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BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of

DOCKET NO. 960757-TP

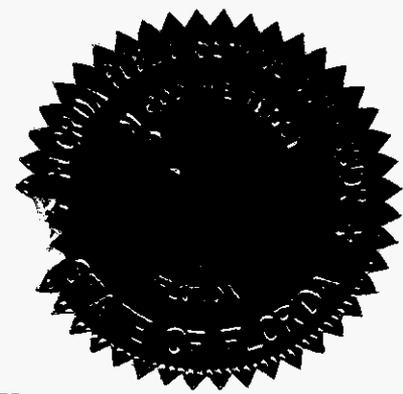
Petition by Metropolitan Fiber
Systems of Florida, Inc. for
arbitration with BellSouth
Telecommunications, Inc.
concerning interconnection, rates,
terms, and conditions, pursuant to
the Federal Telecommunications
Act of 1996.

Petition by AT&T Communications
of the Southern States, Inc. for
arbitration of certain terms and
conditions of a proposed agreement
with BellSouth Telecommunications
Inc. concerning interconnection
and resale under the
Telecommunications Act of 1996.

DOCKET NO. 960833-TP

Petition by MCI Telecommunications
Corporation and MCI Metro Access
Transmission Services, Inc. for
arbitration of certain terms and
conditions of a proposed agreement
with BellSouth Telecommunications,
Inc. concerning interconnection
and resale under the
Telecommunications Act of 1996.

DOCKET NO. 960846-TP



FIRST DAY - MORNING SESSION

VOLUME 1

Pages 1 through 154

PROCEEDINGS: HEARING

DOCUMENT NUMBER - DATE
01799 FEB -4 88
FPSC RECORDS/REPORTING

1
2
3
4
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BEFORE: CHAIRMAN JULIA L. JOHNSON
COMMISSIONER J. TERRY DEASON
COMMISSIONER SUSAN F. CLARK
COMMISSIONER JOE GARCIA
COMMISSIONER E. LEON JACOBS, JR.

DATE: Monday, January 26, 1998

TIME: Commenced at 9:30 a.m.

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: H. RUTHE POTAMI, CSR, RPR
Official Commission Reporter

1 **APPEARANCES:**

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7 **Telecommunications, Inc.**

8 **FLOYD R. SELF** and **NORMAN HORTON**, Messer,
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10 Office Box 1876, Tallahassee, Florida 32302-1876,
11 appearing on behalf of **WorldCom and Metropolitan Fiber**
12 **Systems of Florida.**

13 **RICHARD D. MELSON**, Hopping Green Sams and
14 Smith, Post Office Box 6526, Tallahassee, Florida
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17 Sutherland, Asbill & Brennan, L.L.P, 999 Peachtree
18 Street, N.E, Atlanta, Georgia 30309-3996, appearing on
19 behalf of **MCI Telecommunications Corporation.**

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1 **APPEARANCES CONTINUED:**

2 **TRACY HATCH** and **MARSHA RULE**, AT&T
3 Communications of the Southern States, Inc., 101 East
4 College Avenue, Suite 700, Tallahassee, Florida
5 32301-1509; **JIM LAMOUREAUX**, 1200 Peachtree Street,
6 N.E, Promenade 1, Room 4066, Atlanta, Georgia 30309;
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9 Atlanta, Georgia 30326, and **THOMAS A. LEMMER**, McKenna
10 & Cuneo, L.L.P., Suite 4800, 370 Seventeenth Street,
11 Denver, Colorado 80202-1370, appearing on behalf of
12 **AT&T Communications of the Southern States, Inc.**

13 **BARBARA D. AUGER**, Pennington, Culpepper,
14 Moore, Wilkinson, Dunbar & Dunlap, P.A., 215 South
15 Monroe Street, Tallahassee, Florida 32302-2095, and
16 **CHARLES B. WELCH, JR.**, Farris Mathews, Gilman, Branan
17 & Hellen, P.L.C., Nashville City Center, 5111 Union
18 Street, Suite 2400, Nashville, Tennessee 37219,
19 appearing on behalf of **Time Warner**.

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1 **APPEARANCES CONTINUED:**

2 **BETH KEATING, CHARLIE PELLEGRINI, WILL COX,**
3 **JENNIFER BRUBAKER and MARTHA CARTER BROWN, Florida**
4 **Public Service Commission, Division of Legal**
5 **Services, 2540 Shumard Oak Boulevard, Tallahassee,**
6 **Florida 32399-0870, appearing on behalf of the**
7 **Commission Staff.**

8

9 **ALSO PRESENT:**

10 **CAROLYN MAREK, Vice President of Regulatory**
11 **Affairs, Time Warner.**

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I N D E X

MISCELLANEOUS - VOLUME 1

ITEM	PAGE NO.
Time Warner's Petition for Reconsideration	10

WITNESSES - VOLUME 1

NAME	PAGE NO.
ALPHONSO J. VARNER	
Direct Examination By Mr. Lackey	57
Prefiled Direct Testimony Inserted	61
Prefiled Rebuttal Testimony Inserted	98
Cross Examination By Mr. Lamoureux	150

EXHIBITS - VOLUME 1

NUMBER		ID.	ADMTD.
1	Official recognition list	42	
2	Staff Stip-1	47	
3	Staff Stip-2	48	
4	Staff Stip-3	47	
5	Staff Stip-4	48	
6	Staff Stip-5	49	
7	Staff Stip-6	49	
8	Staff's confidential composite exhibit	53	
9	AJV-1	59	
10	Staff AJV-3	146	
11	Revisions to November 13 testimony of Varner	149	

P R O C E E D I N G S

(Hearing convened at 9:30 a.m.)

CHAIRMAN JOHNSON: We're going to go on the record. Counsel, could you please read the notice?

MR. PELLEGRINI: Pursuant to notice dated December 29, 1997, this time and place have been set for hearing in consolidated Dockets 960757, 960833, and 960846-TP, the petitions for arbitration with BellSouth respectively of MFS, now WorldCom, AT&T and MCI.

CHAIRMAN JOHNSON: Take appearances.

MS. AUGER: Barbara Auger on behalf of Time Warner.

MR. WELCH: I'm Charles Welch.

CHAIRMAN JOHNSON: What was your last name again?

MR. WELCH: Welch.

MS. WHITE: Nancy White, Douglas Lackey, Mike Twomey, and Bennett Ross on behalf of BellSouth Telecommunications.

MR. SELF: Floyd Self of the law firm Messer, Caparello & Self, 215 South Monroe Street, Tallahassee, Florida, appearing on behalf of WorldCom, Inc., Metropolitan Fiber Systems of Florida.

I'd also like to enter an appearance for

1 Norman H. Horton also on behalf of WorldCom.

2 **MR. HATCH:** Tracy Hatch and Marsha Rule, 101
3 North Monroe Street, Tallahassee, Florida, on behalf
4 of AT&T. Also appearing with me will be James P.
5 Lamoureux, in-house counsel to AT&T, and also Tom
6 Lemmer from the firm McKenna & Cuneo, 1900 K Street
7 Northwest, Washington, D.C.

8 Madam Chairman, I would request at this
9 point -- well, go ahead and finish the appearances.

10 **CHAIRMAN JOHNSON:** Mr. Melson.

11 **MR. MELSON:** Richard Melson of the law firm
12 Hopping Green Sams and Smith on behalf of MCI
13 Telecommunications Corporation and MCI Metro Access
14 Transmission Services. Also appearing with me will be
15 Tom Bond of MCI, and seated to my left, Mr. David
16 Adelman on behalf of MCI.

17 **CHAIRMAN JOHNSON:** Okay.

18 **MR. PELLEGRINI:** Charles Pellegrini
19 appearing for the Staff of the Public Service
20 Commission together with Beth Keating, Martha Carter
21 Brown, Will Cox, and Jennifer Brubaker.

22 **CHAIRMAN JOHNSON:** Are there any preliminary
23 matters?

24 **MR. PELLEGRINI:** Yes, Chairman Johnson. It
25 would be appropriate at this time for the Commission

1 to take up Staff's request that the Commission
2 reconsider, on its own motion, its decision at last
3 Tuesday's agenda conference to deny Time Warner's
4 motion for reconsideration of the prehearing officer's
5 order denying party status to Time Warner as well as
6 to others.

7 Through an inadvertence, Time Warner did not
8 receive appropriate and customary notice that its
9 motion would be before the Commission on an emergency
10 basis last Tuesday.

11 Time Warner did not appear to address the
12 Commission; hence, the Commission's decision was made
13 absent Time Warner's addressing the Commission and
14 responding to any questions the Commissioners may have
15 had.

16 Staff's request is intended to provide Time
17 Warner a procedural remedy.

18 **CHAIRMAN JOHNSON:** Okay. Commissioners? He
19 just stated that it would be appropriate if we address
20 the request that we reconsider. Is there a motion?

21 **COMMISSIONER DEASON:** So move.

22 **COMMISSIONER CLARK:** I move.

23 **CHAIRMAN JOHNSON:** There's a motion and
24 second. Any discussion? Seeing none, show that
25 approved, then, unanimously.

1 I guess we're now at the reconsideration
2 stage. It would be appropriate to take arguments.

3 MR. PELLEGRINI: Chairman Johnson, before
4 Time Warner begins, it may be appropriate for me to
5 read the issue as it was presented to the Commission
6 last Tuesday on Staff's recommendation, just to
7 refresh everyone's memory.

8 CHAIRMAN JOHNSON: Certainly.

9 MR. PELLEGRINI: The issue, as we stated it,
10 was as follows: "Should Time Warner's petition for
11 reconsideration of Order No. PSC-98-0008-PCO-TP be
12 granted?"

13 And Staff's recommendation, which the
14 Commission adopted on a unanimous vote, was the
15 following: "No. Time Warner has failed to identify
16 any point of fact or law that the prehearing officer
17 overlooked or failed to consider in rendering Order
18 No. PSC-98-0008-PCO-TP. Furthermore, the Prehearing
19 Officer's order fully comports with the Act's
20 requirements for participation in an arbitration
21 proceeding and is consistent with prior Commission
22 orders regarding participation in arbitration
23 proceedings. Time Warner's petition for
24 reconsideration should, therefore, be denied."

25 CHAIRMAN JOHNSON: Thank you,

1 Mr. Pellegrini.

2 **MS. AUGER:** Commissioners, I'm Barbara
3 Auger, and of my office, Pete Dunbar and I represent
4 Time Warner. We also have with us Carolyn Marek, who
5 is vice-president of regulatory affairs for Time
6 Warner, and Dave Swafford, also of our office.

7 Because Pete Dunbar could not be here --
8 he's in surgery as we speak -- Chuck Welch has come
9 down from Tennessee. He's licensed to practice law in
10 Tennessee, and he represents Time Warner before the
11 Public Service Commission in Tennessee; and I would
12 ask that I sponsor him today and that he be able to
13 make this argument before the Commission.

14 Mr. Pellegrini has indicated that Staff does
15 not have any objection to that.

16 **CHAIRMAN JOHNSON:** Okay. Mr. Welch?

17 **MR. WELCH:** Good morning. Thank you for the
18 opportunity to speak on this issue this morning. I've
19 not been to Tallahassee before and, therefore, some of
20 the argument that I'm about to make I'm sure you've
21 heard at least in part, but I will be very brief.

22 It's my understanding that this Commission,
23 as many commissions in this region, have denied
24 requests of intervenors in arbitration proceedings. I
25 understand and appreciate the reasons that the

1 commissions have taken these positions, not only here,
2 but in other states.

3 The Act requires, however, and the important
4 issue, I think, that's before you today, is that the
5 Act requires that this Commission set
6 nondiscriminatory rates. And this proceeding has
7 taken on a generic issue that's extremely important to
8 all of the parties in the industry.

9 We are, therefore, requesting that -- and
10 not to be confused with a request to get involved in
11 these particular parties' arbitration, we're
12 requesting an opportunity to be heard on the issue of
13 unbundled elements and the setting of those rates, and
14 we think it's very, very important that we be allowed
15 to participate in that decision.

16 The solution that I would suggest to the
17 Commission is to bifurcate this part of the proceeding
18 and make it a generic proceeding so that all parties
19 can participate. This is probably not a very -- won't
20 be a very popular suggestion at this time, but I think
21 that the Commission should suspend or continue the
22 current proceeding, open a generic docket, and let all
23 the parties proceed in that docket and participate in
24 setting those rates, and then we could -- you could
25 adopt those rates in the arbitration proceeding.

1 Now, this would certainly cause some delay,
2 and I understand the problems with that.

3 We have found, however, though, in our
4 participation in other states, in Tennessee, North
5 Carolina, Georgia, and South Carolina, that this issue
6 is the one issue that everybody gets involved in. We
7 see some of the companies elect not to participate in
8 universal service in some of the other important
9 dockets, but everybody participates in the other
10 states in these dockets, and it -- because it's so, so
11 terribly important.

12 The reason it's important -- and, you know,
13 it's always, I guess, the money when we're talking
14 about competition and markets; and our companies have
15 to make money. But we are currently spending
16 somewhere in the neighborhood of a quarter of a
17 million dollars a month in purchasing these type of
18 elements from BellSouth now, and that -- and that's at
19 50% capacity. That will go up as we expand our
20 business.

21 We are interested in what those rates will
22 be. It will affect our bottom line dramatically.
23 We're also very interested in what our competitors,
24 such as AT&T and MCI, are paying for these same
25 elements.

1 It's very important, and I guess the reason
2 it's so crucial is that the -- at the price for
3 these -- if these rates are too high, there won't be
4 any competition. No competition will develop. We'll
5 just be precluded from doing business. If they're too
6 low then, then you'll see only competition develop
7 through resale.

8 **COMMISSIONER CLARK:** Mr. Welch, I need some
9 explanation. You're suggesting bifurcation of what
10 issue?

11 **MR. WELCH:** Of setting rates for unbundled
12 network elements.

13 **COMMISSIONER CLARK:** And those are all the
14 elements listed in Issue 1; is that correct?

15 **MR. WELCH:** Commissioner Clark, I don't have
16 that with me. I'm not --

17 **COMMISSIONER CLARK:** Certainly one issue in
18 this -- I guess I'm having difficulty understanding
19 how it's bifurcated if the sole issue is what you're
20 talking about.

21 **MR. WELCH:** Well, it's probably just a
22 procedural matter. I may be splitting hairs here.

23 **COMMISSIONER CLARK:** Can you take a look at
24 the order?

25 **MR. WELCH:** Yes, ma'am. That is -- the

1 unbundled network elements, I assume that is the issue
2 in this particular arbitration proceeding.

3 **COMMISSIONER CLARK:** Right. That's the only
4 issue, so how would we bifurcate anything?

5 **MR. WELCH:** Well, again, maybe I'm splitting
6 hairs. I just -- I believe the setting of the rates
7 for unbundled network elements is of great importance,
8 and it needs to be done in a generic proceeding
9 because it impacts the entire industry, each and
10 every --

11 **COMMISSIONER CLARK:** And I'm confused about
12 that, because it seems to me in this proceeding we are
13 setting the rates for AT&T, MCI, and somebody else.
14 Let's see. WorldCom MFS. All right.

15 You have the ability to agree to those rates
16 if you choose to, or not agree and arbitrate your own
17 rates if you want to. And I'm having difficulty
18 understanding how your substantial interests are going
19 to be affected by this proceeding and, therefore, we
20 should allow you intervention.

21 And let me point one other thing out. If
22 you are granted intervention, you're going to be bound
23 by these rates, and I don't think you've presented any
24 expert testimony, and I don't know if you're happy
25 with what's been proposed by the various parties.

1 **MR. WELCH:** Quite frankly, we are very
2 concerned that this Commission could go through this
3 proceeding, set rates for these elements, and then
4 later hold another proceeding and find different rates
5 for Time Warner. And that -- quite frankly,
6 Commissioner, that would violate the federal act.

7 I mean, these rates have to be
8 nondiscriminatory. They have to be available to all
9 industry members, all telecommunications service
10 providers, and they have to be the same rate; and
11 that's -- the importance of having one hearing, I
12 believe -- there's several other reasons as well, not
13 the least of which is that BellSouth has a cost model;
14 and they'll use that same cost model in our hearing,
15 in our subsequent hearing.

16 AT&T also has a cost model and it, to the
17 best of my knowledge, is the only other provider that
18 has a cost model, who has had the resources and
19 developed a cost model.

20 If we have another hearing and our -- which
21 is called, I guess, an arbitration for Time Warner,
22 the Hatfield model, the AT&T model, won't even be
23 considered or be presented and --

24 **COMMISSIONER CLARK:** Well, it would be if
25 you presented it. I mean, you would have the ability

1 to come in and say, we think these are the permanent
2 rates that should be arbitrated in this proceeding
3 with respect to these network elements.

4 **MR. WELCH:** Well, certainly we wouldn't be
5 able to present AT&T's model in the same way that AT&T
6 would be able to present it. Obviously we could talk
7 about it and we could refer to it, and we could
8 certainly come up with any sort of evidence that would
9 be admissible before this Commission.

10 But the judicial economy of that -- judicial
11 economy seems to just demand that it be done all at
12 the same time, because we're going to be talking about
13 the exact same rates -- or the exact same elements,
14 and you're going to hear the exact same arguments and
15 be called upon to make the exact same decision; and it
16 seems like such an incredible waste of time, of this
17 Commission's time, not to do it in a generic
18 proceeding where all parties can participate and you
19 can have a full hearing and make a final decision.

20 **COMMISSIONER CLARK:** Thank you.

21 **MR. WELCH:** If I could have one moment,
22 Commissioner Clark. (Pause)

23 Commissioner Clark, I didn't mean to confuse
24 the issue by suggesting that we bifurcate the
25 proceeding. All I mean to suggest there is -- and I

1 don't think it really matters how the Commission gets
2 there so long as it has a proceeding that is open to
3 all telecommunication service providers to participate
4 in setting of those rates; and I just merely suggested
5 that that would be one way of doing it. There's
6 certainly others.

7 **CHAIRMAN JOHNSON:** Are you saying "in
8 addition to this proceeding," or "in lieu of"?

9 **MR. WELCH:** In lieu of.

10 **CHAIRMAN JOHNSON:** So is your request a
11 request to intervene, or is it a request to defer,
12 or -- because if you want to intervene, if we were to
13 rule on that and to allow you in this case, I'm
14 understanding you to say that that's not sufficient,
15 that you really want a more broader, more generic type
16 of proceeding anyway.

17 **MR. WELCH:** I think it needs to be a broader
18 proceeding. If the Commission elects to stay in this
19 proceeding, then I think it needs to allow all
20 telecommunication service providers that will come
21 forward and allow them to participate on this issue.

22 **CHAIRMAN JOHNSON:** You mentioned one other
23 thing, Mr. Welch. You stated that if we were to
24 continue with this proceeding and set the rates for
25 these particular parties for the elements that are

1 delineated, that that would be binding upon the other
2 parties, that we would not under the federal act -- I
3 thought you said that, that it would be binding.

4 **MR. WELCH:** Well, the federal act requires
5 that nondiscriminatory prices be set. Now, if we're
6 talking about the same network element at -- offered
7 at different prices to different telecommunication
8 service providers, I would find it hard -- it would be
9 very difficult to find a situation where that would
10 not be discriminatory. So that would violate the
11 federal act, in my opinion.

12 **CHAIRMAN JOHNSON:** Okay.

13 **COMMISSIONER JACOBS:** I have a question on
14 that. That seems to assume that you enter into your
15 negotiations with BellSouth with these proceedings as
16 a precedent, and it's my understanding that that's not
17 anticipated under the Act, that each round of
18 negotiations begins anew. Is that a correct reading
19 of the statute?

20 **MR. WELCH:** I think that's fair, yes, sir.

21 **COMMISSIONER JACOBS:** It would appear to me
22 that perhaps making this proceeding have a broader
23 impact would even limit your options, because you
24 still have the opportunity to come in and stipulate as
25 to whatever is decided in this docket, or choose to

1 negotiate further.

2 **MR. WELCH:** Yes, sir. I think that's fair.
3 But I think it would be -- I would be remiss to
4 believe that this Commission could hear BellSouth's --
5 go through a three-day hearing this week, hear
6 BellSouth's proof, and then sometime in the future, a
7 month or so from now, Time Warner would come in and
8 put on its case and that this Commission would have a
9 different finding.

10 And since the Commission is broaching this
11 issue for the first time this week in this hearing,
12 and Time Warner does not have an opportunity to
13 participate in this initial finding, I think we're
14 being prejudiced by that.

15 **COMMISSIONER CLARK:** Mr. Welch, I would
16 point out that these -- this original arbitration
17 started over a year ago, and we were -- the Commission
18 was not satisfied with the numbers we got with respect
19 to this cost study, and we set interim rates and said
20 we're going to do permanent rates. So this issue has
21 been pending for more than a year.

22 And I would point out we had other
23 intervenors, which -- requests for intervention which
24 we denied, and one of them, Intermedia, brought up to
25 me what is the more cogent reason that we might let

1 people in; and that is the fact that in a -- is it a
2 271 where the application to the FCC -- that Bell
3 would rely on those permanent rates and say, well, we
4 have set them. And what we did was clarify the fact,
5 and it was based on a representation by BellSouth,
6 that it does not foreclose parties taking issue with
7 the permanent rates in a 271 proceeding. I mean, it
8 doesn't foreclose it from coming up.

9 And with respect to the notion of putting it
10 off or granting you intervention, if we grant you
11 intervention, it's my view that we have to go back and
12 let everybody else in and that we'd have to postpone
13 this.

14 **MR. WELCH:** Commissioner Clark, I'm only
15 here today because Mr. Dunbar is in the hospital, and
16 I don't know much about the history of this
17 proceeding, but Ms. Marek, who is vice-president of
18 Time Warner and has been with this region for some
19 three and a half years now has been, and if you'd like
20 for her to comment on that, she's willing to do so.

21 **COMMISSIONER CLARK:** That would be fine. I
22 guess what I'm suggesting is that this is between the
23 parties, and you are not precluded the opportunity in
24 your own arbitration from disputing these and
25 providing your own information. You're not precluded

1 from relying what gets developed here if you like it.

2 If you don't like it, you can arbitrate your
3 own, and it will not preclude you if you choose to
4 participate in a 271 -- but I don't think you did
5 participate; I'm not sure -- from raising that issue.

6 **MR. WELCH:** Well, again, as I was -- in my
7 dialogue with Commissioner Jacobs, I just find it very
8 hard to believe that this Commission could in a week
9 or two or a month come back and hear much of the
10 same -- hear all of BellSouth's exact same evidence
11 and testimony and come to a different finding.

12 You will make a decision in this case. You
13 will hear BellSouth's evidence and their witnesses,
14 and they have a lot of it, and you will make a
15 decision.

16 **COMMISSIONER DEASON:** Let me ask a question.
17 What is the status of Time Warner's own arbitration
18 with BellSouth. Where does it stand at this point?

19 **MS. MAREK:** We have not arbitrated with
20 BellSouth. In fact, just from a resource perspective,
21 we've been trying not to arbitrate and trying to
22 negotiate. We negotiated prices, and then we opted
23 in, or we MFN'd into the unbundled network elements in
24 Florida so that we would not have to go through an
25 arbitration hoping that there would a generic

1 proceeding.

2 And to respond, Commissioner Clark, to your
3 point about the fact that we've had these arbitrations
4 going on from '95 and that this is a continuation, we
5 agree from the perspective -- and I think,
6 Commissioner --

7 **COMMISSIONER CLARK:** I think '96, not '95.

8 **MS. MAREK:** Right. I'm sorry; in '96.

9 Well, there was -- there was a proceeding in '95 that
10 we were part of that was looking at it before the
11 Telecommunications Act was enacted. But in any event,
12 their arbitration proceedings -- you had some
13 statutory guidelines or deadlines that you had to
14 meet, and we're -- and we agreed at that point in time
15 that it was not appropriate for the parties to be part
16 of that arbitration proceeding, that you had to set
17 some prices within some statutory deadlines.

18 So from that perspective, you all set
19 interim rates. Well, now we're looking at permanent
20 rates, and just from the perspective that this is
21 permanent, it connotes that it's going to be something
22 that's not changeable, that's going to be there in
23 place for some period of time.

24 **COMMISSIONER CLARK:** Through the
25 arbitrations.

1 **MS. MAREK:** Through the arbitrations,
2 correct.

3 **COMMISSIONER CLARK:** Were these part --

4 **MS. MAREK:** And typically in all of the
5 interim -- in all of the arbitrations that you all set
6 before, for those of us who were trying to avoid
7 arbitration, we adopted lot of those rates, those
8 interim rates. And all the other states in the
9 southeast region, there have been -- there has been a
10 generic -- where they've addressed the issue, they
11 have established a generic proceeding now to set the
12 permanent rates so that all parties could have an
13 opportunity to have their voice heard.

14 You have -- you're missing an element in
15 this arbitration right now where you're going to be
16 setting these rates, which we strongly believe are
17 going to set precedents.

18 What Mr. Welch was saying that you may say,
19 well, you know, you can -- you -- we'll do this
20 arbitration and then two weeks from now we'll hear
21 your arbitration, it's going to be the same
22 information except that we'll be presenting a
23 different voice that you potentially could have heard
24 today.

25 And if you set rates during this hearing,

1 and then two weeks later you have another arbitration
2 and you look at all the same data and you say, you
3 know, that was a good point; now we want to set a
4 different rate. You're going to have a conundrum here
5 where you're going to have to try and figure out now
6 which rates really do apply, because we have to set
7 nondiscriminatory rates with the Telecommunications
8 Act.

9 So, I mean, I really feel that from a
10 judicial economy standpoint, that this is a tremendous
11 waste of time. And I hate to be so blunt in saying
12 that, but you potentially could have this arbitration
13 proceeding this week, next week have them with Time
14 Warner, next one have them -- week have them with
15 ACSI, next week have them with ICI. You're going to
16 be looking at the exact same information from
17 BellSouth.

18 Wouldn't it be better to have all of the
19 parties present at a -- in a proceeding where the
20 rates are going to affect all parties?

21 **CHAIRMAN JOHNSON:** What if we did a generic
22 proceeding; would all of the individuals have to
23 participate?

24 **MR. WELCH:** No, ma'am.

25 **CHAIRMAN JOHNSON:** And if they did not

1 participate, are they bound by the permanent rates
2 that were established?

3 **MR. WELCH:** Yes, ma'am.

4 **CHAIRMAN JOHNSON:** Now, the federal act
5 would allow to us hold a proceeding and set rates and
6 then pretty much trump those parties that did not
7 participate?

8 **MR. WELCH:** So long as they had notice and
9 an opportunity to be heard, yes, ma'am.

10 And I would suggest to the Chairman that
11 from our experience in other states, that the parties
12 are very interested in this proceeding and they will
13 participate.

14 In fact, as I said earlier, in a lot of the
15 proceedings -- or not a lot of the proceedings, but
16 several proceedings that you would think would be of
17 great importance, and are, there are companies that
18 elect not to participate; universal service being an
19 example in Tennessee. But in this particular
20 proceeding every party has participated, at least in
21 Tennessee and, I think, elsewhere.

22 **COMMISSIONER DEASON:** What about a new
23 telephone company that starts business today? They're
24 bound by what we would do today if we allowed an open
25 intervention and they didn't even exist today? They

1 start business today or next week or a month from now.
2 Are they bound, or do they have the opportunity to
3 have their own arbitration?

4 I think they have the opportunity to have
5 their own arbitration under the law, do they not?
6 Then what do we do about discriminatory rates if we
7 find something different for them?

8 You see, this Act, this law, is not written
9 for judicial economy. You may argue that, and I agree
10 that it's a good concept, but it's not part of the
11 Act; and I think we're being consistent with the Act
12 when we deny you the intervention.

13 **MR. WELCH:** Well, this is certainly new to
14 all of us and has developed over the course of the
15 last couple years, and there's a lot of things that
16 I'm sure that will present -- that there'll be issues
17 that are presented that we can't foresee now, but I
18 don't think that that should stop us from doing what's
19 right today.

20 **MS. MAREK:** We also had two motions. We had
21 a motion to intervene, and we asked for
22 reconsideration -- (inaudible) --

23 **CHAIRMAN JOHNSON:** I can't really hear you.
24 Could you speak directly into --

25 **MS. MAREK:** We actually had two motions. We

1 had a motion for reconsideration, or in the
2 alternative, a motion to establish a generic
3 proceeding. And so if the -- if our motion for
4 intervention is denied -- and, quite frankly, at this
5 point in time, you know, to be allowed into the party
6 at this point, I don't have a witness, I don't have
7 the opportunity to do effective cross-examination.

8 So your point, you know, Madame Chairman,
9 was right on point. If we're allowed in today, it's
10 not really going to help me. But the motion to
11 establish a generic proceeding is one that I think all
12 parties have agreed to in all the other states and
13 would be a very effective way to conduct this in a
14 proper manner.

15 **COMMISSIONER DEASON:** Then would we be
16 somehow prejudicing the other parties who are prepared
17 and ready to go, wanting to get this settled and go on
18 and do business? What about their right?

19 **MR. WELCH:** I'm not -- we haven't heard from
20 them, but I'm not so sure they wouldn't agree with
21 this proposition.

22 Commissioner Clark brought up the BellSouth
23 271 application. I don't know how BellSouth could
24 proceed with that application without setting
25 permanent rates for everybody.

1 **MS. MAREK:** And there are interim rates
2 right now. I mean, you know, by having the
3 arbitration before and having you all set the interim
4 rates, they still can operate and be in business, so
5 they're still in business today.

6 But while you're setting permanent rates,
7 that's really where the time ought to be spent and why
8 we have argued not only in this jurisdiction, but in
9 North Carolina we had almost exactly the same
10 situation, and the Commission denied our intervention,
11 and then we filed for reconsideration and -- to have a
12 generic proceeding, and upon further reflection, they
13 did exactly that; and we're going through that
14 proceeding as we speak in North Carolina, identical
15 situation.

16 **CHAIRMAN JOHNSON:** Any other questions,
17 Commissioners? Staff?

