faceted entity that performs a number of functions, from establishing a call to providing vertical features, such as, three-way calling. To accurately identify the fundamental unit switch investments necessary for these individual functions, a sophisticated model, like SCIS/MO, is required. BellSouth witness, Mr. Joe Page, describes the SCIS/MO inputs and outputs and its underlying methodology. Also, Appendix I of the cost study filed on April 17, 2000 provides an overview of the SCIS/MO model.

Q. WHAT *MODELS DID BELLSOUTH USE TO DETERMINE SWITCH-*

RELATED COSTS?

A. In past UNE filings in Florida, BellSouth utilized the Telcordia Network Cost Analysis Tool ("NCAT") to develop usage costs and Switching Cost Information System/Intelligent Network ("SCIS/IN") to determine some port and all feature costs. BellSouth no longer supports NCAT. SCIS/IN is another module of Telecordia's SCIS program. Both models were plagued by the proprietary label, making portions of the models inaccessible. To overcome the problem of proprietary models, in this proceeding BellSouth introduces its Simplified Switching Tool ("SST")© Model in this proceeding. The SST model incorporates cost development for all switch-related elements; ports, usage, and vertical features. BellSouth witness, Mr. Joe Page, discusses the scope of the SST model, required inputs, fundamental algorithms, and underlying assumptions. Mr. Page further explains why BellSouth moved to a new model for switch-related cost development.

BELLSOUTH COST CALCULATOR©

Q. IN DOCKET NOS. 960757-TP, 960833-TP AND 960846-TP, BELLSOUTH INTRODUCED THE TELRIC CALCULATOR©. WILL THIS MODEL CONTINUE TO BE USED?

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A. The functions of the TELRIC Calculator have been incorporated into the BellSouth Cost Calculator. It was decided to enhance and rename the model to eliminate any preconceived notion that the model could only produce TELRIC level costs. The BellSouth Cost Calculator converts input data (material prices/investments by field reporting code ("FRC"), recurring additives, nonrecurring additives, and work times by job function code ("JFC")) into cost. The type of cost (i.e., Long Run Incremental Cost ("LRIC"), TSLRIC, or TELRIC) developed is dependent upon the inputs and the selections made by the user. (LRIC cost methodology considers only the volume sensitive direct costs.)

This Commission accepted the TELRIC Calculator as a viable model in its Order No.PSC-96-1579-FOF-TP. The BellSouth Cost Calculator, the modified version of the TELRIC Calculator, adheres to the same underlying methodology as the model previously reviewed by this Commission. However, the BellSouth Cost Calculator has been revised to enhance the user interface and to allow further user flexibility.

Exhibit DDC-3 pictorially displays the interrelationships between the BellSouth Cost Calculator and the other models and price calculators BellSouth used to determine costs. The BellSouth Cost Calculator is the mechanism that performs the mathematical exercise that appropriately applies the correct inflation factors, support loadings, annual cost factors, labor rates, tax factors, and shared and common factors to the inputs. Additionally, to ensure consistency between studies, the BellSouth Cost Calculator serves as the warehouse for annual cost factors, labor rates, loading factors, and inflation factors.

CAPITAL COST CALCULATOR©

Q. HOW DID BELLSOUTH DETERMINE THE CAPITAL COST FACTORS THAT ARE UTILIZED IN THE BELLSOUTH COST CALCULATOR?

A. BellSouth used the Capital Cost Calculator, an internal model designed by BellSouth. BellSouth utilized the Benchmark Cost Proxy Model's ("BCPM's") capital cost module as the foundation for its development of the Capital Cost Calculator. The model produces depreciation, cost of money, and income tax factors that are applied to investments to calculate capital costs.

The user has the ability to modify a set of variables: debt ratio, cost of money, debt interest rate, net salvage ratio and economic life of assets. BellSouth is filing the testimony of Mr. David Cunningham who discusses the appropriate depreciation inputs. Additionally, BellSouth witness, Dr. Randall Billingsley, discusses the appropriate inputs for the cost of money calculation.

Q. IS THE CAPITAL COST CALCULATOR THE SAME VERSION AS WAS FILED IN DOCKET NOS. 960757-TP, 960833-TP, AND 960846-TP?

A. No. Several enhancements have been incorporated into this version of the Capital Cost Calculator. These revisions include the incorporation of survivor curves into

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the development of the depreciation factors and adjustments for differences in book and tax depreciation. In calculating annual depreciation amounts, the Capital Cost Calculator methodology now uses the standard Midyear Equal Life Group ("ELG") approach, which employs a midyear convention. Previously, a straight-line method was used to calculate depreciation.

Additional FRCs have also been added. In particular, FRCs for capitalized software (intangible assets) are included due to changes in the accounting rules.

PRICE CALCULATORS

Q. EXHIBIT DDC-3 ALSO SHOWS SEVERAL "PRICE CALCULATORS". WERE THESE THE SAME PRICE CALCULATORS PREVIOUSLY PRESENTED TO THIS COMMISSION?

A. Not entirely. The four price calculators that BellSouth used in the past are the Loop Multiplexer, Digital Loop Carrier, SONET, and DS1 price calculators. These price calculators develop the material price of specialized components used in the provisioning of various network capabilities. These calculators take vendor prices for various pieces of equipment and express the prices on a per circuit level. In essence, the process involves (1) determining the appropriate types and quantities of equipment required, (2) utilizing vendor-furnished price lists, (3) applying a discount rate (if applicable), and (4) dividing by the capacity of the equipment. The price calculators reflect the latest prices, discount rates, and technology applicable to BellSouth. A vendor-provided "configuration" file that details the manner in

which the equipment is assembled may aid the first step. With the completion of BellSouth's New Loop Model, the Multiplexer and Digital Loop Carrier calculators are incorporated into that model, i.e., they will not be separate entities. Yet, the same type of calculation takes place within the BSTLM's equations.

NONRECURRING COSTS

Q. YOU MENTIONED THAT THE DEVELOPMENT OF NONRECURRING COSTS INVOLVES MODELING. DOES BELLSOUTH HAVE A NONRECURRING COST MODEL?

A. Not in the formal sense. Each analyst is responsible for obtaining estimates of the activities required to provision the element under study. BellSouth personnel familiar with the provisioning process identify the work groups involved and the amount of time it takes to complete the necessary tasks. Consideration is given to anticipated productivity improvements and potential technological advances that may impact the amount of time required. Thus, the projections are forward-looking, yet attainable. These estimates are entered into the BellSouth Cost Calculator on the Nonrecurring Input sheet by element.

INPUTS

GENERAL INPUTS

Q. PLEASE DISCUSS INPUTS IN GENERAL.

A. There are several overriding considerations that must be taken into account when developing inputs. First, the inputs should be forward-looking, realistic, and

achievable. Second, since the objective is to determine the costs BellSouth will incur on a going-forward basis, it is imperative that BellSouth-specific inputs be utilized in the calculations. The use of BellSouth-specific inputs does not violate any of the cost characteristics I listed previously. BellSouth has been a large, efficient provider of telecommunications services in Florida for many years. Thus, economies of scale, negotiated volume discounts, and experience obtained from designing and provisioning an advanced telecommunications network are reflected in values based on BellSouth results.

Q. PLEASE COMMENT ON THE INPUTS COMMON TO ANY UNE COST STUDY.

A. Exhibit DDC-3 outlines the general types of inputs BellSouth utilized in the studies for UNEs and combinations presented in this filing. I will describe each class of input and the process BellSouth used to determine the appropriate value.

INFLATION ADJUSTMENT FACTOR

Q. PLEASE DESCRIBE THE INFLATION ADJUSTMENT FACTOR AND DESCRIBE HOW IT IS DEVELOPED.

A. Over the life of an investment, inflation causes fluctuations in the forward-looking investment amount. Thus, the investment must be averaged over the study period. Investment inflation factors, by FRC, are used to trend plant investment in base year dollars to a levelized amount that is valid for a three year planning period, i.e., the study period (in this case 2000-2002). The investment inflation factors are the

cumulative average of three years' projected inflation rates based on BellSouth telephone plant indices ("TPIs").

The TPIs are price indices that measure the relative changes in prices BellSouth pays for the construction of telephone plant between specific periods of time. The development of TPIs uses econometric techniques to establish mathematical relationships between the historical movement in each of the labor and material components that make up the TPIs and the historical movement in explanatory variables. Explanatory variables are usually aggregate measures of the U. S. economy, e.g., price deflators from the national income and product accounts, union wage rates, copper prices, and other macroeconomic variables. Joel Popkin and Company, a BellSouth consultant, assists BellSouth with the calculation of TPIs.

LOADINGS

Q. WHAT IS MEANT BY THE TERM "LOADINGS"?

A. These factors are designed to augment calculated material prices to account for additional costs that are difficult to ascertain on an individual, element-specific basis. Thus, BellSouth develops mathematical relationships between the material prices and the additional labor expense, miscellaneous material, and support structures to capture the total cost BellSouth will incur on a going-forward basis.

Q. PLEASE DESCRIBE THE DIFFERENT TYPES OF LOADING FACTORS AND THEIR DEVELOPMENT.

A. One type of loadings are In-Plant loadings ("In-Plants"). In-Plants add engineering and installation labor and miscellaneous equipment to the material price, i.e., In-Plants convert a material price to an installed investment. The installed investment is the dollar amount recorded in capital accounts.