18 **MR. PELLEGRINI:** Yes, I would have a couple
19 of points, I think, to make. The first is that what
20 is before us in these three days is merely a
21 continuation of the earlier phases of these
22 arbitration proceedings.

23 At that time the Commission drew a road map,
24 said that because for certain elements BellSouth's
25 cost studies were not adequate, it would set interim

1 rates which would be made permanent upon the filing of
2 cost studies.

3 Now those cost studies have been filed, and
4 here we are looking at how those interim rates should
5 be made permanent. So this is, really -- this
6 proceeding is really a continuum from the earlier
7 phase to the present phase.

8 The second point, I think probably a bit
9 more important even, after considerable deliberation
10 at a very early point in these arbitration
11 proceedings, the Commission determined that what the
12 Act required, what the congressional intent was, was
13 that requesting carriers and incumbent local exchange
14 companies would fully negotiate commercial
15 arrangements for interconnection; and if those
16 negotiations were to fail, then the parties could
17 bring their disputes to the state commissions for
18 resolution.

19 The contemplation was that the arbitration
20 decisions that the state commissions would make would
21 be binding upon those two parties and no one else;
22 therefore, intervention by third parties was improper.

23 Now, that was a position that this
24 Commission took, as I said, after considerable
25 deliberation at a very early point in this proceeding,

1 and it's a position which this Commission has upheld
2 with some consistency ever since.

3 **CHAIRMAN JOHNSON:** Mr. Pellegrini, let me
4 ask you a question. Do you believe, or do you agree
5 with Time Warner that if we decided we wanted to hold
6 a generic proceeding, that that would be binding upon
7 all of the existing carriers in our state? Or would
8 they still have the ability to negotiate and come up
9 with their own rates?

10 **MR. PELLEGRINI:** It would seem only fair
11 that if we were to conduct such a generic proceeding,
12 that it would be a condition of participation that
13 they be bound, but I think that's --

14 **CHAIRMAN JOHNSON:** So we would make them --
15 basically we're forcing them to participate, and if
16 they don't participate, they're bound, and if they do
17 participate they're bound.

18 **MR. PELLEGRINI:** It would seem illogical to
19 me to permit them to participate and then not be bound
20 by the outcome and be free to work their own deal one
21 way or another. But their participation, it just
22 seems to me, is essentially inconsistent with the
23 nature of these arbitration proceedings to this point.

24 **CHAIRMAN JOHNSON:** That's one of my
25 concerns, that the forced participation appears to be

1 contrary with the Act that allows for the negotiations
2 on a party-by-party basis. And for us to say, okay,
3 we're going to have one generic proceeding and you're
4 going to all be bound by these rates, that seems
5 contrary to the intent and purpose of what Congress
6 was trying to accomplish.

7 **MR. WELCH:** Well, I think if you just limit
8 your review of the Act to those sections that deal
9 with arbitration, you're right; but you have to look
10 at the entire Act and the intent of the Act, and one
11 of the most -- one of its most important provisions is
12 that this Commission set nondiscriminatory rates. And
13 to do that, I think it has to set rates for everybody
14 at the same rate at the same time.

15 **COMMISSIONER CLARK:** Well, to follow that,
16 it seems to me, to its logical conclusion is you
17 wouldn't do arbitration. You wouldn't allow
18 individual negotiations, because presumably you're
19 always going to have a different agreement. By its
20 very nature, what the Act has set up is somewhat
21 contradictory.

22 **MR. WELCH:** Yes, ma'am. There is certainly
23 some ambiguity there, but there are and there will
24 continue to be agreements between the providers that
25 look different. That's because there are different

1 kinds of providers, and they have a different mode of
2 operation and they need a different contract; and to
3 that extent they are free to negotiate and agree to
4 something different.

5 But we're talking about just the bottom line
6 here. I mean, these elements are the same for
7 everybody. They are elements that are necessary to do
8 business, and they have to be purchased by all of
9 these other providers and they need to be at the same
10 rate. The one thing -- excuse me. I'm sorry.

11 **COMMISSIONER JACOBS:** Let me just ask the
12 question. Again, going with the logic of your
13 argument, it would appear, then, that the rates will
14 become discriminatory if in some later proceeding a
15 party would be, for some reason, forced to accept
16 rates that are less favorable than we would conclude
17 in this proceeding.

18 Do you have a remedy in that event? Don't
19 you have a remedy in that event that you face
20 negotiations where you find BellSouth intractable and
21 unwilling to negotiate on the rates that resemble what
22 we come out of this proceeding with?

23 **MR. WELCH:** Yes, sir. I think we would have
24 an opportunity to elect the rates that came out of
25 this proceeding.

1 **COMMISSIONER JACOBS:** No, no. My question
2 is, in the event that you do not see that as an
3 acceptable -- or let me say this: In the event that
4 whatever your negotiated position is, when you sit
5 down with BellSouth, you do not see that you have a
6 reasonable opportunity to negotiate for your best
7 interests, whether it be what comes out of this
8 proceeding or whatever you want to select? Don't you
9 have a remedy at that point?

10 **MR. WELCH:** Well, I assume that,
11 Commissioner Jacobs, you're getting to the point that
12 I could come in and ask for an arbitration on those
13 rates, and certainly that's one way to do it.

14 It's going to take a lot of this
15 Commission's time, and the one thing I'd like to ask
16 the Commission is -- and I have seen BellSouth's proof
17 in this case, and I think at the very best, it takes
18 two or three days to put on. They have some 14
19 witnesses and some very complicated testimony and
20 evidence. And I just wonder if this Commission is
21 really going to go through that process every time
22 it's asked that -- a provider such as Time Warner asks
23 for an arbitration when they feel like they're not
24 getting the right rates.

25 **MS. MAREK:** This Commission has addressed

1 many different kinds of generic issues in the past,
2 whether it be universal service, whether it be
3 rulemakings, where those rules or those issues apply
4 to everybody when the Commission orders something.

5 If you have a generic proceeding in which
6 all parties that are certificated at the time are
7 allowed to participate, you're going to catch the
8 lion's share of positions that are out there.

9 Right now in this proceeding you have IXCs
10 participating and matching that against the incumbent
11 LEC. You really don't have the facilities-based
12 carriers like the ACSIs, like the Time Warners, like
13 the ICIs, that are a different voice from what you're
14 going to hear today.

15 So if you had a generic proceeding, at least
16 at this point in time you'd be capturing the lion's
17 share of positions that are out there. If another new
18 entrant now comes on board at some point down the road
19 and takes issue with the price that you all have set,
20 they're not precluded from doing an arbitration.
21 You're right about that.

22 However, it also would, at least for the
23 time being from a judicial economy standpoint, capture
24 a whole lot more folks than it would by having these
25 separate arbitrations one right after the other.

1 **CHAIRMAN JOHNSON:** Thank you?

2 Mr. Pellegrini, I'm sorry.

3 **MR. PELLEGRINI:** Chairman Johnson, just one
4 further point. It's been suggested that this
5 Commission's position regarding intervention is a
6 unique position at odds with the positions taken by
7 the other state commissions.

8 I'm not sure how relevant that is, that
9 argument is, that is with respect to what I said
10 earlier; but I did have a limited opportunity on
11 Friday afternoon to talk with some state commissions.

12 I did not find a uniformity of approach to
13 this problem at all. Missouri, for example, has
14 conducted its proceedings exactly in consonance with
15 our procedures. In fact, they denied a petition by
16 Sprint and United for a generic proceeding.

17 Arizona proceeds without third-party
18 intervenors, but then -- initially in arbitration
19 proceedings, but then conducts generic cost studies
20 which are limited to those parties participating in
21 the arbitrations; limited to those parties
22 participating in the arbitrations.

23 California has set interim rates in
24 arbitration proceedings without intervenors and then
25 has opened generic proceedings to establish permanent

1 rates; the interim rates, of course, being based upon
2 proxy, upon proxy values.

3 Louisiana and Colorado have permitted
4 intervention in consolidated proceedings.

5 The FCC in its First Report and Order at
6 Paragraph 1436, in the event that an arbitration
7 proceeding would default at the state level and the
8 FCC would conduct the proceeding, the FCC has said
9 this: "Finally, we reject the alternative of opening
10 the arbitration process to all third parties, which
11 would minimize the cost involved in such proceeding."
12 And the FCC has codified that position in its rules.

13 All I can say is that different people have
14 looked at the same language and arrived at different
15 conclusions, all of which may be very rational and
16 supportable, but no more or no less than this
17 Commission's interpretation.

18 **COMMISSIONER DEASON:** Well, it seems to me
19 that this Commission has tried to allow for judicial
20 economy whenever it was appropriate. We allowed, for
21 hearing purposes, MCI and AT&T to basically have
22 concurrent hearings, but they had their own positions.
23 Sometimes they agreed, sometimes they differed. But
24 for hearing purposes, we went through that process,
25 but we came out with two different orders and two

1 different results based upon the evidence of the
2 record.

3 I would submit that if Time Warner's
4 arbitration was at the same point that we are with MCI
5 and AT&T and other parties in this docket, they could
6 even be incorporated right in and we could accomplish
7 some judicial economy; but we're not there. For
8 whatever reason, they've chosen not to go this course,
9 but they want to get involved at this, the last
10 minute, and basically defer everything for everyone
11 else who is prepared and ready to go forward.

12 I don't think that's the appropriate way to
13 go, and I move on reconsideration that we again deny
14 the intervention of Time Warner.

15 **MR. MELSON:** Commissioner Johnson, if I
16 could just clarify one thing I think Commissioner
17 Deason possibly misstated.

18 We did have a consolidated hearing on the
19 MCI and AT&T arbitrations, the initial decisions at
20 least. The initial decisions of the initial
21 reconsideration were done on a consolidated basis and
22 one result for both companies.

23 It was only when we went off and drafted
24 particular contracts that it then turned into separate
25 orders. I just wanted the record to be clear.

1 **COMMISSIONER DEASON:** I appreciate that.
2 But the final decisions were not 100% the same for
3 each company.

4 **MR. MELSON:** I believe the final contracts
5 were not 100% the same. I cannot recall offhand any
6 arbitrated decision that was different.

7 **COMMISSIONER DEASON:** But they were two
8 separate arbitrations which were just heard at the
9 same time, and two different orders were entered; and
10 maybe the results were the same. But two different
11 orders were entered, were they not?

12 **MR. MELSON:** The initial final order in the
13 case was a single order that applied to both. The
14 order on reconsideration was a single order that
15 applied to both and directed us then to file our
16 contracts. It was only at the contract approval stage
17 that there were separate orders for AT&T and MCI.

18 **COMMISSIONER DEASON:** Thank you.

19 **COMMISSIONER CLARK:** Second.

20 **CHAIRMAN JOHNSON:** There's a motion and a
21 second. Any further discussion? Seeing none, all
22 those in favor signify by saying aye?

23 **COMMISSIONER DEASON:** Aye.

24 **COMMISSIONER CLARK:** Aye.

25 **COMMISSIONER GARCIA:** Aye.

1 **COMMISSIONER JACOBS:** Aye.

2 **CHAIRMAN JOHNSON:** Aye. Opposed? (No
3 response.) Show that, then, approved unanimously.

4 **COMMISSIONER CLARK:** Madam Chair, I would
5 simply point out it doesn't preclude you from asking
6 for a generic proceeding if you still think that's the
7 way to go in making your case.

8 **MR. WELCH:** Commissioner Clark, I think that
9 that was part of our motion that we were here on
10 today, and I think that's a good point, and I think
11 the Commission should do that.

12 **COMMISSIONER CLARK:** Well, the motion is
13 denied. If you choose to do it again, suggesting a
14 generic proceeding, I think you can, if you choose to
15 do that.

16 **MR. WELCH:** Thank you for the opportunity.

17 **CHAIRMAN JOHNSON:** Thank you. Any other
18 preliminary matters? Mr. Pellegrini?

19 **MR. PELLEGRINI:** Yes. Chairman Johnson, I
20 want to announce at this point that there are three
21 witnesses whose testimony and exhibits will be entered
22 into the record by stipulation.

23 These are BellSouth's Witness Dr. Randall
24 Billingsley, AT&T and MCI Witness Dr. Bradford
25 Cornell, and AT&T/MCI Witness Michael J. Majoros, Jr.

1 Dr. Billingsley's testimony will be entered with
2 updates to Exhibits RSB-6, 8 and 9, and Dr. Cornell's
3 exhibits will be -- Exhibit BC-3 will reflect an
4 update as well.

5 **CHAIRMAN JOHNSON:** Okay. Should we take
6 care of those now, or just in the order in which they
7 would originally come before us?

8 **MR. PELLEGRINI:** I think this would be an
9 appropriate time to take care of getting the testimony
10 and exhibits. If there's a problem with that, we'll
11 do it at a later time.

12 **CHAIRMAN JOHNSON:** We'll just handle them --

13 **COMMISSIONER CLARK:** Who were the three
14 witnesses? I've got Billingsley and Cornell, but I --

15 **MR. PELLEGRINI:** Dr. Billingsley,
16 Dr. Cornell, and Mr. Majoros.

17 **CHAIRMAN JOHNSON:** I'll note that, and then
18 when we get to those particular witnesses, we'll take
19 care of it at that time.

20 **MR. PELLEGRINI:** Yes.

21 **CHAIRMAN JOHNSON:** Any other preliminary
22 matters?

23 **MR. PELLEGRINI:** At this time Staff would
24 like to take official -- would like the Commission to
25 take official recognition of a number of documents,

1 and we're going to distribute a list of those
2 documents to the Commissioners and to the parties at
3 this time, and I would ask that it be marked as
4 Exhibit 1 for identification.

5 **CHAIRMAN JOHNSON:** You'd like for the
6 official recognition list to be marked as Exhibit 1?

7 **MR. PELLEGRINI:** Yes.

8 **CHAIRMAN JOHNSON:** It will be marked as
9 Staff Exhibit 1.

10 (Exhibit 1 marked for identification.)

11 **MR. PELLEGRINI:** Also, as the result of an
12 order issued the 22nd of January, the parties are
13 prepared to strike certain testimony relating to
14 operations support systems.

15 **CHAIRMAN JOHNSON:** Mr. Pellegrini, could we
16 go back to the exhibit that I marked as Exhibit 1?

17 **MR. PELLEGRINI:** Yes. I'm sorry.

18 **CHAIRMAN JOHNSON:** Would you like for me to
19 take official recognition of all these documents at
20 this time?

21 **MR. PELLEGRINI:** Yes.

22 **CHAIRMAN JOHNSON:** And the parties have a
23 copy and have had an opportunity to review the
24 documents upon which I'm going to take official
25 recognition? Okay. Seeing no objection, I'll take

1 official recognition of the documents listed in
2 Exhibit 1.

3 **MR. PELLEGRINI:** Thank you. As I started to
4 say, as a result of an order issued on the 22nd of
5 this month, the parties are prepared to strike certain
6 testimony relating to operations support systems at
7 the time the sponsored witnesses are called to
8 testify. I just want to alert the Commissioners that
9 that's going to happen.

10 **CHAIRMAN JOHNSON:** Thank you.

11 **MR. LACKEY:** Madam Chairman, that is not
12 precisely correct. We are prepared, for instance with
13 Mr. Varner, to strike out of his direct testimony --
14 MCI has told me what they're striking out of their
15 testimony. AT&T has not yet. So I'm not prepared to
16 strike out of the rebuttal testimony yet, and as I
17 understand it, we're putting both the direct and the
18 rebuttal up at one time.

19 So when Mr. Varner gets up on the stand,
20 hopefully in a very few minutes, he will be prepared
21 to strike out of his direct. He will not be prepared
22 to strike out of his rebuttal at this point.

23 I don't know what to do about it, but until
24 I see what they're taking out of theirs, I don't know
25 what to take out of his.

1 **COMMISSIONER CLARK:** It seems like somebody
2 has got to take the white paper from Mr. Selwyn. I
3 thought that was the response to the rebuttal.

4 **MR. LACKEY:** Well, the problem, as I
5 understand it, is that AT&T is not prepared to strike
6 the entire white paper of Dr. Selwyn. They're going
7 to edit or strike parts of it, and I can't strike out
8 of Varner's testimony until I know what they're going
9 to do about it.

10 **MR. HATCH:** Madam Chairman, as you will
11 recall, we were asked to do that, to be ready at the
12 beginning of the hearing. I have endeavored to do
13 that. The problem is, is tracking down my witnesses
14 to confirm those portions that I think need to be
15 stricken. I have not been able to do that.

16 Mr. Selwyn came in late last night, and he
17 is working to go through all of that to confirm what
18 exactly it is that should be stricken; and it is
19 particularly complicated with respect to Mr. Selwyn's
20 white paper.

21 I don't think there's a problem with
22 Mr. Lynott, and I'm prepared to do that tomorrow.
23 Mr. Lynott is coming to town this evening. I was
24 going to confirm what I think is correct with him and
25 do that certainly before they take the stand. I

1 understand the conundrum that this creates. I don't
2 have a particular answer for it.

3 **COMMISSIONER CLARK:** Is it only Mr. Varner's
4 testimony that has the problem?

5 **MR. LACKEY:** (Inaudible)

6 **CHAIRMAN JOHNSON:** I'm sorry. Your
7 microphone isn't on.

8 **MR. LACKEY:** I'm sorry. I think that
9 Mr. Varner is the only one I know I have the problem
10 with right this instant. There's no problem with
11 Caldwell and Zarakas, and they're the next set of
12 witness after Mr. Varner.

13 **COMMISSIONER CLARK:** Madam Chair, if I could
14 make a suggestion, I think it begins, the possible
15 testimony to be stricken in the rebuttal testimony is
16 everything from Page 24 -- well, it is perhaps
17 everything from Page 24 to the end of the testimony.
18 I'm not sure.

19 I guess what we might do is leave it in and
20 then go back and strike it, but he wouldn't summarize
21 that.

22 **MR. LACKEY:** We filed a letter on the 23rd
23 laying out the pages we thought should be stricken,
24 and I have an exhibit that lays them out, too. I'm
25 just concerned about striking it all and then finding

1 out tomorrow that I struck something that responded to
2 something that's still in the testimony.

3 That's just my concern. But as far as I'm
4 concerned, what we can do is go ahead and let him
5 summarize his testimony. I don't think his summary
6 addresses that part of the rebuttal anyway. And then
7 sort out the bodies later once we know what everybody
8 is going to do. I don't know what else to do.

9 **CHAIRMAN JOHNSON:** That will work for us.

10 **MR. HATCH:** That would be my suggestion as
11 well. We'll just have to wait and see how it works
12 out, once I'm done with Mr. Selwyn, trying to figure
13 out what we can and cannot remove without just
14 eviscerating the entire document; and that's probably
15 not appropriate either, at least at this point.

16 **CHAIRMAN JOHNSON:** Okay. Any other
17 preliminary matters?

18 **MR. PELLEGRINI:** Yes. At this time with the
19 agreement of the parties, Staff would proffer six
20 exhibits containing discovery responses for
21 identification. I think it might be appropriate for
22 me to identify these each one at a time.

23 The first is identified as Stip-1, and it
24 contains BellSouth responses to WorldCom's First and
25 Second Set of Interrogatories.

1 **CHAIRMAN JOHNSON:** Mr. Pellegrini, is this
2 something that we, the Commissioners, have?

3 **MR. PELLEGRINI:** Yes. These are being
4 distributed to you at the moment. The first of these
5 is identified as Stip-1, and it contains BellSouth
6 responses to WorldCom's First and Second Set of
7 Interrogatories, and I would ask that it be marked as
8 Exhibit No. 2 for identification purposes.

9 **CHAIRMAN JOHNSON:** It will be marked as
10 Exhibit 2.

11 **MR. PELLEGRINI:** Yes.

12 (Exhibit 2 marked for identification.)

13 **CHAIRMAN JOHNSON:** And identified as Staff
14 Stip-1.

15 **MR. PELLEGRINI:** The second of these is
16 identified as Stip-2. It contains BellSouth's
17 responses to AT&T's Second and Third Set of
18 Interrogatories, and I would ask that it be identified
19 as Exhibit 3 for identification purposes.

20 **CHAIRMAN JOHNSON:** It will be identified as
21 Exhibit 3.

22 **MR. PELLEGRINI:** 3, yes.

23 **CHAIRMAN JOHNSON:** And it will be marked as
24 3 and identified as Staff's Stip-2.

25 (Exhibit 3 marked for identification.)

1 **MR. PELLEGRINI:** The third of these is
2 identified as Stip-3. It contains BellSouth's
3 responses to Staff's Third, Fourth, Fifth, Sixth,
4 Seventh and Eighth Set of Interrogatories, and I would
5 ask that it be marked as Exhibit 4 for identification
6 purposes.

7 **CHAIRMAN JOHNSON:** It will be marked 4, and
8 the short title is Staff Stip-3.

9 (Exhibit 4 marked for identification.)

10 **MR. PELLEGRINI:** Stip-3.

11 **CHAIRMAN JOHNSON:** Yes.

12 **MR. PELLEGRINI:** The next is identified as
13 Stip-4, and it contains BellSouth's responses to
14 Staff's Third and Fourth and Fifth Sets of Production
15 of Documents, and I would ask that it be marked as
16 Exhibit 5 for identification purposes.

17 **CHAIRMAN JOHNSON:** It will be marked as 5,
18 and the short title is Staff Stip-4.

19 (Exhibit 5 marked for identification.)

20 **MR. PELLEGRINI:** And the fifth is identified
21 as Stip-5. The fifth is identified as Stip-5, and it
22 contains responses to AT&T's responses to Staff's
23 Second Set of Interrogatories, Staff's First Set of
24 Production of Documents, which are too voluminous to
25 copy, and responses to Staff's Second Set of

1 Production of Documents, and I would ask that it be
2 marked as Exhibit 5 -- 6 for identification purposes.

3 **CHAIRMAN JOHNSON:** It will be marked as 6
4 and identified as Staff's Stip-5.

5 (Exhibit 6 marked for identification.)

6 **MR. PELLEGRINI:** And last, the last one is
7 identified as Stip-6, and it contains MCI's responses
8 to Staff's First Set of Interrogatories, and I would
9 ask that it be marked as Exhibit 7.

10 **CHAIRMAN JOHNSON:** It will be marked as 7
11 and identified as Staff's Stip-6.

12 (Exhibit 7 marked for identification.)

13 **MR. PELLEGRINI:** Just one additional point,
14 Chairman Johnson. Staff would suggest that it would
15 be expedient if you were to impose limitations on the
16 witnesses' summary of their testimonies in view of the
17 short time schedule available for this hearing; and we
18 would suggest five or 10 minutes, something in that
19 range.

20 **CHAIRMAN JOHNSON:** For the summaries?

21 **MR. PELLEGRINI:** For the testimony
22 summaries, yes.

23 **CHAIRMAN JOHNSON:** Well, I will caution all
24 of the witnesses that you be brief in providing your
25 summaries, and to the extent that you appear to need

1 more than five minutes, let me know, and then we'll
2 make a decision at that time; but I don't expect any
3 witnesses will summarize for more than that.

4 **MR. PELLEGRINI:** And, finally, just to alert
5 everyone, it's Staff's intention to submit exhibits
6 relevant to each of the witnesses to be marked at the
7 time that the witnesses themselves are offered for
8 cross-examination so that those exhibits will be
9 available to all of the parties in cross-examination.

10 **CHAIRMAN JOHNSON:** Okay.

11 **MR. PELLEGRINI:** And I think that clears all
12 of the preliminary matters that I have.

13 **CHAIRMAN JOHNSON:** Are there some other
14 preliminary matters?

15 **MR. LACKEY:** Actually, I need to address two
16 things that just happened, if I could, just to make
17 sure the record is clear. First, Mr. Varner will
18 endeavor to keep his summary short. I think it may
19 run a little bit more than five minutes. Sometimes he
20 just can't help himself.

21 **CHAIRMAN JOHNSON:** I was looking at him when
22 I made that comment.

23 **MR. LACKEY:** Well, I went through his
24 summary last night and I cut out whole paragraphs, so
25 we're trying to make some progress on that.

1 The other thing that I want to address is
2 Exhibit No. 5, which was Staff Stipulation-4, and
3 specifically the description of Item No. 1, which is
4 responses to Staff's Third Set of Production of
5 Documents, and I specifically want to talk about
6 Item 41 and 42.

7 Those were the items that we had the motion
8 hearing over, and I think that what Mr. Pellegrini
9 intends to include are 10, approximately 10, pages out
10 of that that we actually furnished to Staff with
11 copies of, four of which are proprietary and for which
12 we have already filed a notice of intent to request --
13 specify confidential classification.

14 Those are pages out of the BellSouth
15 Telecommunications debt rating manual books, which are
16 the books that we take to New York to discuss with the
17 bond analysts our situation. So it's just those 10
18 pages. I wanted to make that clear on the record, so
19 I could cut off the corporate heart attack in Atlanta,
20 if that would be all right.

21 **CHAIRMAN JOHNSON:** Okay. Thank you. Any
22 other preliminary matters?

23 **MR. PELLEGRINI:** What Mr. Lackey says is
24 correct, and I would point out that some of those
25 pages are confidential and included in the packet that

1 is being distributed to the Commissioners at the
2 moment. And I think that that is an additional
3 preliminary matter; that I would offer the
4 confidential exhibits as a consolidated exhibit and
5 would like to describe what the packet contains.

6 It contains AT&T testimony of witnesses
7 Wells, Petzinger and Bissell, Exhibits P-1 attached to
8 Witness Caldwell's -- BellSouth Witness Caldwell's
9 testimony.

10 **CHAIRMAN JOHNSON:** I'm sorry,
11 Mr. Pellegrini. You've lost me. What are we doing
12 now?

13 **MR. PELLEGRINI:** I'm taking about that
14 packet. I want to introduce that as an exhibit.

15 **CHAIRMAN JOHNSON:** And you want it to be,
16 you said, a composite?

17 **MR. PELLEGRINI:** As a consolidated exhibit.

18 **CHAIRMAN JOHNSON:** Okay. This should be a
19 composite exhibit.

20 **MR. PELLEGRINI:** A composite exhibit. And I
21 was simply describing its contents.

22 **CHAIRMAN JOHNSON:** Okay.

23 **MR. PELLEGRINI:** AT&T testimony of Witnesses
24 Wells, Petzinger and Bissell; Exhibit P-1 of Witness
25 Caldwell's testimony; BellSouth's Stipulation Con-2,

1 BellSouth's Stipulation Con-1; portions of AT&T
2 Witness Wells' deposition transcript, and portions of
3 AT&T Witnesses Klick and Bissell, the deposition
4 transcripts.

5 **CHAIRMAN JOHNSON:** Okay. Thank you for that
6 delineation. It will be marked as Composite
7 Exhibit 8, and the short title will be Staff's
8 Composite Exhibit, confidential, of 960833.

9 (Exhibit 8 marked for identification.)

10 **MS. WHITE:** May I ask for some clarification
11 from Mr. Pellegrini? A couple of those you listed in
12 there, Stipulation Con-1 and 2, can you show me what
13 that is?

14 **MR. PELLEGRINI:** Stip Con-2 relates to
15 interrogatories, and Stip Con-1 relates to production
16 of documents requested --

17 **MS. WHITE:** Oh. Is it part of these that
18 we've already made exhibits? It is?

19 **MR. PELLEGRINI:** Yes.

20 **MS. WHITE:** Okay. Thank you.

21 **MR. PELLEGRINI:** All right.

22 **CHAIRMAN JOHNSON:** Is that it? Any other
23 preliminary matters?

24 **MR. SELF:** Madam Chairman, I have a very
25 brief error in the prehearing order on Page 6 under

1 the witnesses. There's a footnote there for David
2 Porter, WorldCom's witness, and the footnote indicates
3 that he's only available on the third day.

4 I believe that footnote applies to somebody
5 else. Mr. Porter will be here later this afternoon,
6 and I anticipate he will come up by tomorrow. But
7 that footnote is not true for him. It may be true for
8 one of the other parties.

9 **CHAIRMAN JOHNSON:** Okay. Is there a witness
10 who is available only on January 28th, Mr. Melson?

11 **MR. MELSON:** Mr. Wood is available only on
12 the third day of the hearing, yes.

13 **CHAIRMAN JOHNSON:** Mr. Wood?

14 **MR. MELSON:** Yes, ma'am. He's the next to
15 the last witness listed, so I don't think that's going
16 to be much of a problem.

17 **MR. HATCH:** Speaking of footnotes, in the
18 witness order on Page 7 where it has a footnote with
19 respect to Katherine Petzinger, I think that should
20 apply to Mr. Wells. He is available only tomorrow, on
21 the second day.

22 In addition, Ms. Petzinger is now available
23 only on the third day, but she's way back in the
24 lineup, so I don't anticipate that to be any kind of a
25 problem.

1 **CHAIRMAN JOHNSON:** Okay.

2 **MR. PELLEGRINI:** I'd like to be clear now.
3 Witness Wood is available on the second day? Third
4 day?

5 **MR. MELSON:** No; only on the third day.

6 **MR. PELLEGRINI:** Witness Wells on the second
7 day?

8 **MR. HATCH:** That's correct.

9 **MR. PELLEGRINI:** And Witness Petzinger on
10 the third day?

11 **MR. MELSON:** That's correct.

12 **CHAIRMAN JOHNSON:** Any other corrections or
13 preliminary matters?

14 **MR. HATCH:** One more minor preliminary
15 matter, Madam Chairman. James Lemmer, who I entered
16 an appearance for earlier, is in-house counsel for
17 AT&T out of Atlanta. I would request that with
18 respect to Mr. Lemmer, that he be admitted to practice
19 before the Commission for the limited purpose of
20 participation in this hearing. Mr. Lemmer is a member
21 of the Colorado as well as the D.C. Bars.

22 **CHAIRMAN JOHNSON:** What was his last name
23 again?

24 **MR. HATCH:** Lemmer, L-E-M-M-E-R.

25 **CHAIRMAN JOHNSON:** Thank you. Any other

1 preliminary matters? Mr. Lackey?