In-Plants are account specific and are developed on the state level. There are four types of In-Plant loadings: (1) Material Loading, (2) Telco Loading, (3) Plug-in Loading, and (4) Hardwire Loading. The Material Loading is applied to a material price, the Telco Loading to the vendor-installed investment, the Plug-in Loading to the deferrable plug-in and common plug-in material prices, and the Hardwire Loading to the hardwire portion of an equipment material price.

In order to reflect the costs BellSouth will incur, the In-Plant factors are based on information that is specific to BellSouth. BellSouth used year-end reports developed from extracts of BellSouth's financial systems to develop these factors.

Q. WHAT OTHER TYPE OF LOADINGS WERE INCLUDED IN BELLSOUTH'S COST STUDIES?

A. Supporting Equipment and Power ("SE&P") Loadings were used to calculate the incremental investment required to support an additional dollar of central office and circuit investment. The SE&P Loadings were developed for the digital switch account (FRC 377C), digital subscriber pair gain account (FRC 257C), and other digital circuit equipment account (FRC 357C). Examples of the support and power

equipment included in the 377C factor include power equipment, distribution frames, ladders, tools, and test sets.

The source of the data used to develop the SE&P Loading factors is the Central Office Monthly Allocation Process ("COMAP"), a year-end report extract that identifies total investment and supporting investments for FRCs 377C, 257C, and 357C. As with the In-Plant Loading factors, this is BellSouth-specific data.

In addition to the SE&P Loading factors, central office and circuit investments require loadings for land and buildings. Ratios are developed by comparing central office land and building investments to central office and circuit investments. Base year investment amounts are developed from extracts of BellSouth's financial systems and projected plant additions are furnished by Network.

Q. ARE THERE LOADING FACTORS UNIQUE TO CABLE ACCOUNTS?

A. Yes. Poles and conduit are related only to cable placements. As in the past, BellSouth developed translators to determine the amount of investment in poles and conduit associated with aerial and underground cable investment. The Pole Loading factor was developed by comparing the investment in poles to the investment in aerial cable. Similarly, the Conduit Loading factor was determined based on the relationship between investment in conduit and investment in underground cable.

Base year investment amounts are developed from extracts of BellSouth's financial

systems and projected plant additions are furnished by Network.

Q. IS THERE A LOADING FACTOR UNIQUE TO THE DIGITAL SWITCHING (377C) ACCOUNT?

A. Yes. BellSouth developed a loading factor that accounts for the Right-to-Use ("RTU") investment related to central office switching equipment. As I mentioned previously, an accounting change reclassified RTU fees from expense to capital. Thus, it became necessary to develop a method of identifying this investment. The switch vendors' practice of packaging RTU fees together, the preponderance of buy-outs in effect, and the discounting schemes offered to BellSouth made the direct allocation of switching RTU investment impossible. Alternatively, BellSouth calculated a ratio that reflects the relationship between RTU capitalized investment to digital switch investment over the study period. Budget forecasts from Network were used in this calculation.

ANNUAL COST FACTORS

Q. WHAT ARE ANNUAL COST FACTORS AND HOW DID BELLSOUTH DEVELOP THEM?

A. Annual cost factors are translators used to determine the annual recurring cost associated with acquiring and using equipment. When an investment is multiplied by an annual cost factor, the product reflects the annual recurring cost incurred by the company. There are basically two types of cost associated with an investment, capital-related costs and operating-related costs.

An investment includes the initial purchase price of the item of plant and all engineering and installation costs required to make that item of plant ready to provide service. Capital costs associated with the investment consist of three major categories: depreciation, cost of money, and income tax. As I mentioned previously, BellSouth uses an internally developed model to calculate the capital-related annual cost factors based on user changeable inputs.

Plant must also be maintained to provide continuing operations. Ordinary repairs and maintenance, as well as rearrangements and changes, are necessary for all categories of plant (except land) in order to maintain quality service.

Maintenance-type expenses are reflected in the Plant Specific Expense factor. The following types of operations are included:

(1) Inspecting and reporting on the condition of plant investment to determine the need for repairs, replacements, rearrangements, and changes

(2) Performing routine work to prevent trouble

(3) Replacing items of plant other than retirement units

(4) Repairing materials for reuse

(5) Restoring the condition of plant damaged by storms, floods, fire, and other casualties

(6) Inspecting after repairs have been made

(7) Salaries, wages, and expenses associated with plant craft and work reporting engineers, as well as their immediate supervision and office support.

The Plant Specific Expense factor is developed, by FRC, based on three years of projected expense and investment data. Base year expenses are pulled from the Cost Separations System ("CSS"). Projected view data is obtained from BellSouth's Finance Regulatory Group for the study period. Base year investments are determined from extracts from BellSouth's financial systems. Investment projections are obtained from BellSouth Network for the study period. A relationship between the expenses and the investments is established by dividing the cumulative expenses by the cumulative investments for the study period. Adjustments are made for subsequent right-to-use fees, service order expense and rents. Since Plant Specific Expense factors are based on actual and projected BellSouth data, they reflect expenses BellSouth will incur in providing unbundled elements to competitors on a going-forward basis. Additionally, they reflect BellSouth's network practices, quality of service commitments, budget constraints, and process efficiencies.

Finally, BellSouth pays taxes. BellSouth's Tax Department provides the appropriate tax information, by jurisdiction, to be used in the development of the tax-related factors.

UNBUNDLED ELEMENT SPECIFIC INPUTS

LOOP

Q. THE LOOP ELEMENT IS A MAJOR COMPONENT OF THE NETWORK. WHAT INPUTS ARE THE MAIN COST DRIVERS OF LOOP COSTS AND HOW DID BELLSOUTH DETERMINE THESE INPUTS?

A. As I mentioned previously, Exhibit DDC-2 outlines the inputs BellSouth utilized in the running of the BSTLM. One group of inputs that significantly impacts the loop cost results is the investment (material plus engineering and installation) for feeder, distribution, and digital loop carrier. The per unit material prices (for example, material price per sheath foot of cable) are displayed in Exhibit DDC-2. As explained earlier, investment includes the material price as well as the cost to engineer and install (E&I) the item of plant. BellSouth In-Plant factors are used to calculate the engineering costs along with BellSouth-specific placing costs. The material prices are obtained from procurement records that reflect actual BellSouth purchase prices and contractual agreements. Inherent in the material prices are discounts BellSouth enjoys due to its negotiated contracts. In its Order No.PSC-96-1579-FOF-TP, this Commission ruled, "it is appropriate to accept the cable costs proposed by BellSouth." (Order at Page 88)

The loop model design determines the amount of each facility required, i.e., the BSTLM determines the length of the loops based on customer location and network design. Obviously, loop length is a major cost driver. The MSRT routines built into the model ensure the most efficient routes are considered in determining the loop lengths.

Utilization or fill factors also play an important role in the calculation of loop costs. The FCC's TELRIC methodology allows for a reasonable projection of actual utilization to be incorporated into the equation. (¶682) Similar to other models, such as, the HAI model, the FCC Synthesis Model, and the Benchmark Cost Proxy

Model ("BCPM"), utilization is not entered as a percentage in the BSTLM. Rather, the distribution cables are sized based on the appropriate standard size cable and the number of pairs provisioned to each living unit. Still the effective distribution utilization can be calculated from the BSTLM. The average distribution cable effective fill in BellSouth's study for Florida is 47%. For feeder cable, the model uses the cable sizing factor and standard size cables to determine the required cables to be placed. The average effective fill of the copper feeder cables in this filing is 74%. These results are reflective of BellSouth's anticipated future fill in the distribution and feeder routes.

The amount of structure sharing is also a major cost driver. The structure sharing percentages should be BellSouth-specific and representative of BellSouth's achievable sharing arrangements in Florida. Structure sharing is reflected in the loading factors for poles and conduit and in the in-plant factor associated with buried cable.

Additional inputs related to loops will be discussed further in my response to Issue #7.

SWITCHING

Q. WHAT INPUTS ARE CRITICAL TO THE DEVELOPMENT OF SWITCHING-RELATED COSTS?

A. The first step in developing switching costs is the population of the SCIS/MO database. Information is entered for each digital office in BellSouth's territory. For

existing analog offices, digital technology, based on Network's replacement forecasts, has been assumed. (By year-end 1999, less than 15% of BellSouth's lines in Florida were served by analog offices.)

The SCIS/MO data reflects the investment drivers, i.e., what will cause exhaust of the switch. The investment drivers are inputs such as O+T (originating plus terminating) usage, CCS, quantity of analog lines, quantity of digital lines, processor utilization, etc. Another important input in the model is the discount rate. BellSouth utilized a discount that is indicative of the way switching equipment will be purchased in the future. BellSouth buys a limited number of new central office switches, however, BellSouth grows capacity in its existing central offices on a regular basis. Thus, the discount rate should reflect this combination of new/growth purchasing activity.

In determining the investment related to vertical features busy hour usage is an important component. Switches are engineered to handle the busy hour load. Thus, in order to develop flat-rated feature costs, the usage in the busy hour is the only relevant factor. Inputs need to reflect the anticipated demand that is going to be placed on the switch due to the request for feature-enhanced call processing. Consideration must be given to the number of feature-related calls, holding times, and activations/deactivations that occur.

Usage costs are driven by such items as distribution of calls (intra-office/interoffice split), percent local tandem occurrence, busy hour-full day ratio, average number of facility terminations per call, minutes per call, airline miles per call. The outputs

from SCIS/MO also are important contributors to the development of the usage costs.