2 **MR. LACKEY:** Yes, ma'am. I don't think this
3 is going to be an issue, but two of my nine or 10
4 witnesses, Mr. Smith and Mr. Garfield, won't be here
5 until in the morning.

6 **MR. SMITH:** Mr. Smith had a medical problem and couldn't
7 be here until tomorrow. Mr. Garfield works for
8 Bellcore, and tomorrow was the first day I could get
9 him. I don't think that's going to be a problem,
10 given the prior course of hearings like this. We
11 probably won't get to them anyway, but I did want to
12 mention that.

13 **CHAIRMAN JOHNSON:** We'll note that. Any
14 other preliminary matters?

15 **MR. PELLEGRINI:** No, Chairman; no.

16 **CHAIRMAN JOHNSON:** Okay. Those witnesses
17 that are present, if you could stand, I'll go ahead
18 and swear you all in at this time. If you could raise
19 your right hand.

20 (Witnesses collectively sworn.)

21 **CHAIRMAN JOHNSON:** At this time, then, we're
22 prepared for our first witness.

23 **MR. LACKEY:** We call Mr. Varner to the
24 stand, admonishing him as he walks up, to answer yes
25 and no and keep his summary to less than 10 minutes.

ALPHONSO J. VARNER

1
2 was called as a witness on behalf of BellSouth
3 Telecommunications, Inc. and, having been duly sworn,
4 testified as follows:

DIRECT EXAMINATION

5
6 **BY MR. LACKEY:**

7 Q Would you please state your name and address
8 for the record?

9 A My name is Alphonso Varner. My business
10 address is 675 West Peachtree Street in Atlanta,
11 Georgia.

12 Q By whom are you employed, Mr. Varner?

13 A BellSouth Telecommunications.

14 Q Mr. Varner, have you caused to be prefiled
15 in this proceeding 37 pages of direct testimony?

16 A Yes.

17 Q And was that direct testimony revised on
18 December 19th, 1997, with copies furnished to all the
19 parties?

20 A Yes.

21 Q Attached to that testimony, were there two
22 exhibits, AJV-1 and AJV-2?

23 A Yes.

24 Q Now, pursuant to the Commission's order
25 regarding the testimony on OSS, have you prepared a

1 document which indicates which portion of your direct
2 testimony is being stricken in this proceeding?

3 A Yes, I have.

4 MR. LACKEY: Madam Chairman, we have
5 furnished the Commissioners and all the parties with
6 this one-page item which deletes the pages that are
7 related both to Issue No. 2, which was removed from
8 this proceeding after the testimony was filed, and all
9 of the testimony related to the OSS issues that we
10 discussed early.

11 Q (By Mr. Lackey) Does that document which
12 has been handed out to the parties reflect the pages
13 which you believe should be removed from your
14 testimony, Mr. Varner?

15 A Yes.

16 Q With the corrections reflected -- I'm sorry.
17 Do you have any additional corrections to make to your
18 testimony or remaining exhibit?

19 A Yes. The Exhibit AJV-2 should also be
20 withdrawn. It is on the list.

21 Q That's reflected on this list, isn't it?

22 A Yes, it is.

23 Q All right. With those corrections, are
24 there any other corrections or changes in your direct
25 testimony?

1 A No.

2 Q If I were to ask you the questions that
3 appear in your direct testimony today, would your
4 answers be the same?

5 A Yes.

6 **MR. LACKEY:** Madam Chairman, I would like to
7 have the direct testimony of Mr. Varner, modified as
8 just described, included in the record as if given
9 orally from the stand.

10 **CHAIRMAN JOHNSON:** It will be so modified
11 and inserted into the record as though read.

12 **MR. LACKEY:** And I would like to have Varner
13 Exhibit AJV-1 marked with -- I guess we're doing it
14 sequentially -- the next exhibit number.

15 **CHAIRMAN JOHNSON:** It's 9. We'll mark it as
16 Exhibit 9 and identify it as AJV-1.

17 (Exhibit 9 marked for identification.)

18 **MR. LACKEY:** Thank you, ma'am.

19 Q **(By Mr. Lackey)** Now let's turn to your
20 rebuttal testimony, Mr. Varner. Did you cause to be
21 prefiled in this proceeding 28 pages of rebuttal
22 testimony?

23 A Yes.

24 Q And you were present during my earlier
25 comments to the Chair about striking portions of that

1 rebuttal testimony, weren't you?

2 A Yes.

3 Q Other than that issue, that issue of what
4 testimony should be removed, if any, do you have any
5 other changes or corrections to your rebuttal
6 testimony?

7 A No.

8 Q If I were to ask you the same questions that
9 appear in your rebuttal testimony, would your answers
10 be the same?

11 A Yes.

12 **MR. LACKEY:** Madam Chairman, I would like to
13 have the rebuttal testimony inserted in the record as
14 if given from the stand, subject, of course, to the
15 motion to strike that we'll have to resolve at some
16 point.

17 **CHAIRMAN JOHNSON:** It will be so inserted.

18

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25

1 BELLSOUTH TELECOMMUNICATIONS, INC.
2 DIRECT TESTIMONY OF ALPHONSO J. VARNER
3 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
4 DOCKET NOS. 960833-TP, 960846-TP, 960757-TP, 971140-TP
5 NOVEMBER 13, 1997
6

7 Q. PLEASE STATE YOUR NAME, AND BUSINESS NAME AND ADDRESS.
8

9 A. My name is Alphonso J. Varner. I am employed by BellSouth
10 Telecommunications, Inc. ("BellSouth") as Senior Director for State
11 Regulatory for the nine state BellSouth region. My business address is 675
12 West Peachtree Street, Atlanta, Georgia 30375.
13

14 Q. PLEASE GIVE A BRIEF DESCRIPTION OF YOUR BACKGROUND AND
15 EXPERIENCE.
16

17 A. I graduated from Florida State University in 1972 with a Bachelor of
18 Engineering Science degree in systems design engineering. I immediately
19 joined Southern Bell in the division of revenues organization with the
20 responsibility for preparation of all Florida investment separations studies for
21 division of revenues and for reviewing interstate settlements.
22

23 Subsequently, I accepted an assignment in the rates and tariffs organization
24 with responsibilities for administering selected rates and tariffs including
25 preparation of tariff filings. In January 1994, I was appointed Senior Director

1 of Pricing for the nine state region. I was named Senior Director for
2 Regulatory Policy and Planning in August 1994, and I accepted my current
3 position as Senior Director of Regulatory in April 1997.

4
5 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

6
7 A. My testimony addresses the policy issues related to the cost studies and price
8 development for unbundled network elements ("UNEs") and interconnection
9 that BellSouth offers to Alternative Local Exchange Companies ("ALECs").
10 In addition, I will address the recurring and non-recurring rates that BellSouth
11 proposes the Florida Public Service Commission ("Commission") adopt in this
12 docket for those UNEs listed in Issue 1, as follows:

- 13
14 (a) Network Interface Device
15 (b) 2 wire/4-wire Loop Distribution
16 (c) Virtual Collocation
17 (d) Physical Collocation
18 (e) Directory Assistance (Directory Transport - DS1 only)
19 (f) Dedicated Transport (Non-recurring only)
20 (g) 4-wire Analog Port
21 (h) 2-wire ADSL-compatible Loop
22 (i) 2-wire/4-wire HDSL-compatible Loop

23
24 ~~Finally, I will discuss BellSouth's interpretation of the appropriate non-~~
25 ~~recurring charge for each of the following "combinations of network elements"~~

1 for migration of an existing BellSouth customer," listed as Issue 2 in this
2 docket:

- 3 (a) 2-wire analog loop and port;
4 (b) 2-wire ISDN loop and port;
5 (c) 4-wire analog loop and port; and
6 (d) 4-wire DS1 and port.

7
8 The rates BellSouth proposes are supported by the cost studies sponsored by
9 Ms. Daonne Caldwell and others in their testimony. My testimony discusses
10 the following specific areas: 1) the rates that are being proposed and their
11 application, and 2) the relationship between BellSouth's cost studies and the
12 rates and rate application.

13
14 Q. PLEASE IDENTIFY THE OTHER BELLSOUTH WITNESSES FILING
15 DIRECT TESTIMONY AND BRIEFLY DESCRIBE THE PURPOSE OF
16 THEIR TESTIMONY.

17
18 A. Other BellSouth witnesses filing testimony in this proceeding are Ms. Daonne
19 Caldwell, Mr. William Zarakas, Mr. David Garfield, Mr. Dan Baeza, Mr. Eno
20 Landry, Mr. Walter Reid and Mr. Ellis Smith. Ms. Caldwell and Mr. Zarakas
21 jointly present BellSouth's cost methodology and the results of its cost studies.
22 Mr. David Garfield, with Bell Communications Research, Inc. ("BellCore")
23 provides an overview of BellCore's Switching Cost Information System that is
24 used to determine central office switching investment. Mr. Baeza discusses the
25 appropriateness of the network design used in BellSouth's cost studies. Mr.

1 Reid presents the appropriate methodology for including forward-looking
2 shared and common costs in BellSouth's studies. Mr. Smith discusses
3 statistical sampling and the specific loop sample used in BellSouth's loop
4 studies. Mr. Landry discusses BellSouth's provisioning process as it relates to
5 unbundled network elements.

6
7 Q. BRIEFLY OUTLINE THE EVENTS THAT LED TO THIS PROCEEDING.

8
9 A. Following the passage of the Telecommunications Act of 1996 ("the Act"),
10 BellSouth negotiated in good faith with a number of potential local service
11 providers. Many of those negotiations were successfully concluded with the
12 signing of interconnection agreements between the parties. As of October 30,
13 1997 BellSouth has signed approximately 240 interconnection and/or resale
14 agreements with a variety of companies in BellSouth, with approximately 130
15 applicable to Florida. For AT&T, MCI, ACSI, MFS and Sprint, the
16 negotiations resulted in petitions for arbitration. Specifically, the Commission
17 arbitrated issues between BellSouth and these companies and issued orders.

18
19 In the arbitration proceedings, the Commission ordered prices for UNEs and
20 interconnection to be based on BellSouth's Total Service Long Run
21 Incremental Cost ("TSLRIC") studies. The Commission set permanent rates,
22 with the exception of those functions for which BellSouth did not provide a
23 TSLRIC study. In those instances, the Commission set interim rates based on
24 either the Hatfield study results with modifications or BellSouth's tariff. The
25 Commission found that TSLRIC is the "appropriate costing methodology" and

1 ordered BellSouth to file TSLRIC cost studies for those rates for which interim
2 rates were set. (December 31, 1996 Final Order on Arbitration for
3 consolidated Docket Nos. 960833-TP (AT&T), 960846-TP (MCI) and 960916-
4 TP (ACSI), at page 33. Hereinafter, this Order will be referred to as the
5 "December 31, 1996 Arbitration Order.") Today, BellSouth is filing revised
6 TSLRIC studies, as well as TSLRIC plus shared and common costs, for the
7 items listed under Commission Issue No. 1. Additionally, BellSouth is filing
8 the residual recovery requirement ("RRR") for Issues 1(g), 1(h), and 1(i); ~~and~~
9 ~~the non-recurring costs associated with operational support systems ("OSS")~~
10 ~~recovery.~~

11
12 ~~Finally, BellSouth is filing cost studies for the non-recurring portion for the~~
13 ~~combinations listed under Issue No. 2. This is in response to the~~
14 ~~Commission's March 19, 1997 Final Order on Motions for Reconsideration, in~~
15 ~~which BellSouth was ordered to provide non-recurring charges that do not~~
16 ~~include duplicate charges or charges for functions or activities that AT&T and~~
17 ~~MCI do not need when two or more network elements are combined in a single~~
18 ~~order. The proposed rates based on these cost studies will be explained in~~
19 ~~more detail later in the testimony.~~

20
21 Q. HOW WILL PRICES SET IN THIS PROCEEDING AFFECT THE
22 DEVELOPMENT OF LOCAL COMPETITION?

23
24 A. In order to create an environment in which efficient competition will occur and
25 provide the maximum benefit to consumers, local competition must be

1 implemented in a fair and balanced manner. The Act provides for such an
2 environment. There are no provisions of the Act that, on their face, are
3 intended to advantage or disadvantage any provider or group of providers.
4

5 Since cost provides the basis for prices, it is extremely important that costs be
6 developed and set fairly. If costs result in prices being set either too high or
7 too low, the development of efficient competition in the local market will not
8 be encouraged as intended by Congress. Prices that are set either too high or
9 too low will, in the long run, not benefit the consumer. Prices must be set to
10 cover, at a minimum, the actual costs incurred by the Local Exchange
11 Company ("LEC"). Prices must also allow the LEC to recover incremental
12 costs and historical costs plus a reasonable allocation of its joint and common
13 costs.
14

15 Setting prices too low would discourage an ALEC from building its own
16 facilities even when that would be the correct economic decision. No other
17 company would be able to provide its own network any cheaper than it would
18 be able to obtain access to the existing one. Setting prices that only cover
19 incremental cost, i.e., not compensating the LEC for a portion of its shared,
20 common and historical costs, would enable an ALEC to avoid making any
21 capital investment and incurring all the related costs. It would make no
22 economic sense for the ALEC to build facilities. In other words, there would
23 still be no competition for the infrastructure. In addition, such uneconomic
24 pricing may also discourage entry into the market by those ALECs who
25 initially intend to resell BellSouth's retail services until they establish a

1 customer base that is sufficient to produce and support the capital necessary to
2 build facilities.

3

4 Moreover, costs/prices must be established that enable the incumbent LEC to
5 be compensated adequately for the use of its ubiquitous network. BellSouth
6 should receive just compensation for its services. A portion of all of the costs
7 of doing business must be included in such compensation. Setting prices for
8 unbundled network elements and interconnection at incremental cost would
9 force other services to absorb the other related costs. ALECs, as well as end-
10 users, benefit from the facilities that caused these other costs to be incurred
11 and, therefore, should contribute to their recovery.

12

13 Likewise, setting prices for UNEs too high will also not create the result
14 envisioned by Congress. Although setting prices too high will not encourage
15 ALECs to purchase the elements from the LEC, it would give the ALEC the
16 maximum incentive to build its own facilities and, in the long run,
17 infrastructure competition will develop sooner. What Congress envisioned as
18 an interim step, however, will not come to fruition.

19

20 In both of these examples the prices charged for services offered will not be the
21 most efficient, and it is the consumer that stands to lose.

22

23 Q. YOU MENTIONED THE TELECOMMUNICATIONS ACT OF 1996 IN
24 YOUR PREVIOUS ANSWER. WHAT STANDARDS ARE ADDRESSED
25 IN THE ACT?

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A. The Act addresses the pricing of unbundled elements and interconnection. Section 252 (d)(1) of the Act states that the just and reasonable rate for interconnection of facilities and equipment and the just and reasonable rate for network elements:

“(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.”

Q. DOES THE ACT REQUIRE A SPECIFIC COST STANDARD?

A. No. The Act does not prescribe any specific cost standards. Implicit in its language, however, is the requirement that full actual costs may be recovered. If full actual costs were not intended to be recovered, there would be no reason to provide an opportunity for prices to include a reasonable profit. A profit cannot be realized until the full actual costs of the item are recovered.

Q. DOES THE FEDERAL COMMUNICATIONS COMMISSION (“FCC”) HAVE RULES THAT APPLY TO THE DEVELOPMENT OF COSTS AND PRICES FOR UNEs AND INTERCONNECTION?

1 A. No. The FCC's First Report and Order in CC Docket No. 96-98 (the "FCC's
2 Order") included several sections that pertain to the development of costs and
3 prices. Sections 51.505-51.515 (inclusive) which specify a rate structure for
4 the pricing of elements, were vacated by the United States Court of Appeals for
5 the Eighth Circuit. Sections 51.601-51.611 (inclusive) regarding resale, and
6 51.701-51-717 (inclusive), regarding reciprocal compensation for transport and
7 termination of local telecommunications traffic, were also vacated. The Eighth
8 Circuit was very clear that states have sole jurisdiction for establishing prices
9 for UNEs and interconnection. The FCC has no role in establishing prices and
10 cannot direct the states in any manner in this area.

11

12 Q. WERE THE RULES AND RATE STRUCTURE SET FORTH IN THE
13 FCC'S RULES APPROPRIATE?

14

15 A. No. Many of the FCC's Rules conflicted with the Act and were appropriately
16 vacated by the Eighth Circuit. The general guidelines included in Rule 51.503
17 do, however, appear to be appropriate and in compliance with the Act. This
18 Rule states that incumbent LECs shall offer UNEs at rates, terms and
19 conditions that are just and reasonable. Based on the Act and the decision by
20 the Eighth Circuit, a state commission, however, has the sole authority to
21 determine rates that are just and reasonable. This Commission is not bound by
22 any pricing standards developed by the FCC. However, the pricing guidelines
23 included in the Act are applicable. BellSouth's proposed methodology and
24 rates are in compliance with these guidelines.

25

1 The August 19, 1997 FCC Order on the Ameritech/Michigan application does
2 not change this situation. The Commission still has sole authority to establish
3 appropriate rates for UNEs and interconnection in Florida. The issue of what
4 the FCC can require for interLATA relief will be addressed between the FCC
5 and BellSouth once the FCC considers BellSouth's interLATA application. It
6 has no impact on the ability of the Commission to establish prices in this
7 proceeding.

8
9 Q. HAS THE FLORIDA COMMISSION ADOPTED A COST
10 METHODOLOGY?

11
12 A. Yes. In Order No. PSC-96-1531-FOF-TP, issued December 16, 1996
13 (BellSouth/MFS arbitration), the Commission stated "... the appropriate cost
14 methodology to determine prices for unbundled elements should approximate
15 TSLRIC. This is the pricing policy we adopted in our state proceeding on
16 unbundling and resale." Additionally, in establishing permanent rates in the
17 AT&T/MCI/ACSI consolidated arbitration proceedings, the Commission
18 stated "[W]e find it appropriate to set permanent rates based on BellSouth's
19 TSLRIC cost studies."

20
21 Q. IS IT APPROPRIATE TO SET RATES FOR UNBUNDLED ELEMENTS AT
22 TSLRIC?

23
24 A. No. Aside from the fact that it is not a requirement of the Act or the FCC's
25 Order, as I have stated previously, a company would not stay in business long

1 if it set all rates at TSLRIC. More specifically, BellSouth, as well as any
2 multiservice company, has shared and common costs that must be recovered by
3 pricing services, i.e., UNEs, above incremental cost. Although BellSouth
4 acknowledges that competition will appropriately drive prices toward actual
5 cost, competition will not drive prices to TSLRIC. BellSouth submits that
6 prices will move toward a point where all valid costs are recovered. Those
7 costs include shared and common costs as well as historical costs. If one group
8 of services is exempt from the requirement to cover these costs, other services
9 must be priced higher to make up the difference, forcing the prices for those
10 services to be inflated. Setting prices that do not cover actual costs establishes
11 a vicious cycle that harms consumers. If the prices of the services provided to
12 competitors do not cover cost, BellSouth will be subsidizing its competitors.
13 BellSouth must then attempt to recover this shortfall in retail prices. However,
14 this purported solution would not work because the competitor who is using
15 subsidized facilities would not have to recover this shortfall in its prices.
16 Consequently, the competitor could simply undercut BellSouth's retail prices.
17 The result is that this subsidy to competitors would ultimately be borne by
18 those end users who have the least competitive options, e.g., rural residential
19 customers. In addition, by creating a high price umbrella for the competitor,
20 all retail customers would pay higher prices than they would otherwise. The
21 competitors benefit, but the end user loses. This does not seem fair when both
22 the end-user and the ALEC are benefiting from, and share in, the use of
23 BellSouth's network. BellSouth must recover all of its costs to continue to be
24 a viable concern, and all of the users of the network should contribute toward
25 that recovery.

1
2 The Commission agreed that contribution above TSLRIC is appropriate,
3 stating in its December 31, 1996 Arbitration Order, that “[W]e find it
4 appropriate to set permanent rates based on BellSouth’s TSLRIC cost studies. .
5 . The rates cover BellSouth’s TSLRIC costs and provide some contribution
6 toward joint and common costs.” (Order, page 33).

7
8 Q. SHOULD PRICES BE SET EQUAL TO ECONOMIC COSTS?

9
10 A. No, for several reasons. First, it is inappropriate to establish a rigid rule for
11 prices to equal any specific cost standard. In this case, economic costs are
12 defined as TSLRIC plus an allocation of shared and common costs. Pricing
13 must account for the cost of the element plus the market, regulatory and
14 competitive conditions that exist. Further, pricing is not so simplistic that it
15 can be narrowed to an exact numerical exercise. Prices for UNEs must be
16 based on cost, but that is not the only factor to consider. Another consideration
17 is that prices must also be functional in the marketplace and be consistent with
18 prices for similar services. For example, BellSouth is recommending that
19 virtual collocation be priced at the existing interstate tariff rates that already
20 exist in the marketplace. These proposed prices are based on cost, but also
21 account for the fact that there is an existing tariff for virtual collocation.

22
23 Second, prices should be set so sellers and buyers make correct economic
24 choices. Finally, prices must cover total costs, including incremental, common

1 and historical. This is necessary for a firm to remain in business and is
2 required for a firm to make efficient investment.

3

4 Q. WHAT ARE THE CONSEQUENCES OF SETTING PRICES THAT DON'T
5 COVER TOTAL COST?

6

7 A. One consequence of setting prices that don't cover total cost is such pricing
8 creates incentive for inefficiency. It deters the ILEC from undertaking
9 investments because it guarantees that the costs of those investments will not
10 be recovered. ALECs will over-consume the ILEC's facilities and under-
11 invest in their own facilities, even when investing in their own facilities is the
12 efficient choice.

13

14 Another consequence of such pricing is that it encourages the ILEC to invest in
15 technology that involves low shared cost (which reduces economy of scale)
16 and high incremental costs, even if that is not the lowest cost technology. If
17 incremental costs are the only costs that can be recovered, the fact that shared
18 cost technology is cheaper becomes irrelevant.

19

20 A third consequence is such pricing invites inefficient entry of ALECs by
21 placing all of the risks of building and maintaining a network on the incumbent
22 ILEC. As previously discussed, ALECs don't commit to use ILEC facilities
23 over their economic life, but they have the option to do so. If prices don't
24 cover costs, the ALECs don't bring to the marketplace anything more than an
25 arbitrage mechanism that allows them to avoid paying the costs they would

1 otherwise have to pay in a competitive marketplace. End user customers are
2 the losers in this arrangement.

3

4 Q. WHAT COSTS THAT NEED TO BE RECOVERED ARE NOT INCLUDED
5 IN TSLRIC?

6

7 A. There are three additional categories of costs that must be recovered that are
8 not included in the development of incremental cost.

9

10 The first group of costs are referred to as shared costs and are not included in
11 the TSLRIC studies. Shared costs are costs that are shared by several
12 elements, but that can be directly attributed to the particular element being
13 studied. This category of costs may include costs such as general purpose
14 computers, engineering expense, plant administration and network
15 administration.

16

17 Another group of costs excluded is generally referred to as common costs.
18 These costs are common to the corporation as a whole and cannot be directly
19 attributed to an individual element or service. These costs include such
20 functions as the executive, legal, and administrative functions.

21

22 The third type of cost excluded in forward looking incremental cost is
23 historical cost. Historical costs are the difference in costs between the network
24 BellSouth is actually using and the network composed of forward looking
25 technology. These costs include capital costs and plant specific expenses

1 related to the current network and other non-plant specific expenses.

2

3 Q. DOES PRICING AT TSLRIC PROVIDE FOR A REASONABLE PROFIT
4 AS PERMITTED BY THE ACT?

5

6 A. *It certainly does not. Proponents of this theory equate economic profit with*
7 *cost of capital which is not a legitimate comparison. Cost of capital is a cost*
8 *like any other cost of doing business. It is well accepted that a profit cannot be*
9 *realized until all costs, including cost of capital, have been recovered.*

10 *Although pricing at TSLRIC would provide for the cost of capital attributable*
11 *to the investments directly related to the specific element involved, it would*
12 *not provide for any contribution to shared or common costs or any cost of*
13 *capital on investment not related to a specific service. Until BellSouth*
14 *recovers all of its costs, and cost of capital on its total operations is a cost,*
15 *BellSouth does not make a profit.*

16

17 Q. HOW DOES BELLSOUTH PROPOSE TO ESTABLISH PRICES FOR
18 INTERCONNECTION AND UNBUNDLED NETWORK ELEMENTS?

19

20 A. *Prices will be established based on cost and will recognize market conditions*
21 *and regulatory requirements as necessary. Costs are only one input to the price*
22 *setting process. Prices for new services must also be established in appropriate*
23 *relationship to existing services to prevent arbitrage. In addition, where*
24 *regulatory requirements exist, prices must meet those requirements.*

25

1 To encourage development of competition, BellSouth has proposed most of its
2 prices to be equal to TSLRIC plus shared and common costs. Where historical
3 costs were significant, prices equal to the actual costs of providing the service,
4 including shared, common costs and historical costs were proposed. This does
5 not mean that historical cost recovery is not important for any element. It
6 merely recognizes that the bulk of historical costs are resident in a relatively
7 few elements. These are the lowest prices that can be charged and still recover
8 costs. Setting prices lower than these levels would have BellSouth subsidize
9 its competitors. These costs are clearly a price floor, not a price ceiling.

10
11 Q. PLEASE DESCRIBE THE ELEMENTS THAT INFLUENCED
12 BELLSOUTH'S DEVELOPMENT OF RATES FOR THIS DOCKET.

13
14 A. The revised cost studies submitted in this proceeding provide the foundation
15 for establishing the proposed rates for the UNEs as listed by the Commission.
16 As noted earlier, in some instances, the cost data and accompanying cost
17 factors simply become the proposed rate. This is the simplest approach, and in
18 most instances, the most appropriate approach for today's conditions. Other
19 factors, however, must also be considered. For example, for virtual
20 collocation, tariffed rates also exist. In deciding whether to propose the cost
21 study rate or the existing tariff rate, a significant factor is the arbitrage
22 opportunities that arise when two different rates apply for the identical service.
23 As long as the tariffed rate has been established based on costs, that rate may
24 be appropriate for a comparable unbundled element.

25

1 Q. WHAT COSTS ARE INCLUDED IN THE FIRST COMPONENT OF
2 BELLSOUTH'S PROPOSED RATE STRUCTURE?

3
4 A. The first component is TSLRIC. The methodology used is consistent with the
5 guidelines definition established by the Commission in Order No. PSC-96-
6 1579-FOF-TP for the AT&T/ MCI/ACSI consolidated arbitration. The
7 Commission stated: "[W]e find TSLRIC should be defined as the costs to the
8 firm, both volume sensitive and volume insensitive, that will be avoided by
9 discontinuing, or incurred by offering, an entire product or service, holding all
10 other products or services offered by the firm constant." (Order, page 25). Ms.
11 Caldwell and Mr. Zarakas include a more detailed discussion of the
12 development of TSLRIC in their testimony, and Mr. Reid discusses the
13 development of shared and common costs.

14
15 Q. PLEASE DESCRIBE IN MORE DETAIL WHY SHARED AND COMMON
16 COSTS, THE SECOND COMPONENT, ARE APPROPRIATELY
17 INCLUDED IN THE RATE SETTING PROCESS.

18
19 A. Although shared and common costs are not incremental to any one service that
20 BellSouth provides, they are nonetheless valid costs of doing business and
21 must be recovered. For BellSouth to stay in business, revenues from all
22 services must not only cover incremental cost, but they must also provide
23 sufficient contribution to cover all other costs of the firm. The FCC also
24 recognizes that the rates for each element should include "a reasonable
25 allocation of forward-looking common costs."

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Q. PLEASE EXPLAIN FURTHER THE THIRD COMPONENT OF BELL SOUTH'S PROPOSED RATE STRUCTURE THAT YOU MENTIONED EARLIER IN YOUR TESTIMONY.

A. The third component of the proposed rate structure is the difference between TSLRIC plus shared and common costs, and the actual cost of providing the network element. This factor is designed to recognize that the actual element being provided is part of a real, existing network that will be used on a going forward basis, and not some portion of a theoretical projection of a future network. Rate development must recognize that an existing network has real costs and that these costs should be recovered by the cost causers.

The Act states that BellSouth may include a reasonable profit in setting its rates. BellSouth cannot make a reasonable profit unless it is able to set its prices sufficiently above TSLRIC to provide a reasonable contribution toward its shared and common costs and recover historical costs. Since the Act permits rates to contain a profit above costs, it clearly anticipates that rates will recover, at a minimum, the actual costs of the firm. It is certainly reasonable to recover historical costs, which are real costs, since it is also reasonable to make a profit.

Q. WHY SHOULD PRICES FOR CERTAIN UNEs INCLUDE THE RESIDUAL RECOVERY REQUIREMENT?

1 A. As I stated previously, BellSouth is entitled to recover all of its actual costs of
2 doing business. The historical cost of an element that BellSouth provides on
3 an unbundled basis is certainly a legitimate cost of doing business. Using only
4 forward looking costs of providing a service may be appropriate for a firm that
5 is starting from scratch and building a completely new network to provide such
6 a service. This is certainly not the case with BellSouth.

7
8 The fact is, the network in place today allows BellSouth to offer a wide variety
9 of UNEs and reduces the forward looking cost of those elements. The network
10 that provides ALECs that functionality has a cost. BellSouth should have the
11 chance to recover the costs associated with investments previously made and
12 currently used in the network and those made in good faith pursuant to
13 obligations under a traditional regulatory compact. If BellSouth is forced to set
14 all of its rates only at TSLRIC plus reasonable shared and common costs, it is
15 precluded from recovering all of its actual costs.

16
17 Q. HAS BELLSOUTH INCLUDED THE RESIDUAL RECOVERY
18 REQUIREMENT IN ALL RATE ELEMENTS PROPOSED?

19
20 A. No. BellSouth has chosen a simple, straightforward method for recognizing
21 these historical costs: identify the primary area, in this case investment,
22 impacted by recognizing only forward looking incremental costs; identify the
23 primary elements impacted, in this case the 2-wire ADSL-compatible loop, the
24 2-wire/4-wire HDSL-compatible loops and the 4-wire Analog port; and
25 calculate the impacts on these elements.