As with the inputs to the loop model, only BellSouth-specific data will appropriately reflect the costs BellSouth will incur in the provisioning of switch-related UNEs to competitors in Florida. Mr. Page, in his testimony, expands on the inputs required by the SST model in order to determine switch-related costs.

NONRECURRING COST INPUTS

Q. WHAT INPUTS ARE IMPORTANT TO THE DEVELOPMENT OF NONRECURRING COSTS?

A. I have previously discussed the manner in which time estimates are obtained. These inputs drive the nonrecurring costs. However, in addition to the work times, the labor rates are critical in determining the costs to provision unbundled elements. This Commission accepted BellSouth's methodology for developing the direct labor rates in the previously filed UNE studies. It did, however, eliminate the shared component from the labor rate. (Order No.PSC-96-1579-FOF-TP at Page 63) Additionally, this Commission established a rate structure such that disconnect costs are assessed at the time of disconnect. (Order No.PSC-96-1579-FOF-TP at Page 69) BellSouth followed the same process in developing labor rates in this filing and presented the disconnect costs as separate elements.

SECTION 2 - RESPONSES TO ISSUES

Issue 2(b): "For which of the following UNEs should the Commission set deaveraged rates?
(1) loops (all);
(2) local switching;
(3) interoffice transport (dedicated and shared);
(4) other (including combinations)."

Q. WHICH OF THE UNES OUTLINED IN THIS ISSUE SHOULD BE DEAVERAGED?

A. It is BellSouth's contention that only loops and local channels possess attributes that reflect geographic cost differences and thus, only loops and local channels below DS3 speeds should be deaveraged. Costs for loops and local channels above DS1 are developed on a per mile basis and, therefore, do not require further deaveraging. Other UNEs either do not display the same level of cost variation by geographic location or have price structures that already account for geographic cost differences. Additionally, sub-loops and combinations that have a loop as a component should also be deaveraged since they also reflect cost variations by geographic area.

Switching does not vary significantly by geographic location. None of the factors that make the loop cost vary are present with respect to switching cost calculations. The physical characteristics of the loop and the placing costs associated with that loop vary by geographic location due to cable type (aerial, buried or underground) and distance (length). However, these factors do not impact switching costs to any

great degree. Another factor that influences loop costs, customer density, also has little impact on switching costs since the modularity of digital switching equipment allows BellSouth to grow switches as demand dictates. Also, remote switch entities can be deployed to serve pockets of customers.

Additionally, switching cannot be viewed in the same manner as local loops because logically one cannot isolate one switch from the network. The switch is a part of a total integrated network designed to handle a call from the originating switch entity to the terminating switch entity. To segment individual switches based on individual cost differences ignores the interdependencies between switch entities. This is clearly a problem for remote switches that are dependent on a host switch for interoffice call processing. The insignificant variation in switching costs between wire centers does not warrant the deaveraging of switch-based elements.

The cost of other unbundled network elements may vary by geographic location, but these cost differences are reflected in the rate structure, thus, eliminating the need for deaveraging. An example is interoffice transport. The rate structure for interoffice transport is on a per mile basis. This rate structure already accounts for geographic differences by eliminating length from the equation. Thus, there is no reason to include interoffice transport in the deaveraging scheme. Of course, some of the physical attributes of the interoffice route will impact the costs just as they do in the loop, e.g., the type of placement. However, because the cost is expressed on a per unit (mile) basis, these differences are negligible.

Q. HOW DID BELLSOUTH AGGREGATE THE WIRE CENTER LEVEL

COSTS DEVELOPED BY THE BSTLM INTO ZONES?

A. The first step is to partition the wire centers in Florida into rate groups based upon the General Subscriber Tariff. Next, the rate groups were classified into one of three zone designations. The final step in calculating the average monthly cost for a specific loop or local channel in each zone is to weight the wire-center level costs produced by the BSTLM by wire center line counts for that specific loop or channel. Mr. Varner supports the methodology used to develop the definition of the three zones in his testimony

Exhibit DDC-4 displays the recurring costs by the three zones and the statewide average. (If an element only had nonrecurring costs, it is not shown since nonrecurring costs are not subject to deaveraging. Additionally, if a particular zone does not have a cost, no loops or channels of that type were found in that zone.)

Mr. Varner includes the rates BellSouth is proposing for each zone. BellSouth's cost study displays costs for extended loops not currently combined in BellSouth's network , i.e., "new" combinations, in Zones 2 and 3. However, as explained by Mr. Varner, BellSouth is only obligated to offer this combination in Zone 1. This is also reflected in Mr. Varner's rate sheet.

Issue 3(b): "Should a cost study for xDSL-capable loops make distinctions based on loop length and/or the particular DSL technology to be deployed?"

Q. WHAT COST SUPPORT HAS BELLSOUTH PREPARED IN RESPONSE

TO THIS ISSUE?

A. BellSouth previously submitted costs for ADSL and HDSL compatible loops in Docket Nos. 960833-TP, 960846-TP, and 960916-TP. This Commission established rates based upon BellSouth's proposal, essentially validating BellSouth's definition of these xDSL types of loops. These loops meet the transmission requirements set for ADSL and HDSL service.

Additionally, for this proceeding, BellSouth has developed recurring and nonrecurring costs for 2-wire unbundled copper loops ("UCLs") and 4-wire unbundled copper loops. The costs are segmented between loops less than 18,000 feet ("UCL-Short") and loops greater than 18,000 feet ("UCL-Long"). The UCLs are commonly referred to as "dry copper" loops because they have no intervening equipment such as, load coils, bridged tap, repeaters, etc., between the end user premises and the serving wire center. The UCL-Short will be designed to Resistance Design on a non-loaded metallic facility up to 18,000 feet in length. The UCL-Long will be any copper loop longer than 18,000 feet in length. BellSouth does not guarantee the transmission quality beyond the resistance design standards. BellSouth used the BSTLM to calculate the material costs associated with the xDSL loops.

Issue 4(b): "How should access to such subloop elements be provided, and how should prices be set?"

Q. WHAT COST SUPPORT HAS BELLSOUTH PREPARED IN RESPONSE

TO THIS ISSUE?

A. BellSouth has developed costs for Unbundled Sub-Loops that are 2-wire or 4-wire components of a loop that can be technically unbundled. Sub-Loops consist of Sub-Loop Feeder ("USL-F"), Sub-Loop Distribution ("USL-D"), Intra-building Network Cable ("INC"), and Network Terminating Wire ("NTW"). USL-F is also provided for the DS1 digital loop.

Sub-loop feeder is the physical transmission facility (or channel or group of channels on such facility) which extends from the main distributing frame connection in the end office to the cross-connect box. If the loop is served by digital loop carrier, a central office digital loop carrier terminal is required to convert the digital signal to voice grade analog. A test point is provisioned with the sub-loop feeder for remote test access.

Sub-loop distribution is the physical transmission facility from a BellSouth cross-connect device to the customer's premises (i.e., the Network Interface Device ("NID")). This facility will allow an end user to send and receive telecommunications traffic when it is properly connected to other required network elements, such as, loop feeder facility. This facility includes a NID (where applicable) at the customer's location in the loop.

BellSouth will also provide sub-loop interconnection to the Intrabuilding Network Cable ("INC") (riser cable). INC is the distribution facility inside a subscriber's building or between buildings on one customer's premises (continuous property

not separated by a public street or road). USL-INC (riser cable) will include the facility from the cross-connect device in the building equipment room up to and including the end-user's point of demarcation.

Network Terminating Wire ("NTW") is unshielded twisted copper wiring that is used to extend circuits from an INC terminal or from a building entrance terminal to an individual customer's point of demarcation. It is the last segment of the field-side loop distribution facilities. In multi-subscriber configurations, NTW represents the point at which the network branches out to serve individual subscribers.

NTW will be provided in Multi-Dwelling Units ("MDUs") and/or Multi-Tenants Units ("MTUs") where BellSouth provides wiring all the way to the end-users premises. BellSouth will not provide this element in those locations where the property owner provides the wiring to the end user's premises or where the property owner will not allow BellSouth to place its facilities to the end user.

Another group of elements that can be classified as "sub-loop" is unbundled sub-loop concentration ("USLC"). These elements allow an ALEC to concentrate loop distribution elements, provided by the ALEC, on to multiple DS1s. This arrangement allows the ALEC to connect the loop distribution elements (at a concentrated level) to BellSouth's feeder facilities. BellSouth will then transport the DS1s carrying the distribution circuits back to the serving wire center for termination on a BellSouth DSX1 block and ultimately to the ALEC's collocation space.

Mr. Varner addresses the rates BellSouth is proposing for these sub-loop elements in his testimony, while Mr. Milner discusses sub-loop access.

Issue 5: "For which signaling networks and call-related databases should rates be set?"

Q. WHAT COST SUPPORT HAS BELLSOUTH PREPARED IN RESPONSE TO THIS ISSUE?

A. BellSouth previously submitted costs for 800 Access, Line Information Database ("LIDB") Access, and CCS7 Signaling Transport in Docket Nos. 960833-TP, 960846-TP, and 960916-TP. This Commission established rates based upon BellSouth's costs for these items. In this docket, BellSouth has revised these elements to reflect the 2000-2002 study period (i.e., factors, labor rates, and material prices were updated). BellSouth is augmenting its list of database access items to include Calling Name ("CNAM"), Local Number Portability ("LNP"), and E911.

Issue 6: "Under what circumstances, if any, is it appropriate to recover non-recurring costs through recurring rates?"

Q. IN ITS COST STUDY, DID BELLSOUTH CONVERT ANY OF ITS NONRECURRING COSTS TO RECURRING?

A. No. The nonrecurring costs, as contained in the April 17, 2000 study reflect the way in which the costs are incurred. In other words, if the costs result from a one-time provisioning process, they are displayed as a nonrecurring cost. The process of converting nonrecurring cost to recurring is sometimes employed in order to reduce the up-front fees charged. However, this is a pricing decision, not generally a part of cost development.

Issue 7: "What are the appropriate assumptions and inputs for the following items to be used in the forward-looking recurring UNE cost study?

(a) network design (including customer location assumptions);
(b) **depreciation;**
(c) **cost of capital;**
(d) **tax rates;**
(e) **structure sharing;**
(f) **structure costs;**
(g) **fill factors;**
(h) **manholes;**
(i) **fiber cable (material and placement costs);**
(j) **copper cable (material and placement costs);**
(k) **drops;**
(l) **network interface devices;**
(m) **digital loop carrier costs;**
(n) **terminal costs;**
(o) **switching costs and associated variables;**

(p) **traffic data;**

(q) **signaling system costs;**

(r) **transport system costs and associated variables;**

(s) **loadings;**

(t) **expenses;**

(u) **common costs;**

(v) **other."**

Q. TO WHICH OF THE ITEMS ARE YOU RESPONDING?

A. I will discuss (a), (d) – (n), and (q) – (t). Mr. Stegeman will also respond to several of these items in regard to the BSTLM. Mr. Cunningham supports BellSouth's depreciation inputs in his testimony, item (b). Dr. Billingsley discusses the appropriate cost of capital (c) in his testimony. Items related to switching and network usage (items (o) and (p)) will be contained in Mr. Page's testimony and Mr. Reid explains shared and common cost ((t) - (u)) development in his testimony.

Q. WHAT ARE THE APPROPRIATE ASSUMPTIONS FOR NETWORK DESIGN (ITEM (a))?

A. As I have mentioned previously, the network design or architecture must reflect not only a forward-looking perspective, but must also be based upon BellSouth's practices and guidelines. In this manner, the resulting costs will reflect costs BellSouth will incur in providing UNEs and combinations on a going-forward

basis. The network design not only impacts the recurring cost development, but also provides a foundation for the development of nonrecurring costs since provisioning practices are based on the type and the design of the equipment being installed. In general, the network design should:

(1) Be forward-looking, yet attainable.

(2) Reflect equipment utilized in BellSouth's network on a going-forward basis.

(3) Reflect BellSouth's Network Guidelines.

(4) Incorporate efficiencies projected to improve provisioning practices.

Q. HOW DID BELLSOUTH DEVELOP THE TAX FACTORS UTILIZED IN ITS COST STUDY FILED ON APRIL 17, 2000 (ITEM (d))?

A. The ad valorem and other tax factor is an effective tax factor furnished by the BellSouth Tax Department. The BellSouth Tax Department develops the factor by calculating the ratio of certain tax expenses to the telephone plant in service, as follows:

$$\frac{\text{Accounts } 7240.1000 + 7240.3000 + 7240.9000}{\text{Telephone Plant In Service (Account 2001)}} =$$

107,585,824/11,306,437,040 = .009515

Account 7240.1000 includes taxes levied upon the assessed value of property. Account 7240.3000 includes taxes levied upon the value or number of shares of outstanding capital stock, upon invested capital, upon rate of dividends paid, etc.

Account 7240.9000 includes other non-income, non-revenue taxes such as municipal license taxes, state privilege taxes, state self-insurer's tax, etc.

Some states and municipalities tax the revenues that a company receives from services provided within the state/municipality. The taxes may be designed to fund such things as Public Service Commission fees, franchise taxes, license taxes, or other similar items, but because the taxes are levied on the basis of revenues, they are commonly referred to as a gross receipts tax. Unlike some taxes that are billed to the customer and flowed through to the taxing authority, a gross receipts tax is a cost of doing business to BellSouth.

The BellSouth Tax Department provides the effective tax rate at which BellSouth is charged by the taxing authority and that rate is "grossed up" to reflect the following formula:

$$\frac{\text{GROSS RECEIPTS TAX RATE}}{(1 - \text{GROSS RECEIPTS TAX RATE})} = .0096$$

Q. HOW DID BELLSOUTH REFLECT STRUCTURE SHARING IN ITS STUDIES (ITEM (e))? HOW WERE THE ASSOCIATED STRUCTURE COSTS DEVELOPED (ITEM (f))?

A. As I explained earlier, BellSouth utilizes loading factors to identify the amount of pole and conduit investment required to support the associated aerial and underground cable. During the development of these factors, anticipated net rents

(expenses paid to other parties for attaching to their structures less revenues received from others for attaching to BellSouth's structures) from sharing arrangements are considered. Thus, implicitly structure sharing is reflected in the calculation. Past information supports the fact that sharing of poles is a relatively common occurrence. In fact, in Florida BellSouth only owns approximately 40% of the poles to which it attaches cable. However, the sharing of conduit space is not as extensive, as reflected in the relatively low amount of rent BellSouth receives from these structures. Sharing of trenching is reflected in the in-plant factor associated with buried cable. Since this factor is developed by analyzing the relationship between total installed investments and material prices, any savings gleaned from sharing of placement costs has been considered. As with the sharing of conduit, joint trenching occurs on a very limited basis.

BellSouth does not anticipate any major changes to the amount of structure sharing in the future. Arguments have been made in past proceedings alleging dramatic increases in the percent of structure sharing due to competition. BellSouth's experience suggests otherwise. Structure sharing is dependent on timing, location of facilities, and technical considerations. It is difficult for all the factors to coincide. In fact, this Commission agreed with this declaration in its Order No.PSC-96-1579-FOF-TP stating: "We are not persuaded by AT&T/MCI's argument that a competitive environment will encourage more structure sharing." (Order No.PSC-96-1579-FOF-TP at Page 78)

BellSouth utilized loading factors to determine the cost of the poles and conduit. Even though the BSTLM has the flexibility to "place" structures, BellSouth felt the

use of loading factors more accurately portrays the costs BellSouth is expected to incur in provisioning loops on a going-forward basis.

Q. HOW DID BELLSOUTH DETERMINE THE FILL FACTORS THAT WERE UTILIZED IN THE COST STUDY (Item (g))?

A. BellSouth's fill factors were based upon the FCC's directive that "[p]er unit costs shall be derived from total costs using reasonably accurate 'fill factors.'" (¶682) In many cases, BellSouth Network provided the anticipated utilization of the equipment based on projected demand and quality of service considerations.

For unbundled loops (and sub-loops), the fill factors were developed within the BSTLM. As I explained earlier, the BSTLM builds facilities to meet existing customer demand. Cables are then sized to appropriately serve that demand in an efficient manner. Thus, the utilization is a product of this exercise. Even though the model allows for growth to be considered in the sizing of cables, BellSouth set the growth component to zero. Thus, spare capacity for growth was not reserved. As I mentioned previously, the model produced the reasonable utilizations of 47% for distribution and 74% for copper feeder.

Q. HOW DOES BELLSOUTH ACCOUNT FOR THE COST OF MANHOLES IN ITS STUDIES (ITEM (h))?

A. Manhole costs are not developed individually, i.e., BellSouth does not develop the cost of a 4X6X7 manhole or a 12X6X7 manhole and enter those values into the

BSTLM. Instead, manhole costs are incorporated into the study through the conduit loading factor. The manhole placement costs are considered in the in-plant factors associated with underground cable.

Q. WHAT ARE THE APPROPRIATE MATERIAL AND PLACEMENT COSTS FOR CABLE (ITEMS (i) and (j))?

A. BellSouth used BellSouth-specific costs for both copper and fiber cable. Material prices for copper and fiber cable were obtained from procurement records that reflect actual BellSouth purchase prices and contractual agreements. As previously explained, future inflation trends ("TPIs") were also taken into consideration in order to reflect forward-looking costs. Telephone company engineering and labor costs were derived from BellSouth's Florida in-plant loading factors. In-plant factors convert material prices to a Florida-specific installed investment. BellSouth-specific cable costs reflect economies of scale and vendor prices that an efficient provider would be able to expect to achieve on a going forward basis. Exhibit DDC-2 (inputs to the BSTLM) contains material prices for both copper and fiber cable.

Q. HOW WERE THE COSTS FOR DROPS AND NETWORK INTERFACE DEVICES CALCULATED IN BELLSOUTH'S COST STUDY (ITEMS (k) and (l))?

A. BellSouth used BellSouth-specific costs for the material, travel, and installation labor associated with the NID and the drop in the BSTLM. These costs are based

on material prices for equipment/material and BellSouth's expertise and experience in placing the equipment/material. The BSTLM, through internal calculations determines drop length, which for Florida averaged 116 feet for a 2-wire analog loop.

Q. HOW ARE DIGITAL LOOP CARRIER ("DLC") COSTS DEVELOPED IN THE BSTLM (ITEM (m)) ?

A. The BSTLM determines the size, type, and placement of digital loop carrier system required to serve the designated customer locations. Internal algorithms determine the required number of commons and working plug-ins and supporting equipment necessary based upon vendor capacities and equipment configurations. User populated tables contain BellSouth-specific material prices, reflecting negotiated discount rates, for the individual pieces of digital loop carrier equipment and the vendor capacities.