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By providing TSLRIC studies for the loops and port in question, and then adjusting them to recognize historical cost differences, the impact of ignoring these historical costs is identified. The adjustments that recognize the historical costs, used in conjunction with the TSLRIC studies plus shared and common costs, become the basis for establishing the loop and port rates.

Q. COULD YOU EXPLAIN WHY THE HISTORICAL COSTS WERE ONLY CALCULATED FOR THE LOOPS AND PORT AND NOT FOR OTHER UNBUNDLED ELEMENTS?

A. Yes. As described by Ms. Caldwell, the area with the greatest discrepancy when comparing actual and forward looking costs is investment. This should not be surprising because one would expect technological advancement to impact this area substantially. While there are a large number of unbundled elements with an investment component, a predominant portion of investment, (approximately 70 percent) is found in the loops and ports. To simplify the process, BellSouth has limited the historical cost calculation to these two elements even though similar calculations could be made for other unbundled elements. However, the additional amount required would be very small.

Q. IF BELLSOUTH CANNOT RECOVER FULL ACTUAL COSTS FROM THE RATES CHARGED FOR THE UNBUNDLED ELEMENTS AT ISSUE, WHAT WILL BE THE EFFECT ON FLORIDA CONSUMERS?

1 A. As I stated above, BellSouth's end-users, i.e., Florida consumers, will be
2 forced to cover all additional costs. The major result would be that since these
3 costs are legitimate costs of doing business, BellSouth must recover them from
4 some source. If they cannot be recovered from the services or elements with
5 which they are associated, other rates must be increased. Prices for end-user
6 services, out of necessity, will be affected. In the long run, the Florida
7 consumer, and more likely, the rural consumer, will be required to make up the
8 difference and, in effect, subsidize the ALECs. In Florida, this scenario is
9 exacerbated by the price regulation rules. Under price regulation, BellSouth is
10 *precluded from raising certain rates for a specified period*. If BellSouth is
11 *precluded from recovering all of its actual costs*, an artificial advantage is
12 created for the ALECs and an irreversible and unfair disadvantage is created
13 for BellSouth.

14
15 Q. ARE THERE OTHER CONSEQUENCES OF NOT INCLUDING A
16 COMPONENT FOR THE RECOVERY OF SHARED AND COMMON
17 COSTS IN THE RATE FOR UNBUNDLED NETWORK ELEMENTS?
18

19 A. Yes. Dr. Richard Emmerson cited at least two more consequences in his
20 testimony in the North Carolina Utilities Commission's Docket No. P-140, Sub
21 50. Dr. Emmerson stated, "[f]irst, new firms considering undertaking the risk
22 of entering on a facilities basis would be aware that successful entry would
23 yield at most recovery of the incremental costs of entry, without the possibility
24 of contribution towards the firm's joint and common costs and without any
25 reward for the risk of entering. These firms would be unlikely to undertake the

1 risks of entry.”

2

3 He goes on to say that, “BellSouth, faced with receiving no contribution from
4 the unbundled network elements towards its joint and common costs would
5 have to balance the returns on other investments that could yield at least some
6 contribution with investing in new elements and its carrier of last resort
7 obligations. Just as the incentives created by such pricing would make new
8 entrants less likely to enter on a facilities basis, they would make BellSouth
9 less likely to invest in facilities. To the extent BellSouth may be constrained
10 by its legal obligations to invest in new facilities, pricing without recovery of
11 joint and common costs is unfair.”

12

13 Q. PLEASE EXPLAIN THE EXHIBITS ATTACHED TO YOUR TESTIMONY.

14

15 A. Exhibit AJV-1 provides an overall summary of BellSouth’s proposed rates in
16 this docket and their associated costs. The cost study reference number is
17 provided with the description of the corresponding rate element. The summary
18 cost data contained in BellSouth’s cost studies is provided as well as the rates
19 that BellSouth proposes.

20

21 ~~Exhibit AJV-2 demonstrates discounts on non-recurring rates for UNE loops~~
22 ~~and ports when the elements are ordered at the same time.~~

23

24 Q. PLEASE EXPLAIN THE DERIVATION OF BELLSOUTH’S PROPOSED
25 RATES FOR EACH UNE IN THIS DOCKET.

1

2 A. The following section of this testimony describes how BellSouth's rate setting
3 approach applies to the individual UNEs, as listed by issue number. Where an
4 explanation is required, individual cost study results and the corresponding
5 rates are discussed.

6

7 **Issue 1(a): Network Interface Device (NID)**

8

9 Q. WHAT ARE BELLSOUTH'S PROPOSED RECURRING AND NON-
10 RECURRING RATES FOR THE NID?

11

12 A. BellSouth proposes that the NID be priced at a recurring monthly rate of \$1.44,
13 with non-recurring rates of \$5.59/\$46.93 (electronic/manual) for the first and
14 \$2.91/\$14.55 (electronic/manual) for each additional NID. These rates are
15 equal to the TSLRIC plus shared and common costs submitted by BellSouth.

16

17 **Issue 1 (b): 2-wire/4-wire Loop Distribution**

18

19 Q. PLEASE DESCRIBE BELLSOUTH'S PROPOSED RECURRING AND
20 NON-RECURRING RATES FOR 2-WIRE/4-WIRE LOOP DISTRIBUTION.

21

22 A. BellSouth recommends a recurring rate of \$12.57 per month for 2-wire loop
23 distribution and \$16.90 per month for 4-wire loop distribution. These rates are
24 based on TSLRIC plus shared and common costs, and each includes a residual
25 recovery requirement. All rates for 2-wire and 4-wire loop distribution,

1 including non-recurring rates, are listed on Exhibit AJV-1.

2

3 **Issue 1(c): Virtual Collocation and Issue 1(d): Physical Collocation**

4

5 Q. COULD YOU EXPLAIN BELLSOUTH'S PROPOSED RATES FOR
6 VIRTUAL COLLOCATION?

7

8 A. Yes. BellSouth submitted cost studies for both physical and virtual
9 collocation. Unlike many other elements, however, existing tariff rates should
10 apply to virtual collocation. These rates have existed in federal tariffs for
11 several years and came under significant scrutiny at the time of their initial
12 filing. In Florida, these rates, terms and conditions for virtual collocation are
13 set forth in Section E20.1 of the Florida Access Service Tariff. Although
14 these rates are not subject to the pricing standards of Section 252(d) of the Act,
15 they are cost based.

16

17 There are several practical reasons for proposing the existing tariff rates. The
18 Act provides an obligation that LECs offer physical collocation to ALECs.
19 Virtual collocation may be provided only after the ILEC has demonstrated to a
20 state commission that physical collocation is not practical for technical reasons
21 or because of space limitations. These requirements are contained in Section
22 251(c)(6) of the Act. Virtual collocation, therefore, will be the exception rather
23 than the rule. Conversely, existing interexchange carriers ("IXCs") only have
24 virtual collocation available to them and as a practical matter may wish to
25 continue virtual collocation for their combined IXC/ALEC business. It would

1 appear nonsensical to charge the carrier one price for a portion of the virtual
2 collocation space and features and a different rate for others. Further, it would
3 appear somewhat arbitrary to allocate a portion of the space to IXC business
4 and another portion to ALEC business for the sake of applying different rates.
5 The practical effect of establishing different rates is that arbitrage would result.

6

7 Q. WOULD YOU PLEASE COMPARE YOUR RECOMMENDED TARIFF
8 PRICES FOR VIRTUAL COLLOCATION TO THE COST STUDY
9 RESULTS YOU ARE SUBMITTING?

10

11 A. Yes. For comparison purposes, I have listed the results of BellSouth's cost
12 studies for virtual collocation on Exhibit AJV-1, alongside the tariff rates that
13 BellSouth is proposing. Specifically, the exhibit lists BellSouth's TSLRIC
14 results, TSLRIC plus shared and common costs, and the proposed rates. Since
15 there are no tariff rates for the 2-wire and 4-wire cross connects applicable to
16 virtual collocation, BellSouth is proposing TSLRIC plus shared and common
17 costs for these UNEs.

18

19 Q. WHAT RATES DOES BELLSOUTH RECOMMEND FOR PHYSICAL
20 COLLOCATION?

21

22 A. The issues related to virtual collocation as outlined above do not apply to
23 physical collocation. For that reason BellSouth recommends prices equal to
24 cost study results plus shared and common costs for physical collocation.
25 These rates are listed in Exhibit AJV-1.

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Issue 1(e): Directory Assistance (Directory Transport - DS1 Only)

Q: WHAT ARE BELLSOUTH'S PROPOSED RECURRING AND NON-RECURRING RATES FOR DIRECTORY TRANSPORT - DS1 ONLY?

A. BellSouth proposes that the Commission adopt its TSLRIC cost study results plus shared and common costs as the permanent rates for the directory transport - DS1 unbundled elements. The recurring and non-recurring rates for these elements are listed on Exhibit AJV-1.

Issue 1(f): Dedicated Transport (Non-recurring only; DS1)

Q. PLEASE EXPLAIN BELLSOUTH'S APPROACH TO SETTING NON-RECURRING RATES FOR DEDICATED TRANSPORT.

A. Dedicated transport is used only for the traffic of the ALEC ordering it and will typically connect two BellSouth facilities for that ALEC's use. The non-recurring rates for dedicated transport are based on BellSouth's TSLRIC studies, plus shared and common costs, and are listed on Exhibit AJV-1.

Issue 1(g): 4-wire Analog Port

Q. PLEASE COMMENT BRIEFLY ON THE ISSUES THAT RELATE TO THE 4-WIRE UNBUNDLED PORT AS A COMPONENT OF SWITCHING.

1

2 A. There are diverse issues related to this unbundled element. First, the question
3 of recovery of historical costs is relevant to the port, which is the monthly
4 recurring component of unbundled switching. Secondly, the treatment of
5 vertical features that can be provided through the switch is also at issue.

6

7 Q. PLEASE EXPLAIN THE STRUCTURE AND RATES FOR THE 4-WIRE
8 ANALOG PORT.

9

10 A. The proposed rates for the 4-wire analog port (as a component of unbundled
11 switching) are shown on Exhibit AJV-1. The port costs include the TSLRIC-
12 based costs, shared and common costs, and a portion of historical costs in a
13 manner similar to the loop. The proposed rates for this element also include
14 for the recovery of the costs associated with the applicable vertical features.

15

16 Q. PLEASE EXPLAIN BELLSOUTH'S PROPOSAL FOR UNBUNDLED
17 SWITCHING AND THE INCLUSION OF VERTICAL FEATURES.

18

19 A. In its December 31, 1996 Arbitration Order, the Commission adopted the
20 FCC's definition of local switching as an unbundled network element. (Order,
21 pages 15-16). The FCC definition, as quoted by the Commission, defines local
22 switching to encompass ". . . all features, functions, and capabilities of the
23 switch which include, but are not limited to: (1) the basic switching function
24 of connecting lines to lines, lines to trunks, trunks to lines, trunks to trunks, as
25 well as, the same basic capabilities made available to the incumbent LEC's

1 customers, such as a telephone number, white page listing, and dial tone; and
2 (2) all other features that the switch is capable of providing, including but not
3 limited to custom calling, custom local area signaling service features, and
4 Centrex, as well as any technically feasible customized routing functions
5 provided by the switch.”

6
7 In the arbitration proceedings, the cost studies submitted by BellSouth did not
8 include the vertical features because BellSouth treated these features as retail
9 services subject to resale. The Hatfield model data submitted by AT&T was
10 said to include the features in the switching costs. Neither BellSouth nor
11 AT&T, however, provided a study with and without the vertical features to
12 determine what the cost of these features were.

13
14 In this proceeding, BellSouth has again provided switching and port costs
15 excluding the vertical features, but has also included the costs of the vertical
16 features that would be applicable to the 4-wire Analog port, Issue No. 1(g).
17 To determine the rate for switching including these vertical features, it is
18 necessary to add up the costs of all the vertical features and add them to the
19 basic port cost. This would yield a monthly 4-wire analog port cost of \$17.36.

20
21 **Issue 1(h): 2-wire ADSL-compatible Loop and Issue 1(i): 2-wire/4-wire HDSL-**
22 **compatible Loop**

23

24 Q. PLEASE DESCRIBE THE FACTORS USED IN DEVELOPING THE
25 RECURRING AND NON-RECURRING RATES FOR THE 2-WIRE ADSL-

1 COMPATIBLE LOOP AND THE 2-WIRE/4-WIRE HDSL-COMPATIBLE
2 LOOP.

3

4 A. There are several individual factors that are considered in developing the rates
5 and costs for all of BellSouth's unbundled loops. To assist in putting all the
6 factors into perspective, the following summary is provided outlining the
7 considerations that went into the development of the loop costs and rates:

8 1) The types of loops for which costs and rates are provided.

9 2) The level of geographic averaging: Rates are proposed on a statewide
10 basis, i.e., no geographic deaveraging.

11 3) The type of costs to be recovered in the rates: Loop studies are provided to
12 reflect typical TSLRIC results plus an allocation of shared and common costs
13 as well as historical costs (to recognize some of the infirmities of a TSLRIC-
14 only approach).

15

16 Q. WILL THERE BE VARYING RATES FOR THE DIFFERENT TYPES OF
17 LOOPS BELLSOUTH OFFERS?

18

19 A. Yes. First, as discussed earlier, BellSouth is filing loop rates to recognize the
20 impact of shared and common costs and historical costs in addition to the
21 TSLRIC results. Each loop type has characteristics which differentiate it from
22 the others. Following are the loop types, and associated proposed recurring
23 rates:

1

Loop Type	Proposed Monthly Rate
2-Wire ADSL	\$23.28
2-Wire HDSL	\$17.73
4-Wire HDSL	\$27.06

2

3 Q. IN GENERAL, WHAT ARE SOME OF THE CHARACTERISTICS THAT
4 CAUSE DIFFERENT LOOP TYPES TO HAVE DIFFERENT COSTS?

5

6 A. The variance in costs for different types of loops is mainly attributable to the
7 type of facility required. For instance, a 2-wire analog loop can operate
8 effectively with smaller gauge copper and longer loop lengths than some other
9 facility types, because the services that ride these facilities (typically residential
10 and some business local exchange service or Plain Old Telephone Service
11 [POTS]) are not technically demanding. On the other hand, the facilities that
12 are required to provide ISDN, ADSL or HDSL loops are subject to technical
13 limitations and specifications. Such facilities require shorter loop lengths,
14 heavier gauge copper and more manual work activity than POTS. As
15 evidenced by these varying physical loop characteristics, the resulting costs
16 and rates also vary.

17

~~18 Q. ARE THERE OTHER NON-RECURRING COSTS THAT SHOULD BE
19 CONSIDERED IN THE PROVISION OF THE UNBUNDLED ELEMENTS
20 INCLUDED IN THIS PROCEEDING?~~

21

~~22 A. Yes. The non-recurring charges associated with the recovery of operations
23 support systems costs should be considered. In addition, non-recurring prices~~

1 should recognize the difference in cost between unbundled elements that are
2 ordered electronically using the OSS and those that are ordered manually.

3
4 Q. HOW DOES BELLSOUTH PROPOSE TO RECOVER ITS COSTS OF
5 PROVIDING OPERATIONS SUPPORT SYSTEMS?
6

7 A. Access to operations support systems by ALECs is necessary for implementing
8 resale, unbundling and interconnection. Typically, the costs for BellSouth's
9 existing operations support systems are recovered in basic service rates and
10 generally through nonrecurring charges, e.g., service order charges. In this
11 situation where access to OSS are being provided for ALEC use, some
12 additional factors need to be considered. First, ALECs will determine whether
13 they will use manual interfaces, standard electronic interfaces or uniquely
14 designed interfaces. Second, the FCC defined operations support systems as
15 unbundled network elements. In its order in Docket CC 96-98, the FCC
16 concluded, "...that operations support systems and the information they contain
17 fall squarely within the definition of a "network element" and must be
18 unbundled upon request under section 251(c)(3)...." (paragraph 516)

19
20 Given these circumstances, BellSouth has approached this issue in the
21 following manner. First, it has developed the basic nonrecurring costs for the
22 unbundled network elements without reflecting either the costs of electronic or
23 manual interfaces. These are the costs shown in Exhibit AJV-1 that are
24 specifically associated with the various unbundled elements. The next step
25 was to develop an increment for processing an order manually. This increment

1 varies by unbundled network element, as would be expected. The nature of a
2 manual order would lead to different work times based on the type of order.
3 The increment for manual orders has been added to the basic nonrecurring
4 costs, and these costs and charges are so noted on Exhibit AJV-1. For
5 example, Exhibit AJV-1, under TSLRIC plus shared and common cost,
6 indicates a 2-wire ADSL loop (Ref. # A.6.1) with a basic nonrecurring charge
7 of \$619.76. If the order is placed manually, the charge becomes \$661.10, or a
8 \$41.34 additional increment. As demonstrated in BellSouth's cost studies, the
9 costs of manual orders will vary on an item specific basis.

10
11 Q. HOW DOES BELLSOUTH INTEND TO RECOVER THE COSTS
12 ASSOCIATED WITH THE OPERATIONS SUPPORT SYSTEMS AS AN
13 UNBUNDLED ELEMENT?

14
15 The total costs for the electronic interfaces were simply divided by the number
16 of anticipated orders (including resale orders which are not impacted by this
17 proceeding), and it was determined that it would take approximately \$11.00 an
18 order to recover the OSS costs in Florida. Because a large number of the
19 orders will be for resale, recovering this cost for each electronically processed
20 unbundled element order will, in reality, defray only a small portion of the
21 costs. While BellSouth could have selected other means for recovering its
22 OSS costs, the combination of different nonrecurring charges and the
23 electronic interface charges noted above seems to best capture the treatment of
24 OSS as a network element. A balance has been struck between following cost
25 causative principles and treating small and large ALECs equitably

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Q. HOW WILL NON-RECURRING CHARGES BE APPLIED WHEN MULTIPLES OF THE SAME ELEMENTS ARE INSTALLED AT THE SAME TIME?

A. The non-recurring charges for unbundled network elements have been studied and costs developed on a stand-alone basis. The applicable rate will be charged for each individual element for which a non-recurring charge applies. This is true whether the element is ordered alone or in multiples. The one exception is when an element has one non-recurring charge for the first unit installed and another non-recurring charge for additional unit(s) installed at the same time. For example, if an ALEC ordered five units of the same item, one first unit charge would apply and four additional unit charges would apply.

~~Q. PLEASE ADDRESS BELL SOUTH'S APPROACH TO DEVELOPING THE APPROPRIATE NON-RECURRING CHARGE FOR THE COMBINATION OF NETWORK ELEMENTS IDENTIFIED IN ISSUE 2.~~

~~A. BellSouth's suggested non-recurring charges ("NRCs") for each of these combinations are listed on Exhibit A JV-2 and are consistent with this Commission's March 19, 1997 Order No. PSC-97-0298-FOF-TP (Final Order on Motions for Reconsideration and Amending Order No. PSC-96-1579-FOF-TP). In that Order, the Commission stated "[W]e hereby order BellSouth to provide NRCs that do not include duplicate charges or charges for functions or activities that AT&T does not need when two or more network elements are~~

1 combined in a single order.” The Commission also stated that the same is
2 applicable to MCI.

3
4 The Commission’s use of the word “migration” in Issue 2 could lead to
5 confusion in the interpretation of issues in this docket. Specifically, Issue 2
6 calls for NRCs for each combination for “migration of an existing BellSouth
7 customer.” In the telecommunications industry, the term “migration” typically
8 applies to a switch “as is.” A switch “as is” pertains only to a resale
9 environment. This is a UNE cost proceeding, not a resale proceeding.
10 BellSouth is focusing on NRCs as applied to unbundled network elements that
11 are ordered simultaneously, which is consistent with the Commission’s
12 decision in the AT&T and MCI arbitration orders. BellSouth’s discounted
13 non-recurring charges are not intended to accommodate a switch “as is.”

14
15 Q. PLEASE EXPLAIN HOW BELLSOUTH WILL EXCLUDE THE
16 DUPLICATE CHARGES WHEN ALECs ORDER TWO OR MORE OF THE
17 NETWORK ELEMENTS, AS IDENTIFIED IN ISSUE 2, COMBINED ON A
18 SINGLE ORDER.

19
20 A. BellSouth will discount the NRCs for use by ALECs when two or more of the
21 network elements identified in Issue 2 are combined in a single order. The
22 discounted NRCs, listed on AJV-2, reflect the elimination of all duplicate
23 charges. The discounted NRCs will be developed as follows: BellSouth will
24 first consider (1) the non-recurring costs for each of the applicable elements on
25 a stand-alone basis, and then (2) the total that would apply if the NRCs for the

1 stand-alone items were added together without considering duplicate costs.
2 BellSouth will then compare the figure for (2) to (3) the costs for the
3 combination when any duplicate charges have been removed. The comparison
4 between figures (2) and (3) will provide a percentage difference that BellSouth
5 will use as the basis to discount the NRC for the specific combination. To
6 summarize, the new NRCs that BellSouth proposes for the combined orders are
7 specific numbers that are based on a percentage discount that eliminates
8 duplicate charges. All of these NRCs also include shared and common costs.
9 BellSouth has not yet determined whether the discounted NRCs will appear on
10 the bill as a discounted charge or as the original minus the discount.

11

12 Q. PLEASE SUMMARIZE YOUR TESTIMONY.

13

14 A. My testimony requests that the Commission approve BellSouth's proposed
15 prices for the unbundled network elements addressed. The Act allows an
16 incumbent LEC to develop rates based on cost and to include a reasonable
17 profit. BellSouth's proposed rates for these UNEs are based on TSLRIC,
18 including shared costs, and include cost components for common and historical
19 costs. These are the lowest prices that can be charged and allow BellSouth to
20 recover its costs.

21

22 BellSouth must be allowed to recover its actual costs of providing a service.
23 Historical and common costs are legitimate costs that must be recovered. The
24 benefits of historical and common facilities and costs should be shared by
25 BellSouth's end user customers and by those ALECs interconnecting with

1 BellSouth as well as purchasing unbundled network elements from BellSouth.
2 I would not expect, because MCI needs a switch to enter the local telephone
3 market, that Lucent Technologies would provide that switch at its TSLRIC or
4 any other similar cost. Just as Lucent needs a reasonable contribution to its
5 shared and common costs and recovery of its historical costs, BellSouth also
6 needs such cost recovery. If BellSouth is unable to recover such costs, the
7 shortfall will impact its retail prices. Consequently, BellSouth's end users,
8 particularly residential customers, will be harmed while competitors are being
9 subsidized through below cost prices.

10
11 The cost of providing services must also include a component to recover
12 historical costs. BellSouth's actual forward-looking economic cost of a service
13 cannot exclude historical costs. BellSouth has calculated the impact of this
14 cost component and applied those costs only on unbundled loops and ports.

15
16 BellSouth is not asking for anything extraordinary from the Commission.
17 BellSouth asks only that the Commission recognize that BellSouth has real
18 costs associated with the provision of UNEs that are over and above those
19 submitted in its TSLRIC studies and to allow BellSouth to recover those costs
20 in a competitively fair manner. BellSouth further requests that the
21 Commission adopt its prices for UNEs as outlined in my testimony and as
22 specified in my exhibits.

23
24 Q. DOES THIS COMPLETE YOUR TESTIMONY?
25

1 A. Yes.

1 BELLSOUTH TELECOMMUNICATIONS, INC.
2 REBUTTAL TESTIMONY OF ALPHONSO J. VARNER
3 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
4 DOCKET NOS. 960833-TP, 960846-TP, 960757-TP, 971140-TP
5 DECEMBER 9, 1997

6

7 Q. PLEASE STATE YOUR NAME, AND BUSINESS NAME AND
8 ADDRESS.

9

10 A. My name is Alphonso J. Varner. I am employed by BellSouth as Senior
11 Director for State Regulatory for the nine-state BellSouth region. My
12 business address is 675 West Peachtree Street, Atlanta, Georgia
13 30375.

14

15 Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS DOCKET?

16

17 A. Yes. I filed direct testimony and one exhibit on November 13, 1997.

18

19 Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

20

21 A. My rebuttal testimony addresses the direct testimony filed by the other
22 parties' witnesses on November 17, 1997. In responding to other
23 parties' witnesses, my testimony refutes erroneous positions and
24 assertions found in the intervenors' testimony concerning, but not
25 limited to, such issues as: ~~4~~the appropriate pricing standard for

1 unbundled network elements ("UNEs") and interconnection services;
2 ~~combination of UNEs, and 3) recovery of operations support systems~~
3 ~~("OSS") costs.~~

4
5 Q. DO YOU HAVE ANY GENERAL COMMENTS ON THE TESTIMONY
6 FILED BY THE OTHER PARTIES?

7
8 A. Yes. The Florida Public Service Commission (the "Commission") has
9 received detailed testimony from several witnesses generally opposing
10 the views of BellSouth. Throughout my testimony, along with the
11 testimony of our other witnesses, BellSouth responds to a substantial
12 portion of the detail in their testimony in order to demonstrate that these
13 parties' conclusions are seriously flawed. BellSouth does not attempt,
14 however, to respond to each and every erroneous allegation. Given
15 the complexity of these filings, it would be very easy for the
16 Commission to become mired in the details; however, it is unnecessary
17 for the Commission to do so. The focus of this proceeding must remain
18 on determining the appropriate prices for UNEs and interconnection
19 services, which generally, BellSouth has proposed at the minimum
20 level necessary to recover actual costs.

21
22 Q. AT PAGE 4, MR. ELLISON SUGGESTS, "RATES SHOULD BE SET
23 TO RECOVER TOTAL ELEMENT LONG RUN INCREMENTAL COST
24 (TELRIC), PLUS A REASONABLE CONTRIBUTION TO FORWARD -
25 LOOKING COMMON COSTS." DO YOU AGREE?

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A. No. The pricing standards (including TELRIC) contained in the Federal Communications Commission's First Report and Order ("FCC's Order") in CC Docket 96-98, which do refer to costs, have been vacated by the Eighth Circuit Court of Appeals ("Eighth Circuit"). This Commission, therefore, is not obligated to use the FCC's pricing standards when setting the appropriate prices for UNEs and interconnection services in Florida.

Sections 51.505-51.515 (inclusive) of the FCC's rules, which specify a rate structure for the pricing of unbundled elements and interconnection, were vacated. Additionally, Sections 51.601-51.611 (inclusive) regarding resale, and 51.701-51.717 (inclusive) regarding reciprocal compensation for transport and termination of local telecommunications traffic, were also vacated. The Eighth Circuit was very clear in its ruling that states have sole jurisdiction for establishing prices for UNEs and interconnection. The FCC has no role in establishing prices and cannot compel the states to adhere to any particular pricing methodology.

Indeed, this Commission has adopted Total Service Long Run Incremental Cost ("TSLRIC") as the basis for pricing UNEs and interconnection. TSLRIC, however, as with any other cost methodology, should not dictate the actual price of the UNE or interconnection element. There are other costs to consider and the

1 Telecommunications Act of 1996 (“the Act”) allows for a reasonable
2 profit above actual costs.

3

4 Q. AT PAGE 5 OF HIS TESTIMONY, DR. SELWYN ADDRESSES THE
5 EIGHTH CIRCUIT’S RECENT DECISION STATING , “WHILE THE 8TH
6 CIRCUIT COURT REVERSED THE FCC’S PREEMPTION OF STATE
7 JURISDICTION OVER THE PRICING OF THESE ELEMENTS, IT HAS
8 NOT CHALLENGED THE VALIDITY OF THE FCC’S ADOPTION OF
9 TELRIC AS THE APPROPRIATE PRICING STANDARD.” HAS THE
10 EIGHTH CIRCUIT IMPLIED THAT TELRIC IS AN APPROPRIATE
11 PRICE STANDARD?

12

13 A. No. Specifically, the Eighth Circuit ruled, “Having concluded that the
14 FCC lacks jurisdiction to issue the pricing rules, we vacate the FCC’s
15 pricing rules on that ground alone and choose not to review these rules
16 on their merits.” Therefore, to say that the Eighth Circuit did not
17 challenge the validity of TELRIC is to give it credibility as a pricing
18 standard that it does not merit.

19

20 Dr. Selwyn notes that the Eighth Circuit vacated the FCC’s pricing rules
21 then immediately, in the same paragraph, states that the FCC recently
22 ordered that an ILEC’s nonrecurring charges reflect forward looking
23 economic costs. Dr. Selwyn’s statement is completely irrelevant,
24 having just acknowledged that the FCC has no ability to dictate to the
25 ILECs pricing standards that are rightfully within the jurisdiction of the

1 state commissions.

2

3 Q. DOES THE ACT SPECIFY HOW INTERCONNECTION AND
4 UNBUNDLED ELEMENTS SHOULD BE PRICED?

5

6 A. No. As I stated in my direct testimony, the Act does not prescribe any
7 specific cost standard. The Act does state that prices should be based
8 on cost, be nondiscriminatory and may include a reasonable profit.
9 This does not mean that prices must equal cost, nor does it establish a
10 particular pricing methodology that must be followed. There are
11 numerous pricing methodologies that could meet the requirements of
12 the Act. The fact that prices may include a reasonable profit indicates
13 that, at a minimum, the Act contemplates that prices would at least
14 cover actual cost. If this were not the case, there would be no reason
15 for the reasonable profit opportunity to exist. A profit cannot be
16 realized until the actual costs of the item are recovered.

17

18 Q. IN SIMILAR CASES IN OTHER STATES AT&T AND MCI HAVE
19 SUGGESTED THAT PRICES SHOULD BE SET EQUAL TO
20 ECONOMIC COSTS. DO YOU AGREE?