Q. IN PAST PROCEEDINGS, DIGITAL LOOP CARRIER ("DLC") DEPLOYMENT HAS GENERATED SIGNIFICANT CONTROVERSY. IN PARTICULAR, THE ISSUES OF (1) UNIVERSAL DLC ("UDLC") VERSUS INTEGRATED DLC ("IDLC") AND (2) TR008 SYSTEMS VERSUS GR303 SYSTEMS HAVE BEEN DEBATED. HOW DOES THE BSTLM ADDRESS THESE TWO AREAS OF PAST CONCERN?

A. First, let me discuss the issue of universal versus integrated. It is still BellSouth's contention that for an unbundled offering, only universal digital loop carrier is

appropriate. The only way in which BellSouth can "hand-off" a loop, i.e., unbundle the loop, is to terminate the central office end of the loop on a MDF. Thus, only UDLC (non-integrated) is appropriate for this scenario. However, in the combination studies, IDLC is applicable since the loop and the port are combined and no "hand-off" of the loop is needed. In the BSTLM, Scenarios BST2000 and Copper reflect the unbundled configuration, where each loop is not switched. Thus, in these instances, the loop is not integrated in the switch. However in the Combo Scenario, switched loops are considered. Because these loops are switched, they can be directly integrated into the switch and thus, IDLC is appropriate.

In the past, BellSouth's cost studies did not reflect any GR303-based digital loop carrier systems. This assumption resulted from the extremely limited number of GR303 systems deployed in BellSouth's network and guidelines that restricted consideration of GR303 for future systems until a demand threshold was met. However, BellSouth has reconsidered this directive and now considers GR303 systems in its loop cost modeling. The BSTLM places GR303 systems for all DLC systems with greater than 150 DS0s. For consistency, BellSouth also populated the SCIS/MO database such that GR303 terminations are considered in the switch. BellSouth witness, Mr. Keith Milner, explains why this reflects the most economic architecture.

Q. PLEASE EXPLAIN BELLSOUTH'S BSTLM INPUT VALUES FOR DROP TERMINALS (ITEM (n))?

A. Drop terminal costs for line sizes below 100 pairs are included as exempt material in the in-plant factors used to develop the installed investments of cable. Therefore, terminal costs for these sizes are not included. The material prices for larger sized terminals were obtained from procurement records and were adjusted for inflation. The engineering and labor costs were developed from Florida-specific in-plant factors. As previously explained, the in-plant factor converts material prices to installed investments.

Q. HOW ARE SIGNALING COSTS REFLECTED IN BELLSOUTH'S COST STUDIES (ITEM (q))?

A. One of BellSouth's fundamental studies, the Signaling System 7 ("SS7") Price Calculator, determines the unit costs associated with BellSouth's SS7 network. This price calculator calculates the vendor prices for the equipment and facilities deployed in the BellSouth's regional SS7 signaling network. Studies that require SS7 network resources are linked to the results of this study.

Common channel signaling, using the SS7 signaling protocol, provides the capability of transporting signaling messages used to establish calls and query databases separately from the voice network. The study components are comprised of the six mated Gateway Signal Transfer Point ("STP", packet switch) pairs, the thirteen mated Local STP pairs, the BellSouth signaling links, the Link Monitoring System ("LMS") and the Integrated Digital Service Terminals ("IDSTs") that make up the SS7 infrastructure.

Access Links connect end offices or Service Switching Points to STPs. Bridge Links and Diagonal Links connect STPs that are at the same or different switching hierarchies in the system respectively. Cross Links are administrative links mating paired STPs.

The material prices for the SS7-related equipment are divided by the total annual octets to develop the per unit material prices.

Q. HOW ARE TRANSPORT SYSTEM COSTS DETERMINED (ITEM (r))?

A. Transport costs incorporate the forward-looking Synchronous Optical Network ("SONET") architecture in determining network design and subsequent costs. Inputs to this calculation reflect BellSouth-specific costs for Florida. They include fill factors, SONET material prices, number of nodes on a ring, air-to-route factor, and the mix of aerial, underground and buried fiber in the interoffice transport.

Q. WHAT ARE THE APPROPRIATE LOADINGS TO BE USED (ITEM (s))?

A. I have discussed loading factors and their development earlier. BellSouth uses loading factors for land, buildings, poles, conduit, and the capitalized RTU fees associated with switching. Additionally, loading factors were used to augment material prices to account for supporting equipment and power and for capitalized labor (in-plants). To summarize, since these factors are calculated from BellSouth's accounting records and the projected view of BellSouth's future additions in the various accounts, these values reflect costs that an efficient

provider would be able to expect to achieve on a going forward basis.

Q. HOW ARE EXPENSES REFLECTED IN BELLSOUTH'S COST STUDY (ITEM (t))?

A. Expenses are found in three areas of the study, in the shared cost component, in the common cost component and in the plant specific costs. BellSouth witness, Mr. Reid, discusses the types of expenses captured in the shared and common factors. The development of Plant Specific factors has been discussed previously.

Issue 8: "What are the appropriate assumptions and inputs for the following items to be used in the forward-looking nonrecurring UNE cost study?

(a) Network design;
(b) OSS design;
(c) Labor rates;
(d) Required activities;
(e) Mix of manual versus electronic activities;
(f) Other.

Q. WHAT NETWORK DESIGN SHOULD BE ASSUMED TO DEVELOP NONRECURRING COSTS (ITEM (a))?

A. The same network design assumptions that provide the foundation for recurring

costs should be utilized when developing nonrecurring costs. Thus, the network should be forward-looking, reflect BellSouth's guidelines and practices, should consider potential process improvements, and should be attainable.

Q. WHAT OSS DESIGN WAS ASSUMED IN THE COST DEVELOPMENT (ITEM (b))? WHAT IS THE PROPER MIX OF ELECTRONIC AND MANUAL ACTIVITIES (ITEM (e))?

A. BellSouth developed interfaces that allow Alternative Local Exchange Carriers ("ALECs") access to BellSouth's existing legacy systems, as directed by the FCC. Paragraph 523 of the FCC's First Report and Order states:

"We thus conclude that an incumbent LEC must provide nondiscriminatory access to their operations support systems functions for pre-ordering, ordering, provisioning, maintenance and repair, and billing available to the LEC itself."

BellSouth provides ALECs access via mechanized interfaces to certain operational support systems ("OSSs"). The interactive pre-order activities revolve around telephone number reservation, address validation, switch feature and service verification, and due date calculation. ALEC access to Customer Service Records allows ALECs to increase the accuracy of orders by using existing name, address, directory, and line features and service options information.

The ordering processes facilitate interactive order entry, order status inquiry, and supplemental order entry. The ALECs are allowed to access the BellSouth's

internal network legacy systems with a single log-on. The ALEC is then authorized to access the electronic interfaces to perform interactive pre-ordering and ordering functions. The electronic interfaces manage the sending and receiving of data to and from the BellSouth OSSs.

BellSouth also provides the ALECs the option of submitting LSRs manually. LSRs not submitted through a BellSouth Electronic Interface, as described earlier, will be considered a manual LSR. A service representative in the Local Carrier Service Center ("LCSC") manually enters the LSR information into BellSouth's legacy (existing) service order systems. Once the Firm Order Confirmation ("FOC") status is returned from the systems, this notification is faxed to the ALEC.

In this filing, BellSouth did not include the cost of the OSS interfaces developed to allow competitors access to BellSouth's provisioning systems. This Commission in its order in Docket Nos. 960757-TP, 960833-TP, and 960846-TP stated "we strongly encourage the parties to negotiate in good faith to establish rates for OSS functions." (Order at Page 165) However, a resolution has never occurred and BellSouth has not recovered either the cost it incurred to develop the interfaces or the ongoing costs associated with these interfaces that are utilized by the ALECs in Florida.

However, BellSouth did reflect the labor costs associated with the tasks required to fill an order. Two cost elements encompass these costs; Electronic Service Order per local service request and Manual Service Order per local service request. The Electronic Service Order costs were developed based upon projected fall-out rates

for orders placed electronically and include fall-out generated by ALEC errors and "by design." Experts familiar with ALEC order processing provided the distribution of the different types of UNE orders, e.g., individual unbundled network elements, combinations, and complex orders, the time required to handle the different types of orders, and the amount of fall-out that occurs for electronic orders.

Q. HOW DID BELLSOUTH DEVELOP ITS LABOR RATES (ITEM (c))?

A. Labor rates for specific work groups are developed based on extracts of previous year's data from the Financial Front End System. This extract accumulates labor expense and hours. A PC application processes this information to produce labor rates. During processing, the actual costs for a given work group are accumulated by expenditure type (e.g., direct labor productive, premium, other employee, etc.). These actual costs are divided by the actual hours (classified productive hours for plant and engineering work groups and total productive hours for cost groups) reported by work group to determine the basic rates. The base year of labor rate data collection was the 1998 calendar year. A labor inflation factor is developed from the BellSouth Region TPIs and is applied to inflate these rates to the study period 2000-2002.