21

22 A. No. There are several reasons why prices should not be set equal to
23 economic costs. First, it would be impractical to establish a rigid rule
24 for prices to equal any specific cost standard in today's dynamic
25 telecommunications environment. Pricing must account for the cost of

1 the element plus the market, regulatory and competitive conditions
2 which exist. Pricing is not so simplistic that it can be narrowed to an
3 exact numerical exercise. Prices for unbundled network elements must
4 be based on cost, but must also provide the proper signals to, and be
5 functional in, the marketplace. For example, BellSouth is
6 recommending that virtual collocation be priced at the interstate tariff
7 rates that already exist in the marketplace. These proposed prices are
8 based on cost but also account for the fact that there is an existing tariff
9 for virtual collocation.

10

11 Second, establishing a "price equals cost" requirement ignores that this
12 proceeding addresses prices for network components of the services
13 (i.e., local interconnection and unbundled network elements) that
14 BellSouth offers. To establish a uniform "price equals cost" pricing
15 policy would require addressing all of the services offered by BellSouth,
16 including basic local exchange service, which would necessitate
17 consideration of the implications of past social pricing objectives,
18 universal service obligations and price regulation. These
19 considerations cannot be accomplished in this limited proceeding.

20

21 Third, prices should be set so that sellers and buyers have the
22 incentive to make appropriate economic choices. Finally, prices must
23 cover total costs, including incremental, common and historical costs.
24 This requirement is necessary for a firm to remain in business and for
25 all market participants to make efficient investment decisions.

1

2 Q. DOES THE ACT PROVIDE ADDITIONAL SUPPORT FOR THE
3 RECOVERY OF HISTORICAL COSTS?

4

5 A. Yes. Section 252(d) of the Act, which addresses pricing standards,
6 requires a state commission to establish a "just and reasonable" rate
7 for interconnection and unbundled network elements. Whether or not
8 the parties agree as to the appropriate cost methodology upon which
9 prices are to be based, the point remains that prices must be just and
10 reasonable. The question must then be asked: Is it just and
11 reasonable to set a price that does not cover BellSouth's actual costs?
12 The answer is an unequivocal, "No". In order for the just and
13 reasonable standard of the Act to be met, BellSouth must be able to
14 recover its actual costs, including historical costs.

15

16 Q. THERE HAS BEEN SOME CRITICISM OF BELLSOUTH'S
17 PROPOSAL TO USE EXISTING TARIFFED RATES FOR SOME
18 UNEs. PLEASE COMMENT.

19

20 A. BellSouth has priced all of its unbundled network elements at the
21 TSLRIC plus shared and common cost results with the exception of the
22 proposed loops and port which include a residual recovery requirement,
23 and virtual collocation which is proposed at the existing interstate tariff
24 rates. These exceptions are only reasonable given their
25 circumstances. The prices for the proposed loops and port do indeed

1 contain an element to recover actual historical costs. The Act does not
2 prohibit including such costs and the FCC's rules addressing historical
3 costs have been vacated.

4
5 As noted in direct testimony, virtual collocation rates already exist in
6 interstate tariffs and adoption of BellSouth's cost study results would
7 only set the stage for competitors to pick and choose from the tariff or
8 the cost study results, creating an opportunity for arbitrage. It is
9 important to note that virtual collocation will only occur in those
10 instances where BellSouth cannot support a physical collocation
11 installation due to space requirements. Further, the Act does not
12 specify a pricing standard for collocation. Based on these facts,
13 BellSouth has proposed a reasonable course of action regarding virtual
14 collocation.

15

16 Q. ARE EXISTING TARIFFS BASED ON EMBEDDED COST
17 METHODOLOGIES?

18

19 A. No. Unless otherwise directed by a state or federal Commission,
20 BellSouth has, for at least the past ten years, performed incremental
21 cost studies in support of tariff filings and not embedded cost
22 methodologies. Make no mistake - BellSouth has not advocated that
23 prices be set equal to incremental cost. The incremental cost
24 establishes only the lower bound for the price - often referred to as the
25 price floor. It is important to note, once again, that BellSouth's rate

1 proposal in this proceeding contains only one set of rates that are
2 based on existing tariff rates - virtual collocation.

3

4 Q. MR. ELLISON (PAGE 5) AND DR. SELWYN (PAGE 4) SUGGEST
5 THAT PRICES MUST BE SET AT EFFICIENT FORWARD LOOKING
6 COSTS. IN YOUR OPINION, DOES THIS METHODOLOGY
7 ADDRESS BELL SOUTH'S HISTORICAL COSTS?

8

9 A. No. Historical costs are borne by the incumbent local exchange
10 carriers ("ILECs") to maintain a ubiquitous network capable of meeting
11 all reasonable requests for service, and at least for the foreseeable
12 future, ILECs will retain carrier of last resort responsibilities. The costs
13 actually incurred to provide unbundled network elements on a going
14 forward basis will not be recovered from the users of these elements if
15 historical costs are ignored. Any proposal by the other parties that
16 does not allow BellSouth to recover its full costs is discriminatory in that
17 only BellSouth's customers bear the burden of the shortfall and ALEC
18 customers do not.

19

20 In its proposal to recover a portion of historical costs, BellSouth has
21 chosen a simple, straightforward method: 1) identify the primary area,
22 in this case investment, impacted by recognizing only forward-looking
23 incremental costs; 2) identify the primary services impacted, in this
24 case the unbundled loops and port; and, 3) calculate the impacts of
25 these elements. Because the majority of network investment is

1 associated with outside plant and switching, BellSouth has limited the
2 historical cost calculation used to help recover the shortfall (from
3 recovering only TSLRIC plus shared and common costs) to only the
4 proposed unbundled loops and unbundled port.

5

6 Historical costs are real costs that will be incurred on a going forward
7 basis and BellSouth encourages the Commission to recognize these
8 costs and include them in determining the rates for loops and ports.

9 These costs are real, and cannot simply be wished away.

10

11 Q. DOES BELLSOUTH REFER TO THE DIFFERENCE BETWEEN
12 FORWARD-LOOKING AND ACTUAL COSTS AS THE "RESIDUAL
13 RECOVERY REQUIREMENT"?

14

15 A. Yes.

16

17 Q. PLEASE EXPLAIN FURTHER WHY HISTORICAL COSTS
18 (REPRESENTED BY THE RESIDUAL RECOVERY REQUIREMENT)
19 SHOULD BE RECOVERED.

20

21 A. First, telecommunications networks, such as BellSouth's, have
22 enormous sunk costs. These networks have evolved over time using
23 technology available at the time to serve customers wherever they
24 decided to locate during the evolution of the network. In addition,
25 ALECs are today, and will be in the future, using the current network;

1 therefore, the costs being incurred today by BellSouth are the real
2 costs of that network. ALECs should pay that real cost, and not the
3 cost of an idealized, hypothetical network they are not using.

4

5 Second, if rates are always set equal to forward-looking costs, then
6 technological changes will not allow BellSouth to recover costs.

7 Technology continues to force costs down. Actual costs will always be
8 higher than the cost of the newest technology for the foreseeable
9 future. BellSouth will never be able to cover its actual costs if it always
10 has to price all of its products equal to forward-looking costs.

11

12 Third, pricing without regard to historical costs gives ALECs a free ride
13 on investment in existing networks. As I stated previously, technology
14 will continue to force costs down in the future, and, as a result, over
15 time, the actual cost of BellSouth's network will also decline. The
16 decline, however, will not be precipitous because BellSouth cannot
17 instantaneously transform its network to new technology. New
18 technology will be introduced as economically reasonable. In fact, a
19 "flash cut" to a new technology would be more costly than gradual
20 introduction because it would shorten the life of all current technology.
21 ALECs advocate pricing using new technology as if it were magically
22 "flash cut", but then want it to be treated as if it would not be replaced
23 on a "flash cut" basis by the next innovation.

24

25 Finally, such a situation would allow an ALEC to use the ILEC's

1 network without having to bear historical costs that would arise if the
2 ALEC were to build and use its own network. If an ALEC were to build
3 its own network, or purchase from another provider, it would have to
4 pay for historical costs. The bottom line is that ALECs are requesting
5 from the Commission a better deal than they could possibly expect in a
6 competitive marketplace.

7

8 Q. IN SIMILAR PROCEEDINGS, PARTIES CLAIM THAT BELLSOUTH'S
9 APPLICATION OF THE RESIDUAL RECOVERY REQUIREMENT
10 ONLY ON LOOPS AND PORTS RESULTS IN A DISCRIMINATORY
11 PRICING STRUCTURE. DO YOU AGREE?

12

13 A. No. As stated earlier, BellSouth identified the network elements that
14 were significantly impacted by a difference between forward-looking
15 costs and actual costs. In Florida, the proposed loops and 4-wire
16 analog port were significantly impacted. If rates are set to recover the
17 economic cost of the unbundled loop or port as well as the residual
18 recovery requirement, all ALECs ordering unbundled loops and ports
19 will pay the same rate. They will also be incurring the same costs that
20 BellSouth incurs, therefore, I fail to see how this pricing structure is
21 discriminatory.

22

23 In similar proceedings, witnesses have claimed that BellSouth is only
24 applying the residual recovery requirement to monopoly elements -- in
25 other words, BellSouth is only "marking up" those elements that are not

1 competitive. Contrary to such assertions, BellSouth has proposed to
2 include the residual recovery requirement in prices only for those
3 elements where the difference between TSLRIC plus shared and
4 common costs and actual costs is significant.

5

6 Q. DON'T HISTORICAL COSTS SIMPLY REFLECT THE LEC'S
7 REVENUES UNDER RATE-OF-RETURN REGULATION.

8

9 A. No. The rates proposed by BellSouth reflect, where appropriate, the
10 difference between forward-looking costs and actual costs for all of the
11 reasons previously discussed. Revenues have no bearing at all on
12 BellSouth's rate proposal. Indeed, if BellSouth were attempting to
13 develop rates reflective of revenue requirements, it would be necessary
14 to include a portion of the shortfall generated by basic residential
15 exchange access rates which are currently priced significantly below
16 cost for universal service purposes. No consideration of revenue
17 requirement entered into the rate development.

18

19 Q. BELLSOUTH HAS BEEN CRITICIZED IN SIMILAR PROCEEDINGS
20 FOR LACKING INCENTIVE TO OPERATE EFFICIENTLY UNDER
21 RATE OF RETURN REGULATION. ARE SUCH CRITICISMS WELL
22 FOUNDED?

23

24 A. No. BellSouth is running a business, and one of its primary goals has
25 always been to operate efficiently. Further, this Commission has

1 always had the duty to ensure that BellSouth operated efficiently and
2 the authority to disallow any expenditures that it determined were not
3 the result of prudent business decisions. In Florida, prior to coming
4 under price regulation in January 1996, BellSouth operated under an
5 incentive regulation plan for several years. Under all types of
6 regulation, BellSouth has been required to operate efficiently.

7

8 Again, let me stress that BellSouth is simply attempting to recover its
9 actual costs associated with providing these unbundled network
10 elements. These costs are real, and cannot simply be wished away.

11

12 Q. MR. ELLISON'S PRICE EXHIBIT DEMONSTRATES THAT AT&T IS
13 PROPOSING ITS NONRECURRING RATES BASED ON AN
14 ASSUMED "MIGRATION" OF A CUSTOMER FROM AT&T TO
15 BELLSOUTH. MR. LYNOTT CONFIRMS THIS USE OF MIGRATION
16 IN SUPPORTING AT&T AND MCI'S NON-RECURRING COST
17 MODEL. WHAT IS WRONG WITH THIS ASSUMPTION?

18

19 A. Mr. Ellison and Mr. Lynott assume incorrectly that "migration" of the
20 customer from BellSouth to AT&T or MCI can be accomplished by
21 provision of UNEs. Migration of a customer only occurs in a resale
22 environment, not when an ALEC orders unbundled elements, and is
23 therefore not appropriate discussion for this proceeding. According to
24 the Eighth Circuit, the 1996 Act, "does not permit a new entrant to
25 purchase the incumbent LEC's assembled platform(s) of combined

1 network elements (or any lesser existing combination of two or more
2 elements) in order to offer competitive telecommunications services.”
3 The Eighth Circuit found that ALECs can combine unbundled network
4 elements in any manner they choose. The Court was very specific,
5 however, to state that requesting carriers will combine the unbundled
6 elements themselves.

7
8 The Eight Circuit made clear that the arguments put forth by AT&T and
9 others, that BellSouth is required to combine UNEs for ALECs, does
10 not hold water. As a result, AT&T now argues that ILECs like
11 BellSouth must permit the “efficient recombination of elements” and
12 must “provide existing network element combinations to new entrants
13 without disruption.” The Eighth Circuit, however, did not qualify its
14 ruling in that or any other manner, but only found that ILECs such as
15 BellSouth should provide unbundled elements to ALECs for ALECs to
16 combine. It is, therefore, the ALEC’s responsibility to combine UNEs,
17 and in doing so, to determine what is efficient for that ALEC.

18

19 Q. PLEASE EXPLAIN HOW AT&T AND MCI’S NON-RECURRING COST
20 MODEL CONTINUES TO SUPPORT THE “PLATFORM” APPROACH
21 WHICH THE EIGHTH CIRCUIT HAS TWICE REJECTED?

22

23 A. The Non-recurring Cost Model proposed by AT&T and MCI and
24 supported by Dr. Selwyn assumes conversion of an existing service to
25 unbundled network elements, which BellSouth has combined for the

1 ALEC, with little or no human intervention. This is entirely incorrect,
2 because for example, connecting UNE loops to an ALEC requires, at a
3 minimum, activity to physically move connection of the loop from the
4 existing connections at BellSouth's switch to the ALEC's connecting
5 facility. Thus, the model's assumption of 98% flow through is invalid on
6 its face. As I noted earlier, such an assumption includes migration of
7 an existing customer which is a resale function and not an appropriate
8 assumption for the provision of UNEs.

9
10 I wish to make clear that, if an ALEC orders unbundled elements,
11 BellSouth will provide them in a manner that allows the ALEC to
12 combine them. If, however, AT&T, MCI or any other ALEC wishes to
13 migrate a customer's service on a "switch as is" basis which does not
14 involve disruption of a customer's service, this can be done through
15 resale. BellSouth is willing and able to transition existing services to
16 an ALEC on a "switch as is" basis, and in doing so, BellSouth will bill
17 the ALEC for the retail service minus the applicable wholesale discount.

18

19 Q. DOES THE FCC'S RECENT ACCESS REFORM DECISION HAVE
20 ANY IMPACT ON THE ISSUE OF NETWORK ELEMENT
21 COMBINATIONS?

22

23 A. No. In its recent access reform decision, all the FCC did was reaffirm
24 its rule that access charges should not apply to unbundled elements. It
25 did not reaffirm that recombined elements should be offered. As I

1 stated earlier, the Eighth Circuit vacated the FCC Rules that prohibited
2 charging access on unbundled elements and that purported to require
3 BellSouth to provide combined network elements. The fact that the
4 FCC has resurrected this access charge position under access reform
5 has no bearing on this proceeding.

6

7 Q. DOES THE RECENT FCC ORDER ON THE AMERITECH/MICHIGAN
8 271 APPLICATION HAVE ANY IMPACT ON THIS PROCEEDING?

9

10 A. No. There is nothing in the Ameritech Order that is binding on the
11 Commission. The FCC provided its opinions concerning the
12 appropriateness of Ameritech's application; however, those opinions
13 should not be misconstrued as rules. The Commission is not required
14 to follow any of those opinions. Indeed, state commissions, including
15 this Commission were at the forefront in challenging the FCC to
16 preserve their right to act in the best interest of consumers. The Eighth
17 Circuit gave state commissions that right. Other parties would now
18 have the Commission abdicate that right to the FCC. The Ameritech
19 Order is an attempt by the FCC to reimpose the same rules and
20 requirements on the states that the Eighth Circuit very recently told the
21 FCC that it did not have the authority to impose. In fact, the Eighth
22 Circuit issued a second order on October 14, 1997 that mandates that
23 the FCC comply with the Court's July 18, 1997 decision that intrastate
24 pricing authority rests with the state commissions.

25

1 The Commission still has sole authority to establish appropriate rates
2 for UNEs and interconnection in Florida. The issue of what the FCC
3 can require for interLATA relief will be addressed between the FCC and
4 BellSouth when an interLATA application is filed. The Florida
5 Commission's ability to establish prices in this proceeding is in no way
6 impacted by the FCC's recent Order. The Commission has the
7 authority to establish prices that recover actual costs, including
8 historical costs.

9

10 Q. MR. BISSELL AND MR. KLICK DISCUSS PROVISIONING AND
11 COSTING OF COLLOCATION. WHAT OBLIGATIONS DOES THE
12 ACT IMPOSE ON ILECs CONCERNING PROVISIONING OF
13 COLLOCATION?

14

15 A. Section 251(c)(6) of the Act specifies that "the duty to provide, on rates,
16 terms and conditions that are just, reasonable, and nondiscriminatory,
17 for physical collocation of equipment necessary for interconnection or
18 access to unbundled network elements at the premises of the local
19 exchange carrier, except that the carrier may provide for virtual
20 collocation if the local exchange carrier demonstrates to the State
21 commission that physical collocation is not practical for technical
22 reasons or because of space limitations."

23

24 Q. DOES THE ACT SPECIFY A PRICING STANDARD FOR
25 COLLOCATION?

1

2 A. No. The pricing standards specified in the Act relate to Sections
3 251(c)(2) and 251(c)(3); therefore, no standard is specified for the
4 pricing of collocation. BellSouth has provided the Commission with
5 forward-looking studies for both physical and virtual collocation.
6 BellSouth has proposed rates for physical collocation that are equal to
7 economic costs. As described earlier in my testimony, the rates being
8 proposed for virtual collocation are the existing FCC tariff rates.

9

10 Q. DOES BELLSOUTH'S PHYSICAL COLLOCATION STUDY
11 OVERSTATE THE FORWARD-LOOKING COSTS?

12

13 A. No. Testimony filed by opposing parties proposes that the appropriate
14 cost methodology for collocation should be based on a hypothetical
15 central office building designed so that collocators would always be
16 physically located in close proximity to BellSouth's main frame. There
17 is absolutely no basis in the Act or in any valid FCC Rules to support
18 this methodology.

19

20 When intervenors collocate, they will do so in existing buildings and use
21 space where it is available in those buildings. They will not be
22 collocated in their hypothetical building. Even though they want to act
23 as if the existing building has been demolished, they include no
24 provisions for recovering the remaining costs of the existing building or
25 demolishing it. In fact, the methodology proposed by the intervenors is

1 contrary to the requirements of the Act because the Act specifically
2 states that physical collocation is to be provided at the premises of the
3 local exchange carrier. It is ludicrous to propose that the appropriate
4 cost methodology for collocation would ignore the incumbent's current
5 central office configurations.

6

7 Additional support for BellSouth's position is found in the FCC's Rules
8 at paragraph 51.323 which provides the standards for physical and
9 virtual collocation. Under this section, paragraph (f)(1) states the
10 following:

11

12 "An incumbent LEC shall make space available within or on its
13 premises to requesting telecommunications carriers on a first-
14 come, first-serve basis, provided, however, that the incumbent
15 LEC shall not be required to lease or construct additional space to
16 provide for physical collocation when existing space has been
17 exhausted."

18

19 Additionally, paragraph (f)(3) states that:

20

21 "When planning renovations of existing facilities or constructing or
22 leasing new facilities, an incumbent LEC shall take into account
23 projected demand for collocation of equipment."

24

25 It is obvious from these rules that the FCC and the Act envisioned

1 physical collocation arrangements being constructed in the ILEC's
2 existing central office buildings, taking into account the existing
3 physical configuration of BellSouth's equipment. Obviously, prices for
4 collocation should be based on that same configuration, not the
5 hypothetical one posited by AT&T and MCI.

6

7 Q. AT&T HAS SUGGESTED THAT AT&T'S PORT PRICES INCLUDE
8 THE PRICE OF SWITCHING FEATURES AND FUNCTIONS. DO
9 YOU AGREE?

10

11 A. No. AT&T significantly understates the price of local switching. In fact,
12 the Hatfield Model, which AT&T typically relies upon for developing its
13 port prices, can only produce a high level cost calculation for local
14 switching that bears little resemblance to actual cost. It is incapable of
15 disaggregating switching in order to produce specific costs that include
16 local switching and features such as BellSouth has done. Indeed, in
17 the Hatfield model, the cost of switching appears to be the same
18 whether a customer uses all of the features or none of them. This is
19 inaccurate.

20

21 As noted in Mr. Ellison's price exhibit, AT&T will only recommend rates
22 for the 4-wire analog port after reviewing BellSouth's cost study results.
23 In the event that Mr. Ellison makes a downward adjustment to
24 BellSouth's 4-wire analog port study to develop AT&T's port price, he
25 will do so by totally ignoring the costs BellSouth incurs for provision of

1 vertical features.

2

3 By contrast BellSouth has developed a recurring 4-wire analog switch
4 port cost of \$11.14, which represents the cost of switching without any
5 cost of vertical features. BellSouth has also developed recurring costs
6 totaling \$6.18 for the features that are compatible with a 4-wire analog
7 port. Provision of the 4-wire analog switch port with all available
8 features requires that BellSouth cover the cost of the port and the
9 features, resulting in its proposed monthly recurring price of \$17.32.
10 Any price set at a lesser level will not allow BellSouth to recover its
11 actual costs.

12

13 Q. IS BELLSOUTH'S APPROACH CONSISTENT WITH THE FCC'S
14 REQUIREMENTS?

15

16 A. Yes. The approach BellSouth is proposing is consistent with the FCC's
17 requirements. In its August 8, 1996 Interconnection Order, the FCC
18 concluded that, "...the local switching element includes all vertical
19 features...". (paragraph 412). The FCC's Order, however, goes on to
20 say that, "At this time we decline to require further unbundling of the
21 local switch into a basic switching element and independent vertical
22 feature elements." (emphasis added, paragraph 414). The FCC further
23 states, "In addition, the record indicates that the incremental costs
24 associated with vertical switching features on a per-line basis may be
25 quite small, and may not justify the administrative difficulty for the

1 incumbent LEC or the arbitrator to determine a price for each vertical
2 element. Thus, states can investigate, in arbitration or other
3 proceedings, whether vertical switching features should be made
4 available as separate network elements". (footnote omitted, paragraph
5 414)

6
7 Q. DOES BELLSOUTH'S PROPOSAL FOR UNBUNDLED LOCAL
8 SWITCHING COMPART WITH THE EIGHTH CIRCUIT'S DECISION?

9
10 A. Yes. The Eighth Circuit's decision and the FCC's Third Order on
11 Reconsideration appear to more clearly define what BellSouth is
12 obligated to offer under the Act. As a result of these Orders, BellSouth
13 has analyzed its obligations under the Act and determined that
14 BellSouth is only required to offer a port with all compatible features for
15 which it has provided cost studies. For this reason, BellSouth is not
16 required to offer individual vertical features on a stand alone basis.
17 BellSouth, therefore, offers its 4-wire analog port for \$17.32 including
18 all available features.

19
20 Q. PLEASE DESCRIBE YOUR GENERAL OBSERVATIONS
21 CONCERNING DR. SELWYN'S TESTIMONY AND ATTACHED
22 "WHITE PAPER".

23
24 A. Dr. Selwyn's testimony serves primarily as an introduction to his paper
25 entitled, *Regulatory Treatment of ILEC Operations Support Systems*

1 Costs which I will refer to as the "white paper". His white paper,
2 purporting to address ILEC arguments concerning Operations Support
3 Systems ("OSS") cost recovery, arrives at four conclusions. Of his four
4 conclusions, the first is irrelevant to the issues in this proceeding and
5 the last three are simply erroneous. As opposed to a point by point
6 rebuttal of his testimony and white paper, I will limit my comments to his
7 four broad conclusions.

8
9 Q. WHAT IS DR. SELWYN'S FIRST CONCLUSION AND WHY IS IT
10 IRRELEVANT TO THIS PROCEEDING?

11
12 A. Dr. Selwyn concludes, "Most, if not all, of the "costs" that ILECs claim
13 are being imposed upon them by the Act and associated federal and
14 state implementation regulations represent efficiency improvement
15 programs that either were already underway prior to the enactment or
16 should be pursued by ILECs irrespective of the presence of
17 competitors or any specific Section 251(c) obligations." Much of Dr.
18 Selwyn's white paper is devoted to this conclusion. His discussion
19 makes it very clear that the costs he refers to are for those OSS
20 "network management tools whose purpose is to improve the overall
21 efficiency of ILEC operations and quality of ILEC services and
22 performance" (page 6). This, however, is an irrelevant conclusion.
23 BellSouth is not proposing to recover from ALECs the costs associated
24 with its operations support systems and processes either currently in
25 place or planned that support provision of services to its end user

1 customers. BellSouth is only proposing to recover the costs of the
2 electronic interfaces that provide access to BellSouth's internal systems
3 by ALECs. The majority of the white paper contents are, therefore,
4 devoted to a non-issue.

5
6 Q. DR. SELWYN'S SECOND CONCLUSION STATES, "COSTS
7 INCURRED BY ILECs IN ORDER TO ACCOMMODATE THEIR
8 OPERATION IN A MULTI-CARRIER ENVIRONMENT, SUCH AS THE
9 COSTS OF ESTABLISHING AND OPERATING ELECTRONIC
10 INTERFACES WITH OTHER LOCAL EXCHANGE CARRIERS, ARE
11 NOT COMPLIANCE-DRIVEN COSTS." PLEASE COMMENT.

12
13 A. Dr. Selwyn is incorrect. He argues that these same type of electronic
14 interface costs are also incurred by the ALECs and are the necessary
15 costs of doing business in a multi-carrier marketplace. He appears to
16 believe that just because the ALECs incur some cost to use the
17 electronic interfaces, they should not have to bear the cost to develop
18 and implement them, even though the ALECs are the beneficiaries of
19 the interfaces. Taken to its logical conclusion, this assertion would
20 mean that ALECs should not be charged for any UNEs.

21
22 First, the cost to develop and implement the electronic interfaces at
23 issue are real costs that BellSouth has proven to have occurred.
24 These costs have been caused by the entrance of new local service
25 providers into the local exchange marketplace. They would not have

1 occurred otherwise. As such, if BellSouth is unable to recover these
2 costs from the cost causers (ALECs), they will have to be recovered
3 from other customers, namely BellSouth's end users. BellSouth's end
4 user customers, however, will not use nor receive benefit from these
5 electronic interfaces. In effect, what Dr. Selwyn proposes is that
6 BellSouth's end users subsidize ALECs' entry into the local market
7 such that ALECs gain the ability to access those very customers. From
8 another perspective, his proposal means BellSouth pays twice, once to
9 develop the OSSs that are internally used for its own end users and
10 again to pay for the ALEC's access to these OSSs.

11
12 Next, the electronic interfaces which allow ALECs to access
13 BellSouth's internal systems are considered unbundled network
14 elements. As such, they fall under the pricing standards of the Act
15 which allow for cost recovery by BellSouth. To ignore this basic right to
16 recover cost incurred by the ALECs is to be in violation of the Act.

17
18 Finally, companies such as AT&T and MCI that sell their services
19 through resellers surely recover their costs of serving resellers through
20 the prices they charge resellers. Yet, they argue that BellSouth should
21 not be allowed to recover similar costs from ALECs.

22
23 Q. PLEASE COMMENT ON DR. SELWYN'S THIRD CONCLUSION THAT
24 STATES, "TO THE LIMITED EXTENT THAT ANY *POSITIVE*
25 COMPLIANCE COSTS MAY BE INCURRED BY ILECS ALONE,

1 THESE SHOULD BE RECOVERED ACROSS THE ENTIRE
2 COMMUNITY OF ILEC CUSTOMERS, AND NOT BE IMPOSED
3 EXCLUSIVELY UPON CLECS AND RESELLERS.”

4
5 A. Dr. Selwyn's third conclusion is also erroneous. Some how, Dr. Selwyn
6 makes an unfounded leap, suggesting that because Congress intended
7 to bring the benefits of competition to all consumers, Congress
8 intended that ILEC consumers should foot the bill. To support his
9 position, Dr. Selwyn employs an “apples and oranges” analogy by
10 suggesting that, when the Americans with Disabilities Act was passed,
11 existing hotels and restaurants could not impose their compliance costs
12 on new hotels and restaurants. While Dr. Selwyn is correct that they
13 could not impose those costs on their competitors, he conveniently
14 ignores that they did not have to develop anything for their competitors
15 either. Further, existing hotels and restaurants were not required to
16 make their reservations systems, housekeeping services and staffs,
17 food service facilities and administrative services available to the new
18 entrants based on cost. BellSouth is already providing interconnection
19 and UNEs at cost based rates to ALECs. BellSouth should not also
20 have to subsidize ALECs' entry into the business, as Dr. Selwyn
21 proposes.

22
23 Q. PLEASE ADDRESS DR. SELWYN'S FOURTH CONCLUSION.

24
25 A. Dr. Selwyn's fourth conclusion which is also related to his second and

1 third conclusions, suggests that those OSS related costs found to be
2 recoverable by the ILEC, should be spread over ILECs and competitors
3 using forward looking economic cost. First, as noted previously,
4 BellSouth's end users should not bear the cost of ALEC entry into the
5 local exchange marketplace. Next, Dr. Selwyn seems to imply that
6 BellSouth's cost studies are not forward looking. This is simply
7 incorrect. BellSouth's studies are forward looking using the most
8 efficient technology currently available as described by Ms. Caldwell
9 and Mr. Zarakas. In addition, BellSouth applies an appropriate level of
10 shared and common cost as described by Mr. Walter Reid. BellSouth
11 has priced its electronic interfaces at the minimum level that allows it to
12 recover those costs.

13

14 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

15

16 A. Yes.

17

18

19

20

21

22

23

24

25

1 **MR. LACKEY:** Mr. Varner, Do you have less
2 than a 10-minute summary of your direct and rebuttal
3 testimony?

4 **A** Yes.

5 **Q** Would you please give it?

6 **A** All right. Good morning. The purpose of my
7 testimony is to outline BellSouth's proposed prices
8 for unbundled network elements and interconnection.