Q. HOW WERE THE REQUIRED ACTIVITIES DETERMINED BY BELLSOUTH (ITEM (d))?

A. As I have discussed previously, personnel familiar with the provisioning process

provided input into the nonrecurring cost development. They provide the process flow, the work centers involved, any probabilities that may be required, and the time required by work center. Provisioning activities can be desegregated into five basic categories: Service Inquiry, Service Order Processing, Engineering, Connect & Test, and Travel. (Every category is not applicable to every unbundled network element.) Service Inquiry reflects an up-front process by which the availability/suitability of facilities is determined. Service Order Processing considers activities incremental to the Electronic and Manual Service Order rate elements previously described. Let me note that the only work center considered in the two Service Order elements is the LCSC. However, other work centers may be involved in service processing for certain elements. Engineering times reflect activities such as, the work required to construct design lay-out records, review of pending jobs, and confirmation of network design standards. Connect & Test considers the physical activities required to provision the requested element and to ensure the transmission quality of the element. Forces involved with Connect & Test include such groups as Installation and Maintenance, Special Services Installation and Maintenance, Circuit Provisioning Group, and Recent Change Memory Administration Group. The Travel category reflects the amount of time needed by technicians to get to the work location. Travel times consider accomplishing more than one task per trip.

Q. ARE THERE OTHER TOPICS RELATED TO NONRECURRING COST DEVELOPMENT THAT SHOULD BE DISCUSSED (ITEM (f))?

A. Yes. In this proceeding, there are really three different types of nonrecurring

categories; nonrecurring costs for unbundled network elements, nonrecurring costs for combinations that currently exist in BellSouth's network ("switch-as-is" combinations), and nonrecurring costs for combinations that do not currently exist in BellSouth's network ("new" combinations). Thus, the required activities vary based on whether the ALEC is ordering an unbundled element, an existing combination or a new combination.

Issue 9: "What are the appropriate recurring rates (average or deaveraged as the case may be) and non-recurring charges for each of the following UNEs?

(1) 2-wire voice grade loop;
(2) 4-wire analog loop;
(3) ISDN/IDSL loop;
(4) 2-wire xDSL-capable loop;
(5) 4-wire xDSL-capable loop;
(6) 4-wire 56 kbps loop;
(7) 4-wire 64 kbps loop;
(8) DS1 loop;
(9) High capacity loops (DS3 and above);
(10) Dark fiber loop;
(11) Subloop elements (to the extent required by the Commission in Issue 4)
(12) Network interface device;
(13) Circuit switching (where required);

(14) Packet switching (where required);

(15) Shared interoffice transmission;

(16) Dedicated interoffice transmission;

(17) Dark fiber interoffice facilities;

(18) Signaling networks and call-related databases;

(19) OS/DA (where required)."

Issue 10: "What is the appropriate rate, if any, for customized routing?"

Q. WHAT COST SUPPORT HAS BELLSOUTH DEVELOPED IN RESPONSE TO THESE ISSUES?

A. BellSouth has developed recurring and nonrecurring costs, as appropriate, for all of the requested items in Issue #9 except for packet switching and operator call processing and directory assistance services ("OS/DA"). The FCC in its UNE Remand Order recognized that incumbent providers do not have an advantage in deploying packet switching. Paragraph 306 states: "The record demonstrates that competitors [ALECs] are actively deploying facilities used to provide advanced services to serve certain segments of the market – namely medium and large business – and hence they cannot be said to be impaired in their ability to offer service." Thus, the FCC released incumbents from the obligation of unbundling packet switching with one caveat. "Incumbent LECs must provide requesting carriers with access to unbundled packet switching in situations in which the incumbent has placed its DSLAM in a remote terminal. The incumbent will be relieved of this unbundling obligation only if it permits a requesting carrier to

collocate its DSLAM in the incumbents remote terminal." (¶313, FCC Docket CC 96-98 UNE Remand Order) BellSouth has developed the cost associated with allowing an ALEC to collocate in the remote terminal and has filed those costs in this proceeding.

The FCC's UNE Remand Order also states "where incumbent LECs provide customized routing, lack of access to the incumbents' OS/DA service on an unbundled basis does not materially diminish a requesting carrier's ability to offer telecommunications service." (¶441, FCC Docket CC 96-98 UNE Remand Order) Since BellSouth deploys customized routing, it is not obligated to provide operator call processing and directory assistance services. This Commission has established permanent rates for customized routing based on the use of Line Class Codes in Docket Nos. 960757-TP, 960833-TP, and 960846-TP. In this docket, BellSouth is revising those costs and also submitting costs for the AIN-based solution to customized routing (response to Issue #10).

Issue #11: "What is the appropriate rate, if any, for line conditioning, and in what situations should the rate apply?"

Q. WHAT COST SUPPORT HAS BELLSOUTH DEVELOPED IN RESPONSE TO THIS ISSUE?

A. BellSouth has structured the Loop Conditioning (Loop Modification) costs to appropriately reflect the way in which the costs to provide this service will occur. Costs were developed for loops less than 18,000 feet and for loops greater than

18,000 feet. In its study, BellSouth assumed for loops less than 18,000 feet that 10 pairs will be conditioned at the same time. This is based on projected demand for the conditioned loops. Additionally, for loops less than 18,000 feet the impact of this procedure on voice grade service will be minimal since load coils neither enhance nor impair the quality of voice transmission for loops of that length. However, for loops greater than 18,000 feet, the removal of intermediary electronics would likely degrade the voice grade transmission quality, rendering it unusable for voice grade transmission. Thus, to minimize the quantity of voice grade circuits that will be unavailable for transmission of voice grade level service, BellSouth practices assume only one circuit will be conditioned initially.

One may argue that intermediary devices are not required for loops less than 18,000 feet and thus, BellSouth is not entitled to recover costs to remove those devices. However, the FCC responded to such arguments and states: "We agree that networks built today normally should not require voice-transmission enhancing devices on loops of 18,000 feet or shorter. Nevertheless, the devices are sometimes present on such loops, and the incumbent LEC may incur costs in removing them. Thus, under our rules, the incumbent should be able to charge for conditioning such loops." (¶193, FCC CC Docket 96-98 UNE Remand Order)

Issue #12: "Without deciding the situations in which such combinations are required, what are the appropriate recurring and non-recurring rates for the following UNE combinations:

(a) "UNE platform" consisting of : loop (all), local (including packet, where

required) switching (with signaling), and dedicated and shared transport (through and including local termination);

(b) "extended links" consisting of:

(1) loop, DS0/1 multiplexing, DS1 interoffice transport;

(2) DS1 loop, DS1 interoffice transport;

(3) DS1 loop, DS1/3 multiplexing, DS3 interoffice transport."

Q. WHAT COST SUPPORT HAS BELLSOUTH DEVELOPED IN RESPONSE TO THIS ISSUE?

A. BellSouth has developed recurring costs for the following UNE Platforms: 2-wire voice grade loop with 2-wire voice grade port and 2-wire ISDN digital loop with 2-wire ISDN port. Recurring costs for other platform combinations, e.g., 4-wire DS1 digital loop with 4-wire ISDN trunk port, 4-wire DS1 loop with DDITS port, or a 2-wire loop/2-wire voice grade transport/2-wire port combination, can be determined by adding the individual UNE recurring costs. The associated nonrecurring costs are displayed on the summary sheets. For example the nonrecurring cost to switch a res/bus 2-wire voice grade loop with 2-wire voice grade port to an ALEC is $ .198. The additional cost of $2.77 for electronic ordering would also apply.

BellSouth developed "extended link" costs for combinations, e.g., 2-wire voice grade loop with dedicated DS1 interoffice transport, 2-wire ISDN loop with DS1 interoffice transport, 4-wire DS1 digital loop with dedicated STS-1 interoffice

transport, and 2-wire voice grade loop with dedicated DS1 interoffice transport with 3/1 mux.

Refer to BellSouth's Final Cost Summary contained in Section 2 of the study filed on April 17, 2000. Elements P.1 through P.58 are the combinations BellSouth has studied. These combinations reflect the most common configurations.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. This Commission has ruled on the appropriate methodology for developing costs for unbundled network elements, TSLRIC plus shared and common or the equivalent TELRIC economic costs. BellSouth utilized the principles inherent in this methodology for its cost studies filed April 17, 2000. Thus, the incremental recurring and nonrecurring costs are long-run and reflect an efficient, forward-looking, yet attainable, network.

BellSouth employed several models to develop the cost support. These models incorporated the TSLRIC/TELRIC principles and to the greatest extent possible are open for inspection. With this proceeding, BellSouth has introduced two new models, the BSTLM (for loops) and the SST model (for switching). Additionally, BellSouth has made enhancements to the BellSouth Cost Calculator (AKA the TELRIC Calculator) and the Capital Cost Calculator to increase user flexibility and to ease processing.

Since the results of the cost study must replicate the incremental costs BellSouth

will incur in providing unbundled elements and combinations to competitors, BellSouth-specific values are the only relevant source for inputs. Thus, the inputs utilized in BellSouth's cost studies reflect BellSouth network guidelines, provisioning practices, vendor discounts, labor rates, and factors.

Costs have appropriately been deaveraged into three zones that reflect geographic differences. BellSouth contends that only loops and local channels (below DS3 level), sub-loops and combinations that are comprised of loops should be deaveraged.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

BELLSOUTH TELECOMMUNICATIONS, INC.

REBUTTAL TESTIMONY OF D. DAONNE CALDWELL

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 990649-TP

(PHASE 1)

JUNE 29, 2000

Q. PLEASE STATE YOUR NAME, ADDRESS AND OCCUPATION.

A. My name is D. Daonne Caldwell. My business address is 675 W. Peachtree St., N.E., Atlanta, Georgia. I am a Director in the Finance Department of BellSouth Telecommunications, Inc. (hereinafter referred to as "BellSouth"). My area of responsibility relates to economic costs.

Q. ARE YOU THE SAME D. DAONNE CALDWELL THAT FILED DIRECT TESTIMONY ON MAY 1, 2000 IN THIS DOCKET?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to respond to cost development issues raised in the testimony filed by intervening parties. Specifically, I respond to allegations made by AT&T/MCI WorldCom witness, Mr. Jeffrey King, BlueStar/Covad/Rhythms Links witness, Ms. Terry Murray, Supra witnesses, Ms. Carol Bentley and Mr.

David Nilson, and Z-Tel witness, Dr. George Ford concerning Issues 5, 6, and 7(d).

Issue 5: "For which signaling networks and call-related databases should rates be set?"

Q. PLEASE DESCRIBE THE COST SUPPORT BELLSOUTH DEVELOPED FOR UNBUNDLED SIGNALING NETWORKS AND DATABASES.

A. The Federal Communications Commission's ("FCC's") Third Report and Order defines BellSouth's obligations with respect to Signaling Networks and Call-Related Databases in Appendix C of that order. The FCC states that Signaling Networks include signaling links and signaling transfer points. Additionally, BellSouth is obligated to provide access to the signaling network "in the same manner in which it obtains such access itself."

In outlining BellSouth's obligations with respect to unbundling Call-Related Databases, the FCC states:

> "an incumbent LEC shall provide access to its call-related databases, including but not limited to, the Calling Name Database, 911 Database, E911 Database, Line Information Database [LIDB], Toll Free Calling Database, Advanced Intelligent Network [AIN] Databases, and downstream number portability databases".

Thus, in response to these FCC mandates, BellSouth filed costs for 800 Access, Line Information Database ("LIDB") Access, and CCS7 Signaling Transport and database access items, Calling Name ("CNAM"), Local Number Portability ("LNP"), and E911.

Furthermore, the FCC also stated in Appendix C that BellSouth must "provide a requesting telecommunications carrier the same access to design, create, test, and deploy Advanced Intelligent Network-based services at the service management system [SMS]." Thus, BellSouth developed TELRIC based costs for Service Management System Access and AIN Toolkit. AIN Toolkit is a product designed to provide an ALEC with the ability to create and offer AIN service applications to their end users. Service applications are created in a BellSouth-provided Service Creation Environment ("SCE") using a BellSouth-provided Graphical User Interface ("GUI"). AIN SMS Access provides access to the SCE and supports administrative activities (e.g., inputting end user specific data or accessing usage reports) associated with the service applications that are created using AIN Toolkit.

Q. AT&T/MCI WITNESS, MR. KING, INCLUDES DIRECTORY ASSISTANCE ("DA") DATABASE ACCESS IN HIS LIST OF DATABASES FOR WHICH THE COMMISSION SHOULD ESTABLISH RATES. IS BELLSOUTH'S DA DATABASE A "CALL-RELATED DATABASE"?

A. No. The FCC did not identify DA database as a call-related database and it is not a database that is "used in signaling networks for billing and collection or the transmission, routing or other provision of telecommunications service." (Third

Report and Order, ¶403) Furthermore, I explained in my direct testimony and as discussed by Mr. Varner, the FCC exempted operator services and directory assistance from an incumbent's unbundling obligations if the incumbent provides customized routing, which BellSouth does. (Third Report and Order, ¶441) It is my understanding that the issues concerning Operator Services/Directory Assistance will be considered in Phase II of this proceeding.

Q. Z-TEL WITNESS, DR. FORD, MAINTAINS THAT BELLSOUTH MUST DEVELOP THE COST OF "INTERFACING BELLSOUTH SWITCHES WITH Z-TEL PROVIDED CALL-RELATED DATABASES OR SCPS." (PAGE 6) IS HE CORRECT?

A. No. The FCC rejected a similar request by Low Tech Designs that the FCC mandate the interconnection of ALEC-provided AIN Service Control Points ("SCPs"). The FCC stated: 'We decline this request because we find that there is not enough evidence in the record to make a determination as to the technical feasibility of interconnecting third-party SCPs and Intelligent Peripherals to incumbent LECs' signaling networks." (Third Report and Order, ¶407) Thus, BellSouth is not obligated by FCC rules to offer this interconnection.

Q. DID THE FCC LEAVE OPEN THE POSSIBILITY THAT A STATE COMMISSION MAY ADDRESS THE ISSUE OF DIRECTLY INTERCONNECTING AN ALEC'S SCP WITH BELLSOUTH'S SIGNALING NETWORK?

A. Yes. However, this Commission has already considered and rejected an ALEC's direct interconnection with BellSouth's SCP. In its Order No. PSC-96-1579-FOF-TP issued December 31, 1996, the Commission stated that "BellSouth shall be allowed to use mediation mechanisms as necessary" when allowing access to its SS7 network. (Page 21) While the Commission's decision did not directly address the interconnection between an ALEC's SCP and BellSouth's SS7 network, the rationale is the same. Thus, Z-Tel must interconnect its SCP with the mediation mechanism, i.e., BellSouth's Signal Transfer Point ("STP") gateway, in order to prevent intentional and unintentional disruption of BellSouth's network either for BellSouth's end users or the end users of the ALEC.

Q. WHAT ARE MEDIATION DEVICES?

A. Mediation devices are computer programs which during call processing determine the effect of routing instructions or other information returned as a result of an SCP query and then cause appropriate activities to be taken. These devices evaluate the request to determine if it is potentially harmful to BellSouth's network.

Q. HAS BELLSOUTH DEVELOPED COSTS THAT WOULD ALLOW Z-TEL TO INTERCONNECT ITS SCP WITH BELLSOUTH'S NETWORK WITH A MEDIATION DEVICE?

A. Yes. However, as I have stated previously, Z-Tel must interconnect through BellSouth's STP gateway, not directly to the end-office. In fact, this is the architecture BellSouth has deployed for its own SS7 network; SCPs connect with

STPs, which in turn connect to the end-office (Service Switching Point).

The cost study filed on April 17, 2000 contains all of the unbundled components necessary to interconnect Z-Tel's SCP to BellSouth's STP; the facility between the SCP and STP, the termination on the STP, and usage of BellSouth's SS7 network.

Q. DR. FORD ALLEGES THAT BELLSOUTH HAS DOUBLE COUNTED THE COST OF THE AIN TRIGGERS. (PAGE 7) DO YOU AGREE WITH DR. FORD?

A. No. Dr. Ford is clearly wrong. BellSouth has not "double counted" the cost of AIN triggers as he alleges. Trigger costs associated with the end office have appropriately been captured in the vertical feature costs that BellSouth developed since they are part of the features and functions provided by the switch. There are no trigger-related investments in the AIN SMS or AIN Toolkit. Dr. Ford also erroneously states that BellSouth "Trigger Access Charge" is unsupportable. Work activities as outlined in the cost study are required in order to establish, route and translate the specific type of trigger required by the ALEC. The labor costs associated with these activities are reflected in the cost study filed on April 17, 2000.

Issue 6: "Under what circumstances, if any, is it appropriate to recover non-recurring costs through recurring rates?"

Q. BLUESTAR/COVAD/RHYTHMS LINKS WITNESS, MS. MURRAY,

STATES THAT NONRECURRING COSTS ARE SUNK COSTS. IS SHE CORRECT?

A. No. On page 4 of her testimony, Ms. Murray defines a sunk cost as "a cost that, once incurred, a firm cannot recover if it ceases business." I agree that once BlueStar/Covad/Rhythms pays BellSouth for provisioning a UNE, that cost is "sunk" from BlueStar/Covad/Rhythms' viewpoint. However, presumably neither BlueStar, Covad, Rhythms, nor any other ALEC, would incur a cost without anticipating recovering that cost from the ultimate end user. Once this Commission establishes nonrecurring rates, BlueStar/Covad/Rhythms will know the up-front costs it will incur and thus, what and how it needs to charge its end users in order to conduct its business.

From a cost development perspective, BellSouth's sunk costs are excluded from consideration. After all, another definition of a sunk cost is a cost that has been incurred **in the past** and cannot be changed by any current or future decision. Since sunk costs were incurred "in the past," sunk costs are, by definition, embedded. The FCC's TELRIC methodology specifically prohibits the inclusion of embedded costs and thus, they are excluded from BellSouth's study. It is important to remember that the nonrecurring activities associated with UNE provisioning are only begun at the request of an ALEC. Thus, they cannot be "sunk". In other words, only after an ALEC requests a UNE does BellSouth undertake activities to provide the requested UNE. The ALEC initiates the actions and causes BellSouth to incur costs for which BellSouth legitimately should be compensated.

Q. MS. MURRAY COMPARES THE LOOP INVESTMENT TO THE NONRECURRING COST TO DELOAD A LONG UNBUNDLED COPPER LOOP. (PAGES 9-11) IS HER COMPARISON VALID?

A. No. Ms. Murray's apples-to-oranges comparison is not particularly insightful since there is no correlation between the two types of costs. Investments result from the purchasing, engineering, and installing of equipment required to provide the UNE, i.e., the physical plant. Nonrecurring costs are directly proportional to the amount of time required to complete the task. The process of unloading a cable is extremely labor-intensive, thus the perceived "high" cost.