9 In my testimony I explain why BellSouth's
10 approach to setting these prices is appropriate.
11 There are numerous witnesses scheduled to appear in
12 this proceeding, and in an effort to place all of this
13 in some sort of a manageable framework, I want to
14 outline our position a little bit and tell you a
15 little bit about what our witnesses will be sharing
16 with you.

17 BellSouth and its predecessors have been in
18 the telephone business for a long time. As part of
19 our ongoing provision of telephone service, we've had
20 to determine what our cost of various services and
21 pieces of the network are.

22 Over the years we developed cost models and
23 processes that served us fairly well. Were these
24 processes understandable to lay people? Probably not,
25 but there was no need for them to be.

1 With the introduction of competition into
2 the telecommunications industry and the passage of the
3 Telecom Act, cost and cost studies took on a whole new
4 perspective. Suddenly incumbent local telephone
5 companies were required to sell bits and pieces of
6 their network to potential competitors at just and
7 reasonable prices which had to be based on cost, and
8 which might include a reasonable profit.

9 No definition of cost was provided in the
10 Act, however, and a considerable debate is raised over
11 what the appropriate costs should be.

12 You're going to hear a lot of discussion
13 about costs. In fact, most of the testimony in this
14 proceeding will concern costs. However, the purpose
15 of this proceeding is to establish just and reasonable
16 prices. That's what the Act requires. Those just and
17 reasonable prices must be based on cost, but they do
18 not necessarily have to be equal to cost.

19 BellSouth simply proposes that a just and
20 reasonable price should allow the firm to recover its
21 actual cost. Such prices should allow for recovery of
22 incremental costs, or forward-looking costs, shared,
23 common and historical costs.

24 Determining just and reasonable prices is
25 the principal objective of this proceeding. That

1 objective should be kept in mind as we slog through
2 the details of cost models and cost inputs. This
3 proceeding is not a search for the perfect cost study,
4 but a search for just and reasonable prices.

5 Let me tell you what all of us generally
6 agree to. We all agree that in determining the cost
7 of a particular network element or pieces of the
8 network, that we ought to determine the cost that an
9 efficient firm using the least cost, most
10 forward-looking technology would incur.

11 Beyond that, we don't agree on very much.
12 We don't agree on the type of model that should be
13 used to do that, nor do we agree on the inputs that
14 should go into the various models.

15 You'll be asked to reconcile the difference
16 in the proposed rates to decide which cost methodology
17 is more accurate and, importantly, which inputs are
18 more accurate. The evidence BellSouth will present
19 will demonstrate that BellSouth's cost methodology for
20 unbundled network elements and resulting prices are
21 the lowest prices that should be established in
22 Florida.

23 Now I would like to discuss in detail a few
24 specific points about these matters. To begin, I
25 would like to briefly describe the process used by

1 BellSouth to establish prices.

2 For unbundled elements, the basic approach
3 was to set prices equal to the actual cost incurred to
4 provision the elements. This is the lowest price that
5 can be offered which would be consistent with sound
6 business practices. This is the lowest price
7 competitors will receive from other providers in a
8 competitive marketplace.

9 We propose prices at this level to support
10 the development of competition. We have used actual
11 costs to establish prices. This is what we believe
12 the Telecom Act allows and, in fact, requires. The
13 Telecom Act says prices should be just and reasonable,
14 be based on cost, and may include a reasonable profit.

15 This clearly mandates that full, actual
16 costs would be recovered in our prices. If Congress
17 had not intended that full, actual cost be recovered,
18 it would not have made provisions for prices to
19 include a profit.

20 In addition to cost, prices must account for
21 regulatory mandates and marketplace realities. That's
22 one of the reasons why any rigid rule of setting
23 prices equal to cost in all cases would be unsound.

24 For a few network elements, that is those
25 included in virtual collocation, prices could not be

1 set equal to cost. Virtue collocation enables ALECs
2 to connect to equipment in our offices. A tariff
3 already exists for virtual collocation in Florida.
4 And the cost studies on some elements dictate a higher
5 price. Setting another price at this higher level
6 would be fruitless since competitors would simply
7 purchase service from the existing tariff.
8 Consequently, the existing tariff rates were proposed.

9 For all of the remaining elements, however,
10 the objective was to set prices equal to actual casts.
11 There have been many assertions that BellSouth is
12 proposing prices equal to revenue requirements.
13 That's simply not true.

14 It is true, however, that for loops and
15 ports we have ensured that prices equal the actual
16 costs we incur today and expect to incur in the
17 future. For all of the remaining elements, prices
18 were equal to incremental costs.

19 As I mentioned, all parties agree that
20 forward-looking cost is the appropriate standard to
21 use as a basis for pricing decisions. This does not
22 mean that prices must equal those costs, but certainly
23 prices should not be below forward-looking costs.

24 **CHAIRMAN JOHNSON:** Could you go back? You
25 said for loops and ports you set them based on the

1 cost today, and then you said something else, and --

2 **WITNESS VARNER:** And expect to incur in the
3 future; the costs we actually incur today, and
4 actually expect to incur in the future.

5 **CHAIRMAN JOHNSON:** Thank you.

6 **WITNESS VARNER:** The difference between
7 BellSouth and the other parties is how to quantify
8 these costs.

9 BellSouth proposes to use the cost of
10 equipment that we will actually use to provide these
11 elements in the future. Other parties propose to use
12 the cost of imaginary equipment that will not be used
13 and won't even exist in many cases.

14 To illustrate this example, I'll use the
15 example of physical collocation. First, let me give a
16 brief description of what that is.

17 BellSouth has central offices throughout
18 Florida. For example, let's use the Miami/Hialeah
19 office. Other parties are able to put their equipment
20 in that office. That's physical collocation, putting
21 their equipment in our buildings in separated space
22 from the rest of the equipment.

23 Other parties will ask you to ignore the
24 fact that the Hialeah building even exists. They want
25 you to assume that they will occupy a new building

1 designed for the purpose of minimizing collocators'
2 costs. They also want to assume that we won't have to
3 build a safe environment.

4 The reality is that they will be getting
5 space in the existing Hialeah office. They're not
6 getting space in their imaginary buildings that don't
7 even exist. Their only purpose for developing a cost
8 for this imaginary building is to get space at the
9 Hialeah central office at a cheaper price.

10 The same disparity exists for virtually all
11 the prices they're proposing; that is, the subloop
12 unbundling, the use of computers, any other prices
13 they propose. They want you to price unbundled
14 elements as if they were still bundled but the cost to
15 be based on arrangements that will only exist in their
16 minds. BellSouth is proposing prices based on
17 equipment that ALECs will actually be using.

18 Both approaches are forward-looking, but one
19 approach is real and the other approach is surreal.
20 It's obvious that BellSouth's proposal, which bases
21 price on the cost of equipment that will actually be
22 used, is the most sensible.

23 Now, I mentioned before that the prices of
24 loops and ports depart from the price equals
25 forward-looking cost formula. I want to briefly

1 explain why. As I said, our objective is to recover
2 the actual cost of these elements, just as any
3 business would do.

4 For network elements other than loops and
5 ports, the difference between actual and
6 forward-looking costs does not appear to be
7 significant. This is not true for loops and ports,
8 because these elements have a much higher component of
9 long-lived plan investment.

10 **COMMISSIONER CLARK:** I'm sorry. Would you
11 go back to what you said about there's not a
12 significant difference between --

13 **WITNESS VARNER:** Between the actual costs
14 and the forward-looking costs.

15 **COMMISSIONER CLARK:** For what elements?

16 **WITNESS VARNER:** Everything other than the
17 loops and ports. The subloop unbundling; and the
18 subloop bundling has the loop element.

19 **COMMISSIONER CLARK:** So you all agree on the
20 prices for those?

21 **WITNESS VARNER:** We don't agree on the
22 prices. We set the prices equal to forward-looking
23 costs. Where we disagree is on what the
24 forward-looking -- how the forward-looking costs
25 should be determined.

1 **COMMISSIONER CLARK:** Okay.

2 **CHAIRMAN JOHNSON:** But with loops and ports
3 you don't set the price equal to forward-looking
4 costs.

5 **WITNESS VARNER:** Right. We actually add an
6 element, which I identify as a residual recovery
7 requirement, to reflect the difference between actual
8 and forward-looking. So for those items, not only do
9 we disagree on the forward-looking, we disagree on the
10 addition of the residual recovery requirement.

11 **CHAIRMAN JOHNSON:** Let me ask you a
12 question. Would that residual recovery requirement --
13 you don't even see that as a forward-looking cost
14 methodology? You don't --

15 **WITNESS VARNER:** No. I don't even argue
16 that.

17 **CHAIRMAN JOHNSON:** Okay.

18 **WITNESS VARNER:** No. That is added to the
19 forward-looking cost to bring the forward-looking cost
20 to an actual cost.

21 **CHAIRMAN JOHNSON:** Okay.

22 **WITNESS VARNER:** But we have to recover the
23 actual cost, including this residual recovery
24 requirement. These costs can't be just wished away.
25 And the fact that this network exists benefits the

1 ALECs as well.

2 We're not proposing that other parties pay
3 all of our historical costs, just a reasonable portion
4 related to their use of loops and ports.

5 Now, who's harmed if BellSouth doesn't cover
6 its actual cost through prices proposed in this
7 proceeding? End users are harmed. Setting prices
8 that do not cover full costs establishes a --

9 CHAIRMAN JOHNSON: Mr. Varner, let me ask
10 you another question. What's the difference between
11 historic costs and your --

12 WITNESS VARNER: Residual recovery --

13 CHAIRMAN JOHNSON: And your book costs, yes.
14 You know, I thought that --

15 WITNESS VARNER: Okay.

16 CHAIRMAN JOHNSON: And off the --

17 WITNESS VARNER: No, they're not the same.

18 CHAIRMAN JOHNSON: They are not the same.

19 WITNESS VARNER: No. What we've done, you
20 have embedded costs, which are like the book costs,
21 which are actually the costs you have incurred on your
22 books; and it reflects things such as the actual
23 depreciation life that you've used, your actual cost
24 of money that you've used and so forth.

25 What we've done is we've determined,

1 developed the actual cost for utilizing those,
2 utilizing the investment levels, but utilizing
3 forward-looking depreciation and forward-looking cost
4 of money to determine the actual cost, but utilizing
5 the investments that we have actually incurred.

6 Next I think I want to turn to the issue of
7 deaveraged loop prices; that is, charging different
8 prices for loops in different geographic areas.

9 BellSouth believes deaveraging of unbundled
10 loop prices will necessitate dramatic rebalancing of
11 retail prices as well. Until such time as an
12 appropriate universal service plan and rebalancing of
13 retail prices can be accomplished that reflect for the
14 anomaly in the difference between unbundled network
15 elements' prices and retail prices, the Commission
16 should not implement deaveraging of unbundled network
17 elements.

18 Such deaveraging simply allows the CLECs to
19 unfairly siphon the support that allows residence
20 rates to be as low as they are. This is just another
21 attempt by the ALECs to get low prices and force
22 higher prices eventually on residential customers.

23 In conclusion, you have the authority to set
24 prices at levels that ALECs would expect to see in a
25 competitive marketplace. The Act requires that those

1 prices be just and reasonable. BellSouth simply
2 proposes that prices that are set equal to its actual
3 costs are just and reasonable prices.

4 That's what we propose. Our prices are
5 Florida-specific, and they're based on data for
6 equipment that will be used by the ALECs. Recovery of
7 these costs is the minimum level of prices that ALECs
8 could expect. These are the minimum prices that could
9 be charged to prevent harm to end users, whom the
10 ALECs seem to ignore.

11 I ask you to approve them to provide a fair
12 basis for the development of local competition in
13 Florida. And that concludes my summary.

14 **CHAIRMAN JOHNSON:** Thank you.

15 **COMMISSIONER CLARK:** Madam Chair, before I
16 forget these things. I wanted to ask you, on virtual
17 collocation you recommend using the existing tariff.

18 **WITNESS VARNER:** Yes.

19 **COMMISSIONER CLARK:** Is that a federal
20 tariff or a state tariff?

21 **WITNESS VARNER:** Actually, they're both.
22 There is a federal tariff and there is a Florida
23 tariff for virtual collocation, and the rates are the
24 same. There is one element that's in the Florida
25 tariff. It's a DSO level cross-connect. That's not

1 in the federal tariff.

2 **COMMISSIONER CLARK:** Is there arbitrage
3 going on between those two, then?

4 **WITNESS VARNER:** Well, rates are the same.

5 **COMMISSIONER CLARK:** Oh. I got you. You
6 mean the end result is --

7 **WITNESS VARNER:** Yeah, the end results.

8 **COMMISSIONER CLARK:** And that was for
9 interexchange service, right?

10 **WITNESS VARNER:** Yes. That was for IXCs to
11 purchase virtual collocation.

12 **COMMISSIONER CLARK:** And you recommend using
13 those, and I gather your sort of justification is,
14 well, they're there, we've had them, and we don't want
15 arbitrage, so we should use them.

16 **WITNESS VARNER:** It's a little bit more than
17 that. That is one of the principal reasons for doing
18 that is they're there. People have the opportunity to
19 purchase out of that tariff. ALECs can purchase out
20 of that tariff.

21 So we have done the cost studies, and on my
22 exhibit I show what the costs are for virtual
23 collocation, and if we were to propose prices equal to
24 costs, you could see how they match up with what's in
25 that tariff. Some are higher, some are lower. If we

1 were to propose --

2 **COMMISSIONER CLARK:** Wait a minute. Some
3 are higher, some are lower?

4 **WITNESS VARNER:** Yes.

5 **COMMISSIONER CLARK:** Meaning for particular
6 locations.

7 **WITNESS VARNER:** Particular elements.
8 There's several elements, like you have an application
9 fee, space construction, space rental, so forth; and
10 some of the prices may be -- I can't remember which
11 are which. But let's say the application fee may be
12 higher in the tariff than it is in the cost study, and
13 the space rental may be lower the tariff than it is in
14 the cost study.

15 **COMMISSIONER CLARK:** Right. But it's your
16 position that those existing tariffs comply with the
17 requirement of the Act?

18 **WITNESS VARNER:** Yes. The Act requires that
19 it just be just and reasonable prices for collocation.
20 The standard in the Act that requires prices based on
21 cost does not apply to collocation.

22 **COMMISSIONER CLARK:** Well, Mr. Varner, I
23 guess I view just and reasonable as including that
24 they're based on cost. And my question is, is it your
25 testimony that these are, in fact, cost-based?

1 **WITNESS VARNER:** Yes. Well, they were based
2 on costs at the time that they were filed.

3 **COMMISSIONER CLARK:** How are we sure that
4 they are based on costs now? When were they filed?
5 How old are they? I suppose that's the real --

6 **WITNESS VARNER:** About 1994 is when they
7 were filed.

8 **COMMISSIONER CLARK:** Let me just indicate to
9 you that it seems to me that if you want to avoid
10 arbitrage, one of the ways to do it is that you set
11 the rates here on what the appropriate costs are
12 demonstrated to be, and then you change your tariffs
13 for the other ones.

14 **WITNESS VARNER:** Well, we've looked at that,
15 and one of the problems with that is this: We could
16 do that with the Florida tariff, file a new Florida
17 tariff that agrees with these rates. However, the
18 interstate tariff is a region-wide tariff. It's the
19 same price. It's only one tariff, and it's applicable
20 to all nine BellSouth states.

21 So if we were to adopt this one in Florida,
22 and let's say another Commission decided to do the
23 same thing, there is no way we could make it match up
24 with both commissions, because it's one tariff for all
25 nine states.

1 **COMMISSIONER CLARK:** Do you have to have a
2 tariff that applies to all your regions? I would
3 presume that's not a requirement; that you can have
4 tariffs that are state specific.

5 **WITNESS VARNER:** We -- and I don't
6 remember -- at one time we did have state-specific
7 access tariffs, and then we went to regional tariffs.
8 What I cannot remember is whether something has
9 changed such that we can go back to state specific
10 tariffs or not.

11 **COMMISSIONER CLARK:** Let me phrase it in
12 another way. Is that a business decision on your
13 part, or is it a requirement of federal or --

14 **WITNESS VARNER:** That I don't know.

15 **COMMISSIONER CLARK:** The other question I
16 had is on your residual revenue -- what did you --

17 **WITNESS VARNER:** Residual recovery
18 requirement, triple R.

19 **COMMISSIONER CLARK:** Okay. And explain to
20 me again why you chose only those two elements. Why
21 isn't it spread over all the elements if it is an
22 appropriate charge?

23 **WITNESS VARNER:** Okay. The reason it's not
24 spread over all of the elements is that the factor
25 that the -- the item that makes actual costs vary from

1 forward-looking costs to a significant degree is
2 investment; how much capital you've deployed.

3 All of the other items really don't require
4 much in the way of capital, and you do have capital
5 included in those forward-looking costs, and you have
6 a return on that capital included. Those two items,
7 however, do require substantial amounts of capital to
8 produce. So those -- that's why we limited it to
9 those two items.

10 When we've looked at that in various states,
11 in some states it ended up only being on loops,
12 because there wasn't even a significant difference for
13 ports. In Florida it was a significant difference for
14 both, but loops because they have so much, and then
15 sometimes ports.

16 **COMMISSIONER CLARK:** Mr. Varner, help me
17 out. If you would look at Page 10 of the prehearing
18 order.

19 **WITNESS VARNER:** I don't have the prehearing
20 order. (Pause) Yes.

21 **COMMISSIONER CLARK:** Just tell me which ones
22 have the residual recovery element.

23 **WITNESS VARNER:** It's probably easier for me
24 to do it this way. It's the 2-wire and 4-wire loop
25 distribution.

1 **COMMISSIONER CLARK:** (b)?

2 **WITNESS VARNER:** Yes.

3 **COMMISSIONER CLARK:** Okay.

4 **WITNESS VARNER:** The 2-wire ADSL loop, down
5 to (h) and (i).

6 **COMMISSIONER CLARK:** Okay. So just those
7 three --

8 **WITNESS VARNER:** And (g); (g), (h) and (i).
9 (b), (g), (h) and (i).

10 **COMMISSIONER CLARK:** Let me ask you about --
11 it seems like at least physical collocation would have
12 a lot of investment in it, too.

13 Let me ask you a rhetorical question, or a
14 hypothetical question. If we were going to redo the
15 rates on physical collocation based on cost, would you
16 then argue it's appropriate for that to have the
17 residual recovery also?

18 **WITNESS VARNER:** No. We are proposing
19 prices based on the TSLRIC studies for physical
20 collocation.

21 **COMMISSIONER CLARK:** Oh. So it's only
22 virtual --

23 **WITNESS VARNER:** Only virtual is where we're
24 proposing the tariff. We don't have a tariff for
25 physical.

1 **COMMISSIONER CLARK:** Oh. Okay.

2 **WITNESS VARNER:** There is no tariff for
3 physical collocation.

4 **COMMISSIONER CLARK:** All right. Virtual
5 collocation, is it --

6 **WITNESS VARNER:** Yes. That's the only one.

7 **COMMISSIONER CLARK:** Is investment
8 appropriate for that? Assuming you would set the
9 tariff, would your argument -- the rationale of it
10 carry to the virtual collocation, that it should have
11 a --

12 **WITNESS VARNER:** No, because when you are --
13 when you look at collocation, you're talking about
14 space rental. It's use of space in buildings.

15 When you look going forward, for one thing,
16 land is not depreciable, so that doesn't enter into
17 the picture. Buildings, however, are. And I say --
18 the reason that doesn't enter into the picture,
19 because the thing that causes you to have to deal with
20 the residual recovery requirement is the fact that you
21 have long-lived depreciable plant in place; things
22 like copper wire, switching equipment, so forth.

23 Land you don't have to worry about.
24 Buildings, when we go in and when we look at the
25 collocation prices, much of the cost of collocation is

1 associated with actually setting up the space, getting
2 the space put in place, which is expense items or
3 capital that you're actually going to recover as you
4 put it up.

5 So a very small part of it is for the actual
6 rental of the space in the building. So it didn't
7 appear -- doesn't appear that it would be significant.

8 You're right. If you were going to go
9 through and do this residual recovery requirement, you
10 could do it on all of these elements, and you could --
11 you may be able to come up with a number, but it would
12 probably be a very, very small number. What we tried
13 to do was to just limit it to those where it appeared
14 to be a significant item and only deal with it on
15 those items.

16 **COMMISSIONER CLARK:** Thank you, Madam
17 Chairman.

18 **CHAIRMAN JOHNSON:** Any questions?

19 **MR. LACKEY:** Mr. Varner is available for
20 cross.

21 **MS. KEATING:** Madam Chairman, excuse me.
22 Staff has identified one exhibit for this witness, and
23 we think it would appropriate that it be marked for
24 the record at this time.

25 **CHAIRMAN JOHNSON:** Okay.

1 **MS. KEATING:** It's identified as AJV-3, and
2 it contains the deposition transcript, the deposition
3 exhibits, and the late-filed deposition exhibits from
4 Mr. Varner's January 12th deposition.

5 **CHAIRMAN JOHNSON:** Okay. It will be marked
6 as Exhibit 10 and identified as Staff AJV-3.

7 (Exhibit 10 marked for identification.)

8 **CHAIRMAN JOHNSON:** The witness has been
9 tendered.

10 **MR. SELF:** Chairman Johnson, I would like to
11 defer my time to AT&T and MCI and let them go first,
12 and if there's anything left, I can ask after that.
13 But before I do that, I'd like to ask Mr. Lackey a
14 clarifying question with respect to the sheet that he
15 passed out earlier of the proposed revisions to
16 Mr. Varner's testimony.

17 And just so I'm clear about what BellSouth
18 is proposing here, will there be additional revisions
19 that will be made later after we clarify what other
20 testimony is being stricken?

21 **MR. LACKEY:** The document that was handed
22 out only went to Mr. Varner's direct testimony. It
23 doesn't touch his rebuttal testimony at all. These
24 are all the provisions of his direct testimony that we
25 believe should be removed subject to the prehearing

1 officer's orders.

2 Once we sort out what's going to happen to
3 the other witnesses, then we have another sheet that
4 would relate to the rebuttal testimony. I just don't
5 want to do it until I know what I'm looking at, but if
6 there's something else in the direct testimony that
7 you think, that counsel thinks should be stricken,
8 we're going to have to have a discussion about it,
9 because we have removed everything that we believe is
10 encompassed within the prehearing order.

11 **MR. SELF:** With respect to that, then, the
12 only question I would have is regarding Mr. Varner's
13 Exhibit AJV-1. That exhibit has prices for electronic
14 OSS and manual OSS, and will there be a revision to
15 that that will be coming forth later?

16 **MR. LACKEY:** No -- we'll have to ask
17 Mr. Varner, but I thought that what he removed was the
18 \$10.99 which was the fee that was the subject of the
19 motion.

20 There's still a charge for ordering
21 encompassed within this docket; it's just not the OSS
22 charge, the electronic OSS charge. But we'll have to
23 get Mr. Varner to clarify that because I've just told
24 you everything I know about it.

25 **CHAIRMAN JOHNSON:** Mr. Varner --

1 **WITNESS VARNER:** Yes. Did you want me to --

2 **MR. LACKEY:** Let me ask Mr. Varner.

3 Mr. Varner, did we -- there's been a question raised
4 about whether something should be stricken out of
5 AJV-1 related to the motion to strike. Is there
6 something on that schedule that needs to be removed?

7 **WITNESS VARNER:** Nothing -- as we understand
8 it, nothing other than the \$10.99. There is a column
9 on there that says Electronic Orders and one that says
10 Manual Orders. As you can see, the one for manual
11 orders is always higher.

12 The reason for that is that that column
13 includes the cost of ordering the items manually. Our
14 understanding was that the parties would still be
15 allowed to order the items electronically; we just
16 could not recover the cost in this proceeding of the
17 OSS interfaces that they would be using.

18 So what we're doing is we're reflecting the
19 fact that it does not cost us as much when a party
20 orders it electronically. That's why they have a
21 lower, nonrecurring charge if they were to order it
22 that way.

23 We, however, have not -- don't have the
24 element in there that allows us to recover the cost of
25 the system that they're actually going to be using to

1 get the lower price.

2 If we were to delete that column, then they
3 would be paying as if they ordered everything manually
4 even though they ordered it electronically, and they
5 would be paying a higher price.

6 **MR. LACKEY:** The answer, Madam Chairman, is
7 that there's nothing else we're going to strike, at
8 least voluntarily, on Exhibit AJV-1, if was the
9 question.

10 **MR. SELF:** I think these issues will be gone
11 into on cross-examination, so perhaps we should move
12 on to that.

13 The only other question is whether this
14 sheet should be identified as an exhibit just so it --
15 since he has not read these into the record or
16 anything.

17 **MR. LACKEY:** Actually, I think those reflect
18 a letter that was filed with the clerk, but I have no
19 objection to having that document marked with the next
20 exhibit number and including it in the record.

21 **CHAIRMAN JOHNSON:** We'll go ahead and mark
22 it, then, as Exhibit 11, and the short title will be
23 Revisions to the November 13th Testimony of Varner.

24 (Exhibit 11 marked for identification.)

25 **MR. SELF:** Thank you, Madam Chairman.

1 **CHAIRMAN JOHNSON:** Mr. Melson, are we going
2 to start with you? Oh. I'm sorry.

3 **MR. LAMOUREUX:** It makes no difference to
4 me, but that's fine.

5 **CHAIRMAN JOHNSON:** Go ahead.

6 **MR. LAMOUREUX:** Good morning, Commissioners.
7 My name is Jim Lamoureux. I'm in-house counsel with
8 AT&T in Atlanta.

9 **CROSS EXAMINATION**

10 **BY MR. LAMOUREUX:**

11 **Q** Good morning, Mr. Varner.

12 **A** Good morning, Mr. Lamoureux.

13 **Q** Did I hear correctly; Mr. Lackey, when he
14 called you up told you to give me yes and no answers
15 this morning?

16 **A** I didn't -- what was the first part that you
17 said?

18 **Q** Never mind. (Laughter)

19 **COMMISSIONER CLARK:** Can I just ask you to
20 give me your name again?

21 **MR. LAMOUREUX:** Sure. It's Jim Lamoureux.
22 It's L-A-M-O-U-R-E-U-X.

23 **CHAIRMAN JOHNSON:** How do you pronounce it
24 again?

25 **MR. LAMOUREUX:** "Lam-or-oh."

1 Q (By Mr. Lamoureux) Mr. Varner, do you
2 agree that the Act requires that prices for unbundled
3 network elements be based on cost, correct?

4 A Oh, yes.

5 Q And you agree that under the Act, that cost
6 must be determined without reference to a rate of
7 return or other rate-based proceeding?

8 A That's correct.

9 Q You do not believe, however, that the Act
10 prescribes any cost approach for any type of
11 collocation, virtual or physical; is that correct?

12 A That's correct.

13 Q But you would agree with me that the Act
14 requires that collocation be offered at rates that are
15 just, reasonable and nondiscriminatory?

16 A Yes.

17 Q I think that's Section 251(c)(6) of the Act?

18 A Yes, it is.

19 Q I think you would also agree with me that
20 collocation has been defined by the FCC as an
21 unbundled network element; is that correct?

22 A I'm not sure. They've defined it as access
23 to unbundled network elements, and I've never been
24 able to get clear whether they consider the
25 collocation an element or whether it's considered as a

1 means of access to the elements.

2 Q All right. Well, let's work with access to
3 an unbundled element. The FCC -- do you agree with me
4 that the FCC has defined access to unbundled elements
5 as unbundled elements themselves?

6 A That's what I'm not clear on.

7 MR. LAMOUREUX: Let me, if I could -- may I
8 approach the witness?

9 CHAIRMAN JOHNSON: Yes. Sir, but you're
10 going to have to speak into a microphone whenever you
11 talk.

12 Q (By Mr. Lamoureux) Mr. Varner, what I
13 handed you was Page 26 out of your deposition that was
14 taken in this proceeding.

15 A Yes.

16 Q And I've highlighted some lines there.
17 Since I've stepped away, I can't tell you exactly what
18 those lines are. But didn't you say in your
19 deposition that you agreed that the FCC had defined
20 access to an unbundled element as an unbundled
21 element?

22 A No. I said I believe that it's been defined
23 as one. I wasn't sure.

24 Q Okay.

25 A And I'm still not sure.

1 Q Okay. But you do believe that that is the
2 case?

3 A Yes.

4 Q So if access to an unbundled element is
5 defined as an unbundled element, and collocation is a
6 means of providing access to unbundled elements, then
7 the cost standards in the Act that apply to unbundled
8 elements would also apply to collocation, wouldn't
9 they?

10 A No, because the Act specifically says, lays
11 out in Section 251(c)(6), is collocation, and it says
12 under the pricing standards that it applies to -- I
13 think it's 251(b)(5) and (c)(3).

14 Q Can you rattle off those numbers again for
15 me?

16 A I think -- well, I don't have the Act in
17 front of me, but it says in the preamble of 252(b),
18 which sections -- I think it's 251(b)(5) and
19 251(c)(3).

20 Q Okay.

21 A But I don't have it in front of me.

22 Q So you're talking about the section of the
23 Act that talks about pricing standards for unbundled
24 elements?

25 A And interconnection; as interconnection and

1 unbundled elements. That's the section that
2 establishes the based on cost criteria, the criteria
3 that you previously mentioned.

4 **CHAIRMAN JOHNSON:** Mr. Lamoureux, at an
5 appropriate time could you let me know when it would
6 be convenient for us to take a break?

7 **MR. LAMOUREUX:** Take a break whenever you'd
8 like.

9 **CHAIRMAN JOHNSON:** So this is fine?

10 **MR. LAMOUREUX:** This is fine.

11 **CHAIRMAN JOHNSON:** How much more do you
12 have? Quite a bit?

13 **MR. LAMOUREUX:** Oh, I think I might have 20
14 minutes, maybe half an hour.

15 **CHAIRMAN JOHNSON:** We're going to go ahead,
16 then, and take a 10-minute break.

17 (Brief recess.)

18 - - - - -

19 (Transcript continues in sequence in
20 Volume 2.)