However, even if one were to give some weight to Ms. Murray's argument, her comparison is still flawed. Ms. Murray compares an activity performed in conjunction with a long loop. Thus, assuming that the exercise in which she is engaging was relevant, the proper comparison would be to the investment for the same type of loop. For some reason, Ms. Murray compares the nonrecurring cost associated with unloading an unbundled long loop to a 2-wire analog loop of average length. For discussion purposes the investment associated with a 2-wire unbundled copper loop – long is $2,466, as compared to the investment used by Ms. Murray of $835.

As I explained in my direct testimony, BellSouth will unload only one pair at a time for long copper loops in order to maintain the integrity of the other loops carrying voice grade service within the same cable.

Q. ARE THERE OTHER COMMENTS THAT MS. MURRAY MAKES THAT REQUIRE COMMENT?

A. Yes. There are several incorrect statements Ms. Murray makes in her testimony to which I must respond. On page 8, she states that "BST has proposed a charge of $772.31 for removing **the first load coil** from a loop of greater than 18,000 feet." (Emphasis added.) This is inaccurate. BellSouth's rate is to unload the entire loop, not just to remove the first load coil. Within the study, an assumption was made as to the average number of load coils that would be removed from each loop.

On page 9, Ms. Murray states: "it appears that BST is proposing to apply nonrecurring 'conditioning' charges to every xDSL-capable loop, including those that do not require 'conditioning'." Ms. Murray's statement misses the point. BellSouth has endeavored to expand the universe of xDSL-capable loops for short loops by unloading 10 pairs each time conditioning takes place. The cost has been allocated among those 10 pairs. Thus, the ALEC pays only $1/10^{th}$ of the total cost when conditioning is requested on short loops. The additive is intended to recover the portion of the cost for conditioning not recovered elsewhere; i.e., not recovered from retail services or other requests for unbundled xDSL loops. It is projected that of the 10 conditioned loops, an ALEC will purchase 2 and BellSouth will utilize 4 pairs. That leaves 4 pairs whose conditioning costs will not be recovered. BellSouth developed an additive that is applied to ADSL-compatible loops, HDSL-compatible loops, and UCLs in order to be compensated for the unrecovered costs based on the probability of these xDSL lops requiring conditioning.

Also on page 9, Ms. Murray discusses additional nonrecurring charges she claims may be required when an ALEC orders ADSL-compatible loops. She states that the "total does not include any charges for manual service order processing, order coordination, manual loop qualification, or specific loop 'conditioning'". (Page 9) Ms. Murray is mistaken. Rebuttal Exhibit DDC-5 shows the input sheet BellSouth included in its April 17th filing. Currently, the first step is a Service Inquiry, i.e., loop qualification. If the loop does not qualify, i.e., it does not meet the design standards for an ADSL loop, BellSouth informs the ALEC and no charge is assessed. Additionally, BellSouth informs the ALEC if the reason the loop does not qualify is because of load coils or bridge tap. At this point, the ALEC has the option of requesting loop conditioning. If another xDSL loop would qualify (e.g., UCL-Short), this information is also provided to the ALEC. Note in Exhibit DDC-5 that if the loop does qualify, order coordination is included in the nonrecurring cost.

Q. SUPRA WITNESS, MR. NILSON, STATES THAT "NON-RECURRING COSTS OF INFRASTRUCTURE, PURCHASE, AND CONSTRUCTION IS A COST TO BE SHARED BY THE CARRIERS USING THE FACILITY, OVER THE USEFUL LIFE OF THE FACILITY." (PAGE 9) DOES BELLSOUTH'S COST STUDY FOR THE UNES UNDER CONSIDERATION IN THIS PROCEEDING ADHERE TO THIS DEFINITION?

A. Yes. Mr. Nilson is describing the capitalized labor included in the cable investment. BellSouth considers these costs in its study through the use of in-plant factors that

augment the material price to recognize the associated labor required to install the cable. By including these labor costs as part of the investment, the cost is recovered over the useful life of the plant. Additionally, because these costs are spread over the life of the plant, AT&T/MCI witness, Mr. King's concern that "the first user will be forced to pay more than its fair share" is a not an issue. (Page 6 of King Testimony)

Q. MR. NILSON ALSO STATES THAT "TASK RELATED NON-RECURRING COSTS ARE SPECIFIC TO A GIVEN CARRIERS ORDER FOR A PARTICULAR SERVICE AND SHOULD REMAIN NON-RECURRING COSTS." (PAGE 9) DOES BELLSOUTH AGREE?

A. Yes, at least from a cost development perspective. The Commission has the option of mandating a recurring rate that is financially equivalent to the nonrecurring costs. Additionally, the ALEC also has the option of charging the end user a recurring rate to recover the nonrecurring cost paid to BellSouth. However, BellSouth's cost study reflects the one-time costs that are unique to the request made by the ALEC as nonrecurring costs. However, Mr. Nilson goes on to advocate that these costs could be charged on an Individual Case Basis ("ICB"). The use of ICB billing has been portrayed as a deterrent to the ALEC's ability to accurately project expenditures. Thus, every attempt has been made in BellSouth's cost studies to eliminate ICB charges. Nonrecurring costs are based upon standardized procedures that are used throughout the BellSouth region. Work time estimates reflect subject matter experts' anticipated <u>average</u> requirements.

Q. ON PAGE 6, AT&T/MCI WITNESS, MR. KING, DISCUSSES DISCONNECT COSTS. PLEASE COMMENT ON HIS OBSERVATIONS.

A. Mr. King confuses the disconnect issue by never distinguishing between disconnecting unbundled elements and disconnecting combinations of UNEs. The work effort to disconnect an unbundled element is very different from disconnecting a combination. An unbundled element is not a working circuit; it is only a piece of the network. Thus, an unbundled loop, for example, can never be placed in a "soft dial" tone state as Mr. King asserts. The costs BellSouth calculated for UNE disconnect reflect the physical activities that must be undertaken to disconnect each UNE. For loop/port combinations on a switch-as-is basis, the disconnect costs have been paid by the end-user when they initially purchased service. Thus, no additional disconnect costs are appropriate. For loop/transport combinations, BellSouth must perform physical activities, as reflected in the cost study; in order to disconnect the circuit and disconnect costs should apply.

Q. ON PAGE 5 OF HIS TESTIMONY, MR. KING APPEARS TO QUESTION BELLSOUTH'S ADHERENCE TO THE FCC'S TELRIC METHODOLOGY IN DEVELOPING NONRECURRING COSTS. PLEASE COMMENT.

A. Mr. King states that often "nonrecurring charges are based on the activities the ILEC **has** incurred in the past." (Page 5) To the extent Mr. King is implying that BellSouth has based its nonrecurring costs on an outdated process, he is mistaken.

BellSouth's nonrecurring studies are based upon anticipated work times and forward-looking processes that exist today and will be used to provision UNEs for the foreseeable future.

Issue 7: "What are the appropriate assumptions and inputs for the following items to be used in the forward-looking recurring UNE cost study?

(d) **tax rates.**

Q. SUPRA WITNESS, MS. BENTLEY STATES THAT "THE ILEC WILL GENERALLY INCUR NO TAX LIABILITY IN THE UNE ENVIRONMENT." (PAGE 10) IS SHE CORRECT?

A. No. Some states and municipalities tax the revenues that a company receives from services provided within the state/municipality. The taxes may be designed to fund such things as PSC fees, franchise taxes, license taxes, or other similar items, but because the taxes are levied on the basis of revenues they are commonly referred to as a gross receipts tax. Unlike some taxes that are billed to the customer and flowed through to the taxing authority, a gross receipts tax is a cost of doing business to BellSouth. BellSouth receives revenues from the ALECs for the purchase of UNEs and interconnection services and thus must pay this tax. Additionally, BellSouth must pay an ad valorem tax based on the assessed value its property, including the "property" which comprise UNEs leased by ALECs. City and county governments levy these taxes. Both of these taxes are real costs to BellSouth that must be considered in the cost study, as the Florida Commission has previously recognized.

Additionally, Ms. Bentley's statement that "consideration for income taxes have already been factored into the cost of capital" (Page 10) is not correct. It is true that the impact of income taxes is taken into account during the calculation of the capital portion of the annual cost factors. However, income tax is not considered in the development of the cost of capital. Instead cost of capital is considered in the calculation of the income tax expense. Income tax expense is the federal and state taxes levied on "taxable income." While interest to bondholders is book expense and deductible for income tax purposes, the federal government and most state governments levy a tax on the revenues, which are earned to compensate stockholders for the use of their money. BellSouth must pay income taxes on the equity portion of return, but the debt portion is tax exempt.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

(Transcript follows in sequence in Volume 2.)

STATE OF FLORIDA)

: CERTIFICATE OF REPORTER

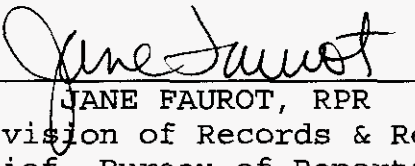
COUNTY OF LEON)

I, JANE FAUROT, RPR, Chief, FPSC Bureau of Reporting Official Commission Reporter, do hereby certify that the Hearing in Docket No. 990649-TP was heard by the Florida Public Service Commission at the time and place herein stated.

It is further certified that I stenographically reported the said proceedings; that the same has been transcribed under my direct supervision; and that this transcript, consisting of 154 pages, Volume 1 constitutes a true transcription of my notes of said proceedings and the insertion of the prescribed prefiled testimony of the witness(s)..

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorneys or counsel connected with the action, nor am I financially interested in the action.

DATED this 25TH DAY OF JULY, 2000.



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