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22

23

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25

\$

\$10.99 147/18, 148/8

&

& 3/9, 3/17, 4/7, 4/10, 4/14, 4/17, 7/22, 8/6

'95 23/4, 23/7, 23/9
'96 23/7, 23/8

1

1 1/20, 1/21, 4/6, 6/2, 6/6, 6/12, 6/14, 14/14, 42/4, 42/6, 42/9, 42/10, 42/16, 43/2, 51/3
10 6/4, 6/23, 49/18, 51/9, 51/17, 56/3, 56/25, 142/17, 146/6, 146/7
10-minute 126/2
100% 39/2, 39/5
101 4/3, 8/2
11 6/24, 149/22, 149/24
1200 4/5
12th 146/4
13 6/24
13th 149/23
14 34/18
1436 37/6
146 6/23
148 2/8
149 6/24
150 3/3, 6/10
154 1/21
1600 4/7
1870 3/5
1876 3/10
1900 8/6
1994 140/6
1996 1/8, 1/12, 1/17
1997 7/6, 57/18
1998 2/5
19th 57/18

2

2 6/15, 47/8, 47/10, 47/12, 53/12, 58/7
2-wire 142/24, 143/4
215 3/9, 4/14, 7/22
22nd 42/12, 43/4
23rd 45/22
24 45/16, 45/17
2400 4/18
251 151/17, 153/11, 153/13, 153/18, 153/19
252 153/17
2540 5/5
26 2/5, 152/13
271 21/2, 21/7, 22/4, 28/23
28 59/21
28th 54/10
29 7/6

3

3 6/16, 47/19, 47/21, 47/22, 47/24, 47/25, 153/13, 153/19
30309 4/6
30309-3996 3/18
30326 4/9
30342 3/16
32301-1509 4/5
32302-1876 3/10
32302-2095 4/15
32314 3/15
32399-0850 3/4
32399-0870 5/6
3343 4/8
365 3/5
37 57/15
370 4/10
37219 4/18

4

4 6/17, 48/5, 48/7, 48/9
4-wire 142/24
400 3/4
4066 4/6
4075 2/9
41 51/6
42 6/14, 51/6

47 6/15, 6/17
48 6/16, 6/18
4800 4/10
49 6/19, 6/20

5

5 6/18, 48/16, 48/17, 48/19, 49/2, 51/2, 153/13, 153/18
50% 13/19
5111 4/17
53 6/21
57 6/9
59 6/22

6

6 6/19, 49/2, 49/3, 49/5, 53/25, 151/17, 153/11
61 6/9
6526 3/14
675 57/10

7

7 6/20, 49/9, 49/10, 49/12, 54/18
700 3/15, 4/4
70180-1102 3/6
780 3/15

8

8 6/21, 41/2, 53/7, 53/9
80202-1370 4/11

9

9 6/22, 41/2, 59/15, 59/16, 59/17
960757 7/7
960833-TP 1/3
960833 7/7, 53/8
960833-TP 1/9
960846-TP 1/13, 7/8
98 6/10
999 3/17
9:30 2/6, 7/2

A

a.m 2/6, 7/2
ability 15/15, 16/25, 31/8
absent 9/13
accept 33/15
acceptable 34/3
Access 1/14, 8/13, 141/7, 151/22, 152/1, 152/2, 152/4, 152/20, 153/4, 153/6
accomplish 32/6, 38/6
accomplished 136/13
account 129/20
accurate 128/17, 128/18
ACSI 25/15
ACSI's 35/12
Act 1/8, 1/12, 1/17, 12/3, 12/5, 16/6, 19/2, 19/4, 19/11, 19/17, 23/11, 25/8, 26/4, 27/8, 27/11, 30/12, 32/1, 32/8, 32/10, 32/20, 127/3, 127/10, 127/16, 129/12, 129/13, 136/25, 139/17, 139/18, 139/20, 151/2, 151/5, 151/9, 151/13, 151/17, 153/7, 153/10, 153/16, 153/23
Act's 10/19
add 134/5
added 134/18
address 9/11, 9/19, 50/15, 51/1, 57/7, 57/10
addressed 24/10, 34/25
addresses 46/6
addressing 9/13
ADELMAN 3/16, 8/16
adequate 29/25
admissible 17/9
admitted 55/18
admonishing 56/24
ADMTD 6/13
adopt 12/25, 140/21
adopted 10/14, 24/7
ADSL 143/4
Affairs 5/11, 11/5
affect 13/22, 25/20
affected 15/19
afternoon 36/11, 54/5
agenda 9/3
agree 15/15, 15/16, 23/5, 27/9, 28/20, 31/4, 33/3, 128/6, 128/11, 128/12, 128/13, 130/19, 133/19, 133/21, 151/2, 151/5, 151/13, 151/19, 152/3
agreed 23/14, 28/12, 37/23, 152/19

agreement 1/10, 1/15, 32/19, 46/19
agreements 32/24
agrees 140/17
AJV-1 6/22, 57/22, 59/13, 59/16, 147/13, 148/5, 149/8
AJV-2 57/22, 58/19
AJV-3 6/23, 146/1, 146/6
ALECs 130/1, 132/17, 135/1, 136/21, 136/24, 137/6, 137/7, 137/10, 138/19
alert 43/8, 50/4
allow 15/20, 18/13, 18/19, 18/21, 26/5, 32/17, 37/19, 127/20, 127/21
allowed 12/14, 26/24, 28/5, 28/9, 35/7, 37/20, 148/15
allows 32/1, 129/12, 136/18, 136/19, 148/24
ALPHONSO 6/8, 57/1, 57/9
alternative 28/2, 37/9
ambiguity 32/23
amounts 142/7
analysts 51/17
announce 40/20
anomaly 136/14
answer 45/2, 56/24, 149/6
answers 59/4, 60/9, 150/14
anticipate 54/6, 54/24
anticipated 19/17
appearance 7/25, 55/16
APPEARANCES 3/1, 4/1, 5/1, 7/11, 8/9
applicable 140/19
application 21/2, 28/23, 28/24, 139/8, 139/11
applied 39/13, 39/15
applies 54/4, 141/2, 153/12
apply 25/6, 35/3, 54/20, 139/21, 153/7, 153/8
appreciate 11/25, 39/1
approach 36/12, 126/10, 129/2, 132/19, 151/10, 152/8
approaches 132/18
appropriate 8/25, 9/8, 9/19, 10/2, 10/4, 23/15, 37/20, 38/12, 41/9, 46/15, 46/21, 126/10, 127/11, 130/20, 136/12, 140/11, 141/22, 143/16, 144/8, 145/23, 154/5
approval 39/16
approve 137/11
approved 9/25, 40/3
arbitrage 138/2, 138/15, 140/10
arbitrate 15/16, 22/2, 22/21
arbitrated 17/2, 22/19, 39/6
arbitration 1/5, 1/10, 1/15, 7/8, 10/20, 10/22, 11/24, 12/11, 12/25, 15/2, 16/21, 20/16, 21/24, 22/17, 22/25, 23/12, 23/16, 24/7, 24/15, 24/20, 24/21, 25/1, 25/12, 27/3, 27/5, 29/3, 29/22, 30/10, 30/19, 31/23, 32/9, 32/17, 34/12, 34/23, 35/20, 36/18, 36/24, 37/6, 37/10, 38/4
arbitrations 23/3, 23/25, 24/1, 24/5, 35/25, 36/21, 36/22, 38/19, 39/8
areas 136/8
argue 27/9, 134/15, 143/16
argued 29/8
argument 11/13, 11/20, 33/13, 36/9, 144/9
arguments 10/2, 17/14
Arizona 36/17
arrangements 30/15, 132/15
arrived 37/14
Asbill 3/17
assertions 130/11
associated 145/1
AT&T 1/9, 4/2, 4/12, 7/9, 8/4, 8/5, 13/24, 15/13, 16/16, 16/22, 17/5, 37/21, 38/5, 38/19, 39/17, 40/24, 42/15, 44/5, 52/23, 53/1, 53/3, 55/17, 146/11, 150/8
AT&T&T 52/6
AT&T's 17/5, 47/17, 48/22
AT&T/MCI 40/25
Atlanta 3/16, 3/18, 4/6, 4/8, 4/9, 51/19, 55/17, 57/10, 150/8
attached 52/7, 57/21
attack 51/19
attempt 136/21
AUGER 4/13, 7/12, 11/3
authority 136/23
available 16/8, 49/17, 50/9, 54/3, 54/10, 54/11, 54/20, 54/22, 55/3, 145/19
Avenue 4/4
avoid 24/6, 140/9
aye 39/22, 39/23, 39/24, 39/25, 40/1, 40/2

B

BARBARA 4/13, 7/12, 11/2
Bers 55/21
based 21/5, 37/1, 38/1, 127/7, 127/17, 129/14, 130/25, 132/15, 132/16, 137/5, 139/20, 139/24, 140/1, 140/4, 143/15, 143/19, 151/3, 154/2
bases 132/20
basis 9/10, 32/2, 38/21, 130/21, 137/12
BC-3 41/3
Bell 21/2

Bellcore 56/8
 BellSouth 1/5, 1/11, 1/16, 3/6, 7/9, 7/19, 13/18,
 16/13, 19/15, 21/5, 22/18, 22/20, 25/17, 28/22, 28/23,
 33/20, 34/5, 46/24, 47/5, 51/14, 52/8, 57/2, 57/13,
 126/17, 127/19, 128/18, 129/1, 130/11, 131/7, 131/9,
 131/17, 132/16, 135/5, 136/9, 137/1, 140/20, 146/17
 BellSouth's 20/4, 20/6, 22/10, 22/13, 29/24, 34/16,
 40/23, 47/16, 48/2, 48/13, 52/25, 53/1, 126/7, 126/9,
 128/19, 132/20
 benefits 134/25
 BENNETT 3/2, 7/19
 BETH 5/2, 8/20
 Betty 2/8
 bifurcate 12/17, 15/4, 17/24
 bifurcated 14/19
 bifurcation 14/9
 Billingsley 40/24, 41/14
 binding 19/1, 19/3, 30/21, 31/6
 Bissell 52/7, 52/24, 53/3
 bit 30/8, 50/19, 126/14, 126/15, 138/16, 154/12
 bits 127/5
 blunt 25/11
 board 35/18
 bodies 46/7
 BOND 3/15, 8/15, 51/17
 book 135/13, 135/20
 books 51/15, 51/16, 135/22
 bottom 13/22, 33/5
 Boulevard 5/5
 bound 15/22, 26/1, 26/24, 27/2, 31/13, 31/16, 31/17,
 31/19, 32/4
 Box 3/10, 3/14
 Branan 4/16
 break 154/6, 154/7
 Brennan 3/17
 brief 11/21, 49/24, 53/25, 131/16
 bring 30/17, 134/19
 broaching 20/10
 broader 18/15, 18/17, 19/22
 brought 20/24, 28/22
 BROWN 5/3, 8/21
 BRUBAKER 5/3, 8/21
 build 132/3
 building 131/24, 131/25, 132/8, 145/6
 buildings 131/21, 132/6, 144/14, 144/17, 144/24
 bundled 132/14
 bundling 133/18
 business 13/20, 14/5, 26/23, 27/1, 28/18, 29/4, 29/5,
 33/8, 57/9, 126/18, 129/6, 133/3, 141/12

C

c/o 3/3
 Caldwell 45/11
 Caldwell's 52/8, 52/25
 California 36/23
 call 56/23
 came 33/24, 37/25, 44/16
 Canal 3/5
 capacity 13/19
 Caparelo 3/9, 7/22
 capital 142/2, 142/4, 142/6, 142/7, 145/3
 capture 35/23
 capturing 35/16
 care 41/6, 41/9, 41/19
 Carolina 13/5, 29/9, 29/14
 CAROLYN 5/10, 11/4
 carriers 30/13, 31/7, 35/12
 carry 144/10
 CARTER 5/3, 8/20
 case 18/13, 20/8, 22/12, 34/17, 39/13, 40/7, 153/2
 cases 129/23, 131/13
 casts 130/10
 catch 35/7
 caused 57/14
 causes 144/19
 caution 49/23
 Center 2/8, 4/8, 4/17
 central 131/17, 132/9
 certificated 35/6
 Chair 40/4, 45/13, 59/25, 137/15
 CHAIRMAN 2/1, 7/3, 7/11, 7/15, 8/8, 8/10, 8/17,
 8/22, 8/24, 9/18, 9/23, 10/3, 10/8, 10/25, 11/16, 18/7,
 18/10, 18/22, 19/12, 25/21, 25/25, 26/4, 26/10, 27/23,
 28/8, 29/16, 31/3, 31/14, 31/24, 36/1, 36/3, 39/20,
 40/2, 40/17, 40/19, 41/5, 41/12, 41/17, 41/21, 42/5,
 42/8, 42/15, 42/18, 42/22, 43/10, 43/11, 44/10, 45/6,
 46/9, 46/16, 47/1, 47/9, 47/13, 47/20, 47/23, 48/7,
 48/11, 48/17, 49/3, 49/10, 49/14, 49/20, 49/23, 50/10,
 50/13, 50/21, 51/21, 52/10, 52/15, 52/18, 52/22, 53/5,
 53/22, 53/24, 54/9, 54/13, 55/1, 55/12, 55/15, 55/22,
 55/25, 56/13, 56/15, 56/16, 56/21, 58/4, 59/6, 59/10,
 59/15, 60/12, 60/17, 130/24, 131/5, 134/2, 134/11,

134/17, 134/21, 135/9, 135/13, 135/16, 135/18, 137/14,
 145/17, 145/18, 145/21, 145/25, 146/5, 146/8, 146/10,
 147/25, 149/6, 149/21, 149/25, 150/1, 150/3, 150/23,
 152/9, 154/4, 154/9, 154/11
 change 140/12
 changeable 23/22
 changed 141/9
 changes 58/24, 60/5
 charge 141/22, 147/20, 147/22, 148/21
 charged 137/9
 charging 136/7
 CHARLES 4/16, 7/14, 8/18
 CHARLIE 5/2
 cheaper 132/9
 choose 15/16, 19/25, 22/3, 40/13, 40/14
 chose 141/20
 chosen 38/8
 Chuck 11/8
 City 4/17
 clarification 53/10
 clarify 21/4, 38/16, 146/19, 147/23
 clarifying 146/14
 CLARK 2/2, 9/22, 14/8, 14/13, 14/15, 14/17, 14/23,
 15/3, 15/11, 16/24, 17/20, 17/22, 17/23, 20/15, 21/14,
 21/21, 23/2, 23/7, 23/24, 24/3, 28/22, 32/15, 39/19,
 39/24, 40/4, 40/8, 40/12, 41/13, 44/1, 45/3, 45/13,
 133/10, 133/15, 133/19, 134/1, 137/15, 137/19, 138/2,
 138/5, 138/8, 138/12, 139/2, 139/5, 139/15, 139/22,
 140/3, 140/8, 141/1, 141/11, 141/15, 141/19, 142/16,
 142/21, 143/1, 143/3, 143/6, 143/10, 143/21, 144/1,
 144/4, 144/7, 145/16, 150/19
 classification 51/13
 clear 38/25, 50/17, 51/18, 55/2, 146/17, 151/24, 152/6
 clearly 129/15
 clears 50/11
 CLECs 136/18
 clerk 149/18
 codified 37/12
 cogent 20/25
 College 4/4
 collocation 129/25, 130/1, 130/3, 131/15, 131/20,
 137/17, 137/23, 138/11, 138/23, 139/19, 139/21,
 143/11, 143/15, 143/20, 144/3, 144/5, 144/10, 144/13,
 144/25, 151/11, 151/14, 151/20, 151/25, 153/5, 153/8,
 153/11
 collocators' 132/1
 Colorado 4/11, 37/3, 55/21
 column 148/8, 148/12, 149/2
 Commenced 2/6
 comment 21/20, 50/22
 comments 59/25
 commercial 30/14
 COMMISSION 1/1, 2/11, 5/4, 5/7, 8/20, 8/25, 9/1,
 9/9, 9/12, 9/13, 10/5, 10/14, 10/21, 11/11, 11/13,
 11/22, 12/5, 12/17, 12/21, 16/2, 17/9, 18/1, 18/18,
 20/4, 20/8, 20/10, 20/17, 22/8, 29/10, 29/23, 30/11,
 30/24, 31/1, 32/12, 34/16, 34/20, 34/25, 35/4, 37/19,
 40/11, 41/24, 55/19, 136/15, 140/22
 Commission's 9/12, 17/17, 34/15, 36/5, 37/17, 57/24
 COMMISSIONER 2/2, 2/3, 9/21, 9/22, 14/8, 14/13,
 14/15, 14/17, 14/23, 15/3, 15/11, 16/6, 16/24, 17/20,
 17/22, 17/23, 19/13, 19/21, 20/15, 21/14, 21/21, 22/7,
 22/16, 23/2, 23/6, 23/7, 23/24, 24/3, 26/22, 28/15,
 28/22, 32/15, 33/11, 34/1, 34/11, 37/18, 38/15, 38/16,
 39/1, 39/7, 39/18, 39/19, 39/23, 39/24, 39/25, 40/1,
 40/4, 40/8, 40/12, 41/13, 44/1, 45/3, 45/13, 133/10,
 133/15, 133/19, 134/1, 137/15, 137/19, 138/2, 138/5,
 138/8, 138/12, 139/2, 139/5, 139/15, 139/22, 140/3,
 140/8, 141/1, 141/11, 141/15, 141/19, 142/16, 142/21,
 143/1, 143/3, 143/6, 143/10, 143/21, 144/1, 144/4,
 144/7, 145/16, 150/19
 Commissioners 9/14, 9/18, 11/2, 29/17, 42/2, 43/8,
 47/2, 52/1, 58/5, 150/6
 commissions 11/23, 12/1, 30/17, 30/20, 36/7, 36/11,
 140/24
 common 127/23
 Communications 1/9, 4/3, 4/12
 companies 13/7, 13/14, 26/17, 30/14, 38/22, 127/5
 company 26/23, 39/3
 competition 13/14, 14/4, 14/6, 127/1, 129/10, 137/12
 competitive 129/8, 136/25
 competitors 13/23, 127/6, 129/7, 130/6
 complicated 34/19, 44/19
 comply 139/16
 component 133/8
 comports 10/19
 composite 6/21, 52/16, 52/19, 52/20, 53/6, 53/8
 computers 132/12
 Con-1 53/1, 53/12, 53/15
 Con-2 52/25, 53/14
 concept 27/10
 concern 46/3, 127/14
 concerned 16/2, 45/25, 46/4

concerns 31/25
 conclude 33/16
 concludes 137/13
 conclusion 32/16, 136/23
 conclusions 37/15
 concurrent 37/22
 condition 31/12
 conditions 1/7, 1/10, 1/15
 conduct 28/13, 31/11, 37/8
 conducted 36/14
 conducts 36/19
 Conference 2/8, 9/3
 confidential 6/21, 51/13, 51/25, 52/4, 53/8
 confirm 44/14, 44/17, 44/24
 confuse 17/23
 confused 12/10, 15/11
 Congress 32/5, 129/16
 congressional 30/12
 connect 130/2
 connotes 23/21
 considerable 30/9, 30/24, 127/10
 consistency 31/2
 consistent 10/21, 27/11, 129/5
 consolidated 7/7, 37/4, 38/18, 38/21, 52/4, 52/17
 consonance 36/14
 construction 139/9
 containing 46/20
 contains 46/24, 47/5, 47/16, 48/2, 48/13, 48/22, 49/7,
 52/5, 52/6, 146/2
 contemplation 30/19
 contents 52/21
 continuation 23/4, 29/21
 continue 12/21, 18/24, 32/24
 CONTINUED 4/1, 5/1
 continuum 30/6
 contract 33/2, 39/16
 contracts 38/24, 39/4, 39/16
 contradictory 32/21
 contrary 32/1, 32/5
 conundrum 25/4, 45/1
 convened 7/2
 convenient 154/6
 copies 51/11, 57/18
 copper 144/22
 copy 42/23, 48/25
 Cornell 46/25, 41/14
 corporate 51/19
 Corporation 1/14, 3/19, 8/13
 correct 14/14, 19/18, 24/2, 43/12, 44/24, 51/24, 55/8,
 55/11, 151/3, 151/8, 151/11, 151/12, 151/21
 corrections 55/12, 58/16, 58/17, 58/23, 58/24, 60/5
 correctly 150/13
 cost 16/13, 16/14, 16/16, 16/18, 16/19, 20/19, 29/25,
 30/2, 30/3, 36/19, 37/11, 126/20, 126/22, 127/3, 127/7,
 127/9, 127/17, 127/18, 127/21, 128/2, 128/3, 128/6,
 128/8, 128/9, 128/16, 128/19, 129/3, 129/14, 129/17,
 129/20, 129/23, 130/1, 130/4, 130/20, 131/1, 131/9,
 131/12, 132/7, 132/14, 132/21, 132/25, 133/2, 134/13,
 134/19, 134/20, 134/23, 135/6, 135/23, 136/1, 136/3,
 136/4, 138/21, 139/12, 139/14, 139/21, 139/24, 143/15,
 144/25, 148/13, 148/16, 148/19, 148/24, 151/3, 151/5,
 151/10, 153/7, 154/2
 cost-based 139/25
 costs 127/11, 127/13, 127/14, 127/22, 127/23, 129/11,
 129/16, 130/16, 130/18, 130/22, 130/23, 131/3, 131/8,
 132/2, 133/6, 133/13, 133/14, 133/23, 133/24, 134/4,
 134/24, 135/3, 135/8, 135/11, 135/13, 135/20, 135/21,
 137/3, 137/7, 138/22, 138/24, 140/2, 140/4, 140/11,
 141/25, 142/1, 142/5
 Counsel 7/4, 8/5, 55/16, 147/7, 150/7
 couple 27/15, 29/18, 53/11
 course 27/14, 37/1, 38/8, 56/10, 60/14
 cover 135/5, 135/8
 COX 5/2, 8/21
 creates 45/1
 criteria 154/2
 Cross 6/10, 145/20, 150/9
 cross-connect 137/25
 cross-examination 28/7, 50/8, 50/9, 149/11
 crucial 14/2
 CSR 2/11
 Culpepper 4/13
 Cuneo 4/10, 8/6
 currently 13/15
 customary 9/8
 customers 136/22
 cut 50/24, 51/19

D

D.C. 8/7, 55/21
 data 25/2, 137/5
 DATE 2/5

dated 7/5
 Dave 11/6
 DAVID 3/16, 54/1
 DAY 1/19, 54/3, 54/12, 54/21, 54/23, 55/3, 55/4, 55/5, 55/7, 55/10, 56/8
 days 29/20, 34/18
 deadlines 23/13, 23/17
 deal 31/20, 32/8, 144/19, 145/14
 DEASON 2/2, 9/21, 22/16, 26/22, 28/15, 37/18, 38/17, 39/1, 39/7, 39/18, 39/23
 deaveraged 136/7
 deaveraging 136/9, 136/16, 136/18
 debate 127/10
 debt 51/15
 December 7/6, 57/18
 decide 128/16
 decided 19/23, 31/5, 140/22
 decision 9/2, 9/12, 12/15, 17/15, 17/19, 22/12, 22/15, 39/6, 50/2, 141/12
 decisions 30/20, 38/19, 38/20, 39/2, 130/21
 default 37/7
 defer 18/11, 38/10, 146/11
 defined 151/20, 151/22, 152/4, 152/19, 152/22, 153/5
 definition 127/9
 degree 142/1
 delay 13/1
 delete 149/2
 deletes 58/6
 deliberation 30/9, 30/25
 delineated 19/1
 delineation 53/6
 demand 17/11
 demonstrate 128/19
 demonstrated 140/12
 denied 10/24, 11/23, 20/24, 28/4, 29/10, 36/15, 40/13
 Denver 4/11
 deny 9/3, 27/12, 38/13
 denying 9/5
 depart 132/24
 deployed 142/2
 deposition 53/2, 53/3, 146/2, 146/3, 146/4, 152/13, 152/19
 depreciable 144/16, 144/21
 depreciation 135/23, 136/3
 describe 52/5, 128/25
 described 59/8
 describing 52/21
 description 51/3, 131/16
 designed 132/1
 detail 128/23
 details 128/2
 determine 126/20, 128/8, 136/4
 determined 30/11, 133/25, 135/25, 151/6
 Determining 127/24, 128/6
 develop 14/4, 14/6
 developed 16/19, 22/1, 27/14, 126/22, 136/1
 developing 132/7
 development 129/10, 137/12
 dialogue 22/7
 dictate 130/4
 differed 37/23
 difference 128/15, 131/6, 133/5, 133/12, 134/7, 135/10, 136/14, 142/12, 142/13, 150/3
 difficult 19/9
 difficulty 14/18, 15/17
 Direct 6/9, 43/13, 43/17, 43/21, 57/5, 57/15, 57/17, 58/1, 58/24, 59/3, 59/7, 126/2, 146/22, 146/24, 147/6
 directed 39/15
 disagree 133/23, 134/9
 discovery 46/20
 discriminatory 19/10, 27/6, 33/14
 discuss 51/16, 128/23
 discussed 58/10
 discussion 9/24, 39/21, 127/12, 147/8
 disparity 132/10
 disputes 30/17
 disputing 21/24
 distribute 42/1
 distributed 47/4, 52/1
 distribution 142/25
 Division 5/4
 DOCKET 1/3, 1/9, 1/13, 12/22, 12/23, 19/25, 38/5, 147/21
 Dockets 7/7, 13/9, 13/10
 document 46/14, 58/1, 58/11, 146/21, 149/19
 documents 41/25, 42/2, 42/19, 42/24, 43/1, 48/15, 48/24, 49/1, 51/5, 53/16
 doesn't 21/8, 40/5, 135/5, 144/16, 144/18, 145/7, 146/23
 dollars 13/17
 DOUGLAS 3/2, 7/18
 Dr. Billingsley 41/15
 Dr. Billingsley's 41/1

Dr. Bradford 40/24
 Dr. Cornell 41/16
 Dr. Cornell's 41/2
 Dr. Randall 40/23
 Dr. Selwyn 44/6
 drafted 38/23
 dramatic 136/10
 dramatically 13/22
 drew 29/23
 DSO 137/25
 Dunbar 4/14, 11/3, 11/7
 Dunlap 4/14
 during 24/25, 59/24

K

easier 142/23
 Easley 2/8
 East 4/3
 economy 17/10, 17/11, 25/10, 27/9, 35/23, 37/20, 38/7
 edit 44/7
 effective 28/7, 28/13
 efficient 128/9
 effort 126/12
 Eighth 48/4
 elect 13/7, 26/18, 33/24
 electronic 147/13, 147/22, 148/9
 electronically 148/15, 148/20, 149/4
 elects 18/18
 element 19/6, 24/14, 128/7, 133/18, 134/6, 137/24, 142/22, 148/24, 151/21, 151/25, 152/3, 152/20, 152/21, 153/4, 153/5
 elements 12/13, 13/18, 13/25, 14/12, 14/14, 15/1, 15/7, 16/3, 17/3, 17/13, 18/25, 22/23, 29/24, 33/6, 33/7, 126/8, 128/20, 129/2, 129/4, 129/24, 130/4, 130/9, 130/17, 131/11, 132/14, 133/2, 133/4, 133/8, 133/15, 136/17, 139/7, 139/8, 141/20, 141/21, 141/24, 145/10, 151/3, 151/23, 152/1, 152/4, 152/5, 153/6, 153/8, 153/24, 154/1
 elements' 136/15
 embedded 135/20
 emergency 9/9
 employed 57/12
 enacted 23/11
 encompassed 147/10, 147/21
 end 45/17, 135/7, 137/9, 138/6, 138/7
 endeavor 50/18
 endeavored 44/12
 ended 142/11
 ensured 130/15
 enter 7/25, 19/14, 144/16, 144/18
 entered 39/9, 39/11, 40/21, 41/1, 55/15
 entrant 35/18
 environment 132/3
 equal 127/18, 129/3, 129/23, 130/1, 130/10, 130/12, 130/15, 130/18, 130/22, 133/22, 134/3, 137/2, 138/23
 equals 132/24
 equipment 130/2, 131/10, 131/12, 131/19, 131/21, 131/22, 132/17, 132/21, 137/6, 144/22
 error 53/25
 Esplanade 2/9
 establish 28/2, 28/11, 36/25, 127/15, 129/1, 129/11
 established 24/11, 26/2, 128/21
 establishes 135/8, 154/2
 evening 44/23
 event 23/11, 33/18, 33/19, 34/2, 34/3, 37/6
 evidence 17/8, 22/10, 22/13, 34/20, 38/1, 128/18
 eviscerating 46/14
 Examination 6/9, 6/10, 57/5, 150/9
 exchange 30/13
 excuse 33/10, 145/21
 exhibit 6/21, 41/3, 42/4, 42/6, 42/9, 42/10, 42/16, 43/2, 45/24, 47/8, 47/10, 47/12, 47/19, 47/21, 47/25, 48/5, 48/9, 48/16, 48/19, 49/2, 49/5, 49/9, 49/12, 51/2, 52/4, 52/14, 52/17, 52/19, 52/20, 52/24, 53/7, 53/8, 53/9, 58/18, 58/19, 59/13, 59/14, 59/16, 59/17, 138/22, 145/22, 146/6, 146/7, 147/13, 149/8, 149/14, 149/20, 149/22, 149/24
 EXHIBITS 6/12, 40/21, 41/2, 41/3, 41/10, 46/20, 50/5, 50/8, 52/4, 52/7, 53/18, 57/22, 146/3
 exist 26/25, 131/13, 132/7, 132/15
 existing 31/7, 130/7, 130/8, 132/5, 137/17, 139/16
 exists 130/3, 131/24, 132/10, 134/25
 expand 13/19
 expect 50/2, 130/16, 131/2, 131/4, 136/24
 expedient 49/15
 expense 145/2
 experience 26/11
 expert 15/24
 explanation 14/9

F

face 33/19
 facilities-based 35/11
 fact 10/16, 21/1, 21/4, 22/20, 23/3, 26/14, 36/15, 127/13, 129/12, 131/24, 134/25, 139/25, 144/20, 148/19
 factor 141/24
 fall 30/16
 failed 10/15, 10/17
 fair 19/20, 20/2, 31/10, 137/11
 Farris 4/16
 favor 39/22
 favorable 33/16
 FCC 21/2, 37/5, 37/8, 37/12, 151/20, 152/3, 152/4, 152/19
 Federal 1/7, 16/6, 19/2, 19/4, 19/11, 26/4, 137/19, 137/22, 138/1, 141/13
 fee 139/9, 139/11, 147/18
 Ferry 3/15
 Fiber 1/4, 3/11, 7/24
 Fifth 48/3, 48/14, 48/20, 48/21
 figure 25/5, 46/12
 file 39/15, 140/16
 filed 29/11, 30/3, 45/22, 51/12, 58/8, 140/2, 140/4, 140/7, 149/18
 filing 30/1
 Financial 4/8
 find 16/4, 19/8, 19/9, 22/7, 27/7, 33/20, 36/12
 finding 20/9, 20/13, 22/11, 45/25
 fine 21/21, 150/4, 154/9, 154/10
 finish 8/9
 firm 7/21, 8/6, 8/11, 127/20, 128/9
 five 49/18, 50/1, 50/19
 FLORIDA 1/1, 1/5, 2/9, 3/4, 3/10, 3/12, 3/14, 4/4, 4/15, 5/3, 5/6, 7/23, 7/24, 8/3, 22/24, 128/22, 130/3, 131/18, 137/13, 137/22, 137/24, 140/16, 140/21, 142/13
 Florida-specific 137/5
 FLOYD 3/8, 7/21
 folks 35/24
 follow 32/15
 follows 10/10, 57/4
 footnote 54/1, 54/2, 54/4, 54/7, 54/18
 footnotes 54/17
 force 136/21
 forced 31/25, 33/15
 forcing 31/15
 foreclose 21/6, 21/8
 foresee 27/17
 formula 132/25
 forward-looking 127/22, 128/10, 130/20, 130/23, 132/18, 132/25, 133/6, 133/14, 133/22, 133/24, 134/3, 134/8, 134/9, 134/13, 134/19, 136/3, 142/1, 142/5
 found 13/3
 four 51/11
 Fourth 48/3, 48/14
 framework 126/13
 free 31/20, 33/3
 Friday 36/11
 front 153/17, 153/21
 fruitless 130/6
 furnished 51/10, 57/18, 58/5
 future 20/6, 130/17, 131/3, 131/4, 131/11

G

GARCIA 2/3, 39/25
 gather 138/13
 generic 12/7, 12/18, 12/22, 15/8, 17/17, 18/15, 22/25, 24/10, 24/11, 28/21, 28/2, 28/11, 29/12, 31/6, 31/11, 32/3, 35/1, 38/5, 38/15, 36/16, 36/19, 36/25, 40/6, 40/14
 geographic 136/8
 Georgia 3/16, 3/18, 4/6, 4/9, 13/5, 57/11
 Gilman 4/16
 grant 21/10
 granted 10/12, 15/22
 granting 21/10
 Green 3/13, 8/12
 guess 10/1, 13/13, 14/1, 14/18, 16/21, 21/22, 45/19, 59/13, 139/23
 guidelines 23/13

H

hairs 14/22, 15/6
 half 21/19
 hand 56/19
 handed 58/12, 146/21, 152/13
 handle 41/12
 happy 15/24
 hard 19/8, 22/8
 harm 137/9
 harmed 135/5, 135/7

HATCH 4/2, 8/2
hate 25/11
Hatfield 16/22
hearings 37/22, 56/10
heart 51/19
Hellen 4/17
help 28/10, 50/20, 142/16
Hialeah 131/24, 132/5, 132/9
high 14/3
higher 130/4, 130/5, 133/8, 136/22, 138/25, 139/3,
139/12, 148/11, 149/5
highlighted 152/16
historic 135/11
historical 127/23, 135/3
history 21/16
hold 16/4, 26/5, 31/5
hoping 22/25
Hopping 3/13, 8/12
HORTON 3/8, 8/1
hospital 21/15
hypothetical 143/14

I

ICI 25/15
ICIs 35/13
ID 6/13
identical 29/14
identification 42/4, 42/10, 46/21, 47/8, 47/12, 47/19,
47/25, 48/5, 48/9, 48/16, 48/19, 49/2, 49/5, 49/12,
53/9, 59/17, 146/7, 149/24
identified 46/23, 47/5, 47/13, 47/16, 47/18, 47/20,
47/24, 48/2, 48/12, 48/20, 48/21, 49/4, 49/7, 49/11,
145/22, 146/1, 146/6, 149/14
identify 10/15, 46/22, 59/16, 134/6
ignore 131/23, 137/10
illogical 31/18
illustrate 131/14
imaginary 131/12, 132/6, 132/8
impact 19/23
impacts 15/9
implement 136/16
importance 15/7, 16/11, 26/17
impose 49/15
improper 30/22
in-house 8/5, 55/16, 150/7
inadvertence 9/7
inaudible 27/22, 45/5
inconsistent 31/22
incorporated 38/6
incredible 17/16
incremental 127/22, 130/18
incumbent 30/13, 35/10, 127/4
incur 128/10, 130/16, 131/2, 131/3, 131/4
incurred 129/3, 135/21, 136/5
indicate 140/8
indicated 11/14
indicates 54/2, 58/1
industry 12/8, 15/9, 16/9, 127/2
information 21/25, 24/22, 25/16
initial 20/13, 38/19, 38/20, 39/12
inputs 128/2, 128/13, 128/17
inserted 6/9, 6/10, 59/11, 60/13, 60/17
instant 45/10
intent 30/12, 32/5, 32/10, 51/12
intention 50/5
interconnection 1/6, 1/11, 1/16, 30/15, 126/8, 153/25
interexchange 138/9
interfaces 148/17
interim 20/19, 23/19, 24/5, 24/8, 29/1, 29/3, 29/25,
30/4, 36/23, 37/1
Intermedia 20/24
interpretation 37/17
Interrogatories 46/25, 47/7, 47/18, 48/4, 48/23,
49/8, 53/15
interstate 140/18
intervene 18/11, 18/12, 27/21
intervenor 11/24, 20/23, 36/18, 36/24
intervention 15/20, 15/22, 20/23, 21/10, 21/11,
26/25, 27/12, 28/4, 29/10, 30/22, 36/5, 37/4, 38/14
intractable 33/20
introduce 52/14
introduction 127/1
investment 133/9, 136/2, 142/2, 143/12, 144/7
investments 136/5
issue 10/5, 10/9, 11/18, 12/4, 12/7, 12/12, 13/5, 13/6,
14/10, 14/14, 14/17, 14/19, 15/1, 15/4, 17/24, 18/21,
20/11, 20/20, 21/6, 22/5, 24/10, 35/19, 56/3, 58/7,
60/3, 136/6
issued 42/12, 43/4
issues 27/16, 35/1, 35/3, 58/9, 149/10
ITEM 6/3, 51/3, 51/6, 58/6, 141/25, 145/14
items 51/7, 134/8, 142/3, 142/6, 142/9, 145/2, 145/15,

148/13, 148/15
IXCa 35/9, 138/10

J

JACOBS 2/3, 19/13, 19/21, 22/7, 33/11, 34/1, 34/11,
40/1
James 8/4, 55/15
January 2/5, 42/12, 54/10, 146/4
JENNIFER 5/3, 8/21
JIM 4/5, 150/7, 150/21
JOE 2/3
JOHNSON 2/1, 3/15, 7/3, 7/11, 7/15, 8/10, 8/17,
8/22, 8/24, 9/18, 9/23, 10/3, 10/8, 10/25, 11/16, 18/7,
18/10, 18/22, 19/12, 25/21, 25/25, 26/4, 27/23, 29/16,
31/3, 31/14, 31/24, 36/1, 36/3, 38/15, 39/20, 40/2,
40/17, 40/19, 41/5, 41/12, 41/17, 41/21, 42/5, 42/8,
42/15, 42/18, 42/22, 43/10, 45/6, 46/9, 46/16, 47/1,
47/9, 47/13, 47/20, 47/23, 48/7, 48/11, 48/17, 49/3,
49/10, 49/14, 49/20, 49/23, 50/10, 50/13, 50/21, 51/21,
52/10, 52/15, 52/18, 52/22, 53/5, 53/22, 54/9, 54/13,
55/1, 55/12, 55/22, 55/25, 56/13, 56/16, 56/21, 59/10,
59/15, 60/17, 130/24, 131/5, 134/2, 134/11, 134/17,
134/21, 135/9, 135/13, 135/16, 135/18, 137/14, 145/18,
145/25, 146/5, 146/8, 146/10, 147/25, 149/21, 150/1,
150/5, 150/23, 152/9, 154/4, 154/9, 154/11
judicial 17/10, 25/10, 27/9, 35/23, 37/19, 38/7
JULIA 2/1
jurisdiction 29/8
justification 138/13

K

Katherine 54/19
KEATING 5/2, 8/20
Kilck 53/3
knowledge 16/17

L

L-A-M-O-U-R-E-U-X 150/22
L-E-M-M-E-R 55/24
L.L.P 3/17, 4/10
LACKEY 3/2, 7/18
Lam-or-oh 150/25
lame 150/7
LAMOUREAUX 4/5
Lamoureux 8/5, 150/7, 150/21
land 144/16, 144/23
language 37/14
late-filed 146/3
later 16/4, 25/1, 33/14, 41/11, 46/7, 54/5, 146/19,
147/15
Laughter 150/18
LAUREEN 4/7
law 7/21, 8/11, 10/16, 11/9, 27/5, 27/8
lay 126/24
laying 45/23
lays 45/24, 153/10
leave 45/19
LEC 35/11
left 8/15, 146/12
Legal 5/4
LEMMER 4/9, 8/6, 55/15, 55/24
LEON 2/3
letter 45/22, 149/18
level 37/7, 129/9, 130/5, 137/7, 137/25
levels 136/2, 136/24
licensed 11/9
life 135/23
limit 19/23, 32/7, 145/13
limitations 49/15
limited 36/10, 36/20, 36/21, 55/19, 142/8
line 13/22, 33/5
lines 152/16, 152/18
lineup 54/24
lion's 35/8, 35/16
list 6/14, 42/1, 42/6, 58/20, 58/21
listed 14/14, 43/1, 53/11, 54/15
little 50/19, 126/14, 126/15, 138/16
local 30/13, 127/4, 137/12
locations 139/6
logic 33/12
logical 32/16
long-lived 133/9, 144/21
loop 133/18, 136/7, 136/10, 142/24, 143/4
loops 130/14, 130/25, 132/24, 133/4, 133/7, 133/17,
134/2, 135/4, 136/8, 142/11, 142/14
lost 52/11
Louisiana 3/6, 37/3
low 146, 136/20, 136/21
lower 138/25, 139/3, 139/13, 148/21, 149/1

lowest 128/21, 129/4, 129/6

M

Madam 8/8, 40/4, 43/11, 44/10, 45/13, 53/24, 55/15,
58/4, 59/6, 60/12, 137/15, 145/16, 145/21, 149/6, 149/25
Madame 28/8
Majors 40/25
manageable 126/13
mandates 129/15, 129/21
manner 28/14
Manning 4/7
manual 51/15, 147/14, 148/10
manually 148/13, 149/3
map 29/23
MAREK 5/10, 11/4
mark 59/15, 149/21
marked 42/3, 42/6, 42/8, 42/10, 42/16, 47/7, 47/9,
47/12, 47/23, 47/25, 48/5, 48/7, 48/9, 48/15, 48/17,
48/19, 49/2, 49/3, 49/5, 49/9, 49/10, 49/12, 50/6, 53/6,
53/9, 59/13, 59/17, 145/23, 146/5, 146/7, 149/19, 149/24
marketplace 129/8, 129/21, 136/25
markets 13/14
MARSHA 4/2, 8/2
MARTHA 5/3, 8/20
Martin 4/7
match 130/24, 140/23
matching 35/10
Mathews 4/16
Matter 1/3, 14/22, 52/3, 55/15
matters 8/23, 18/1, 40/18, 41/22, 46/17, 50/12,
50/14, 51/22, 53/23, 55/13, 56/1, 56/14, 128/24
McGURK 4/7
MCI 1/13, 1/14, 3/19, 7/10, 8/12, 8/13, 8/15, 8/16,
13/24, 15/13, 37/21, 38/4, 38/19, 39/17, 40/24, 43/14,
146/11
MCI's 49/7
McKenna 4/9, 8/6
Meaning 139/5
medical 56/6
meet 23/14
MELSON 3/13, 8/11
member 55/20
members 16/9
memory 10/7
mention 56/12
mentioned 18/22, 130/19, 132/23, 154/3
Messer 3/8, 7/22
methodology 128/16, 128/19, 134/14
Metro 1/14, 8/13
Metropolitan 1/4, 3/11, 7/24
MFN'd 22/23
MFS 7/9, 15/14
Miami/Hialeah 131/18
MICHAEL 3/4, 40/25
microphone 45/7, 152/10
Mike 7/19
million 13/17
mind 128/1, 150/18
minds 132/16
minimize 37/11
minimizing 132/1
minimum 137/7, 137/8
minor 55/14
minute 38/10, 139/2
minutes 43/28, 49/18, 50/1, 50/19, 56/25
MISCELLANEOUS 6/2
missing 24/14
Missouri 36/13
mistated 38/17
mode 33/1
model 16/13, 16/14, 16/16, 16/18, 16/19, 16/22, 17/5,
128/12
models 126/22, 128/2, 128/14
modified 59/7, 59/10
moment 17/21, 47/4, 52/2
Monday 2/5
money 13/13, 13/15, 135/24, 136/4
Moaroe 3/3, 3/9, 4/15, 7/22, 8/3
month 13/17, 20/7, 22/9, 27/1, 43/5
Moore 4/14
MORNING 1/19, 11/17, 11/18, 56/5, 126/6, 150/6,
150/11, 150/12, 150/15
Merris 4/7
motion 9/2, 9/4, 9/9, 9/20, 9/23, 27/21, 28/1, 28/2,
28/3, 28/10, 39/20, 40/9, 40/12, 51/7, 60/15, 147/19,
148/5
motions 27/20, 27/25
move 9/21, 9/22, 38/13, 149/11
Mr. David 8/15
Mr. Dunbar 21/15
Mr. Garfield 56/4, 56/7
MR. HATCH 8/2, 44/10, 46/10, 54/17, 55/8, 55/14,

55/24
Mr. Lackey 6/9, 43/11, 44/4, 45/5, 45/8, 45/22,
50/15, 50/23, 51/23, 56/1, 56/2, 56/23, 57/6, 58/4,
58/11, 59/6, 59/12, 59/18, 59/19, 60/12, 126/1, 145/19,
146/13, 146/21, 147/16, 148/2, 149/6, 149/17, 150/13
Mr. Lamoureux 6/10, 150/3, 150/6, 150/10, 150/12,
150/21, 150/25, 151/1, 152/7, 152/12, 154/4, 154/7,
154/10
Mr. Lemmer 55/18, 55/20
Mr. Lynott 44/22, 44/23
Mr. Majoros 41/16
Mr. Nelson 8/10, 8/11, 38/15, 39/4, 39/12, 54/10,
54/11, 54/14, 55/5, 55/11, 150/1
MR. PELLEGRINI 7/5, 8/18, 8/24, 10/3, 10/9,
11/1, 11/14, 29/18, 31/3, 31/10, 31/18, 36/2, 36/3,
40/18, 40/19, 41/8, 41/15, 41/20, 41/23, 42/7, 42/11,
42/15, 42/17, 42/21, 43/3, 46/18, 47/1, 47/3, 47/11,
47/15, 47/22, 48/1, 48/10, 48/12, 48/20, 49/6, 49/13,
49/21, 50/4, 50/11, 51/8, 51/23, 52/11, 52/13, 52/17,
52/20, 52/23, 53/11, 53/14, 53/19, 53/21, 55/2, 55/6,
55/9, 56/15
Mr. Porter 54/5
MR. SELF 7/21, 53/24, 146/10, 147/11, 149/10,
149/25
Mr. Selwyn 44/2, 44/16, 46/12
Mr. Selwyn's 44/19
Mr. Smith 56/4, 56/6
Mr. Varner 43/13, 43/19, 45/9, 45/12, 50/17, 56/23,
57/12, 57/14, 58/14, 59/7, 59/20, 126/1, 135/9, 139/22,
142/16, 145/19, 147/17, 147/23, 147/25, 148/2, 148/3,
150/11, 151/1, 152/12
Mr. Varner's 45/3, 146/4, 146/16, 146/22, 147/12
MR. WELCH 7/14, 7/17, 11/16, 11/17, 14/8, 14/11,
14/15, 14/21, 14/25, 15/5, 16/1, 17/4, 17/21, 18/9,
18/17, 18/23, 19/4, 19/20, 20/2, 20/15, 21/14, 22/6,
24/18, 25/24, 26/3, 26/8, 27/13, 28/19, 32/7, 32/22,
33/23, 34/10, 40/8, 40/16
Mr. Wells 54/20
Mr. Wood 54/11, 54/13
MS. AUGER 7/12, 11/2
MS. KEATING 145/21, 146/1
Ms. Marek 21/17, 22/19, 23/8, 24/1, 24/4, 27/20,
27/25, 29/1, 34/25
Ms. Petzinger 54/22
MS. WHITE 7/18, 53/10, 53/17, 53/20

N

N.E. 3/18, 4/6, 4/8
NAME 6/7, 7/15, 55/22, 57/7, 57/9, 150/20
NANCY 3/2, 3/3, 7/18
Nashville 4/17, 4/18
nature 31/23, 32/20
necessary 33/7
necessitate 136/10
need 14/8, 33/2, 33/9, 44/14, 49/25, 50/15, 126/25
needs 15/8, 18/17, 18/19, 148/6
negotiate 20/1, 22/22, 30/14, 31/8, 33/3, 33/21, 34/6
negotiated 22/22, 34/4
negotiations 19/15, 19/18, 30/16, 32/1, 32/18, 33/20
neighborhood 13/16
network 14/12, 15/1, 15/7, 17/3, 19/6, 22/23, 126/8,
126/21, 127/6, 128/7, 128/8, 128/20, 129/24, 133/4,
134/25, 136/14, 136/16, 151/3, 151/21, 151/23
New 3/5, 26/22, 27/13, 35/17, 51/16, 127/3, 131/25,
140/16
night 44/16, 50/24
nine 56/3, 140/20, 140/25
nondiscriminatory 12/6, 16/8, 19/5, 25/7, 32/12,
151/15
nonrecurring 148/21
NORMAN 3/8, 8/1
North 8/3, 13/4, 29/9, 29/14
Northwest 8/7
note 41/17, 56/13
notice 7/4, 7/5, 9/8, 26/8, 51/12
notion 21/9
November 6/24, 149/23
NUMBER 6/13, 41/25, 59/14, 145/11, 145/12, 149/20
numbers 20/18, 153/14

O

Oak 5/5
objection 11/15, 42/25, 149/19
objective 127/25, 128/1, 130/10, 133/1
occupy 131/25
odds 36/6
offer 52/3
offered 19/6, 50/7, 129/5, 151/14
Office 3/10, 3/14, 11/3, 11/6, 131/19, 131/20, 132/5,
132/9

officer 10/16
officer's 9/4, 10/19, 147/1
offices 130/2, 131/17
Official 2/11, 6/14, 41/24, 41/25, 42/6, 42/19, 42/24,
43/1
old 140/5
one-page 58/6
open 12/22, 18/2, 26/24
opened 36/25
opening 37/9
operate 29/4
operation 33/2
operations 42/14, 43/6
opinion 19/11
opportunity 11/18, 12/12, 19/24, 20/12, 21/23,
24/13, 26/9, 27/2, 27/4, 28/7, 33/24, 34/6, 36/10,
40/16, 42/23, 138/18
Opposed 40/2
opted 22/22
options 19/23
orally 59/9
order 9/5, 10/11, 10/17, 10/19, 14/24, 37/5, 39/12,
39/13, 39/14, 41/6, 42/12, 43/4, 53/25, 54/18, 57/24,
142/18, 142/20, 147/10, 148/15, 148/21
ordered 149/3, 149/4
ordering 147/20, 148/13
orders 10/22, 35/4, 37/25, 38/25, 39/9, 39/11, 39/17,
147/1, 148/9, 148/10, 148/11, 148/20
original 20/16
originally 41/7
Orleans 3/5
OSS 57/25, 58/9, 147/14, 147/21, 147/22, 148/17
outline 31/20
outline 126/7, 126/14
overlooked 10/17

P

P-1 52/7, 52/24
P.A. 4/14
P.L.C. 4/17
packet 51/25, 52/5, 52/14
Pages 1/21, 45/23, 51/9, 51/14, 51/18, 51/25, 57/15,
58/6, 58/12, 59/21
paper 44/2, 44/6, 44/20
Paragraph 37/6
paragraphs 50/24
part 11/21, 12/17, 23/10, 23/15, 24/3, 27/10, 40/9,
46/6, 53/17, 126/18, 141/13, 145/5, 150/16
participate 12/15, 12/19, 12/23, 13/7, 17/18, 18/3,
18/21, 20/13, 22/4, 22/5, 25/23, 26/1, 26/7, 26/13,
26/18, 31/15, 31/16, 31/17, 31/19, 35/7
participated 26/20
participates 13/9
participating 35/10, 36/20, 36/22
participation 10/20, 10/22, 13/4, 31/12, 31/21,
31/25, 55/20
parties 12/8, 12/18, 12/23, 15/25, 17/18, 18/25, 19/2,
21/6, 21/23, 23/15, 24/12, 25/19, 25/20, 26/6, 26/11,
28/12, 28/16, 30/16, 30/21, 30/22, 35/6, 36/20, 36/21,
37/10, 38/5, 42/2, 42/12, 42/22, 43/5, 46/19, 50/9,
54/8, 57/19, 58/5, 58/12, 130/19, 131/7, 131/11,
131/19, 131/23, 135/2, 148/14
parties' 12/11
parts 44/7
party 9/5, 26/20, 28/5, 33/15, 148/19
party-by-party 32/2
passage 127/2
passed 146/15
Pause 17/22, 142/20
pay 138/2
paying 13/24, 149/3, 149/5
Peachtree 3/17, 4/5, 4/8, 57/10
PELLEGRINI 5/2, 8/18
pending 20/21
Pennington 4/13
period 23/23
permanent 17/1, 20/20, 21/3, 21/7, 23/19, 23/21,
24/12, 26/1, 28/25, 29/6, 30/1, 30/5, 36/25
permit 31/19
permitted 37/3
perspective 22/20, 23/5, 23/18, 23/20, 127/4
Pete 11/3, 11/7
Petition 1/4, 1/9, 1/13, 6/4, 10/10, 10/23, 36/15
petitions 7/8
Petzinger 52/7, 52/24, 54/19, 55/9
phase 30/7
phases 29/21
phrase 141/11
physical 131/15, 131/20, 143/11, 143/15, 143/19,
143/25, 144/3, 151/11
picture 144/17, 144/18
pieces 126/21, 127/5, 128/7

PLACE 2/8, 7/6, 23/23, 126/12, 144/21, 145/2
plan 133/9, 136/12
plant 144/21
point 8/9, 10/16, 15/21, 20/16, 20/22, 22/18, 23/3,
23/14, 25/3, 28/5, 28/6, 28/8, 28/9, 30/8, 30/10, 30/25,
31/23, 34/9, 34/11, 35/16, 35/18, 36/4, 38/4, 40/5,
40/10, 40/20, 43/22, 46/15, 49/13, 51/24, 60/16
points 29/19, 128/24
popular 12/20
Porter 54/2
portion 58/1, 135/3
portions 44/14, 53/1, 53/2, 59/25
ports 130/15, 130/25, 132/24, 133/5, 133/7, 133/17,
134/2, 135/4, 142/13, 142/15
position 30/23, 31/1, 34/4, 36/5, 36/6, 37/12, 126/14,
139/16
positions 12/1, 35/8, 35/17, 36/6, 37/22
possible 45/14
Post 3/9, 3/14
postpone 21/12
POTAMI 2/11
potential 127/6
practice 11/9, 55/18
practices 129/6
preamble 153/17
precedent 19/16
precedents 24/17
preclude 22/3, 40/5
precluded 14/5, 21/23, 21/25, 35/20
predecessors 126/17
Prefiled 6/9, 6/10, 57/14, 59/21
prehearing 9/4, 10/16, 10/18, 53/25, 142/17, 142/19,
146/25, 147/10
prejudiced 20/14
prejudicing 28/16
preliminary 8/22, 40/18, 41/21, 46/17, 50/12, 50/14,
51/22, 52/3, 53/23, 55/13, 55/14, 56/1, 56/14
prepared 28/16, 38/11, 42/13, 43/5, 43/12, 43/15,
43/20, 43/21, 44/5, 44/22, 56/22, 57/25
prescribes 151/10
presented 10/5, 15/23, 16/23, 16/25, 27/17
presenting 24/22
President 5/10
pretty 26/6
prevent 137/9
price 14/2, 35/19, 127/20, 129/4, 129/6, 130/5, 132/9,
132/13, 132/21, 132/24, 134/3, 140/19, 149/1, 149/5
prices 19/5, 19/7, 22/22, 23/17, 126/7, 126/10, 127/7,
127/16, 127/17, 127/21, 127/24, 128/4, 128/20, 128/21,
129/1, 129/3, 129/9, 129/11, 129/13, 129/16, 129/18,
129/20, 129/23, 129/25, 130/10, 130/12, 130/15,
130/17, 130/22, 130/23, 132/11, 132/12, 132/16,
132/23, 133/20, 133/22, 135/6, 135/7, 136/7, 136/8,
136/10, 136/11, 136/13, 136/15, 136/21, 136/22,
136/24, 137/1, 137/2, 137/3, 137/4, 137/7, 137/8,
138/23, 139/10, 139/19, 139/20, 143/19, 144/25,
147/13, 151/2
pricing 130/21, 153/12, 153/23
problem 36/13, 41/10, 44/4, 44/13, 44/21, 45/4, 45/9,
45/10, 54/16, 54/25, 56/6, 56/9
problems 13/2, 140/15
procedural 9/17, 14/22
procedures 36/15
proceed 12/23, 28/24
proceeding 10/21, 12/6, 12/17, 12/18, 12/22, 12/25,
15/2, 15/8, 15/12, 15/19, 16/3, 16/4, 17/2, 17/18,
17/25, 18/2, 18/8, 18/16, 18/18, 18/19, 18/24, 19/22,
21/7, 21/17, 23/1, 23/9, 23/16, 24/11, 25/13, 25/19,
25/22, 26/5, 26/12, 26/20, 28/3, 28/11, 29/12, 29/14,
30/6, 30/25, 31/6, 31/11, 32/3, 33/14, 33/17, 33/22,
33/25, 34/8, 35/5, 35/9, 35/15, 36/16, 37/7, 37/8,
37/11, 40/6, 40/14, 57/15, 58/2, 58/8, 59/21, 126/12,
127/14, 127/15, 127/25, 128/3, 135/7, 148/16, 151/7,
152/14
PROCEEDINGS 1/23, 10/23, 11/24, 19/15, 23/12,
26/15, 26/16, 29/22, 30/11, 31/23, 36/14, 36/19, 36/24,
36/25, 37/4
proceeds 36/17
process 34/21, 37/10, 37/24, 128/25
processes 126/23, 126/24
produce 142/8
Production 48/14, 48/24, 49/1, 51/4, 53/15
proffer 46/19
profit 127/8, 129/14, 129/19
progress 50/25
Promenade 4/6
pronounce 150/23
proof 20/6, 34/16
proposal 132/20
propose 129/9, 131/11, 132/13, 137/4, 138/23, 139/1
proposed 1/10, 1/15, 15/25, 126/7, 128/16, 130/8,
135/6, 146/15
proposes 127/19, 131/9, 137/2

proposing 130/12, 132/11, 132/16, 135/2, 143/18, 143/24, 146/18
proposition 28/21
proprietary 51/11
provide 9/16, 131/10, 137/11
provider 16/17, 34/22
providers 16/10, 18/3, 18/20, 19/8, 32/24, 33/1, 33/9, 129/7
provision 126/19, 129/4
provisions 32/11, 129/18, 146/24
proxy 37/2
PSC-98-0008-PCO-TP 10/11, 10/18
PUBLIC 1/1, 5/4, 8/19, 11/11
purchase 130/7, 138/11, 138/19
purchased 33/8
purchasing 13/17
purpose 32/5, 55/19, 126/6, 127/14, 132/1, 132/7
purposes 37/21, 37/24, 47/8, 47/19, 48/6, 48/16, 49/2
put 20/8, 34/18, 131/19, 145/2, 145/4
putting 21/9, 43/17, 131/20

Q

quantify 131/7
quarter 13/16
question 19/13, 22/16, 31/4, 33/12, 34/1, 134/12, 135/10, 139/24, 141/15, 143/13, 143/14, 146/14, 147/12, 148/3, 149/9, 149/13
questions 9/14, 29/16, 59/2, 60/8, 145/18

R

raise 56/18
raised 127/10, 148/3
raising 22/5
range 49/19
rate 16/10, 25/4, 32/14, 33/10, 151/6
rate-based 151/7
rates 1/6, 12/6, 12/13, 12/24, 12/25, 13/21, 14/3, 14/11, 15/6, 15/13, 15/15, 15/17, 15/23, 16/3, 16/4, 16/7, 17/2, 17/13, 18/4, 18/24, 20/19, 20/20, 21/3, 21/7, 23/19, 23/20, 24/7, 24/8, 24/12, 24/16, 24/25, 25/6, 25/7, 25/20, 26/1, 26/5, 27/6, 28/25, 29/1, 29/4, 29/6, 30/1, 30/4, 31/9, 32/4, 32/12, 32/13, 33/13, 33/16, 33/21, 33/24, 34/13, 34/24, 36/23, 37/1, 128/16, 130/8, 136/20, 137/23, 138/4, 140/11, 140/17, 143/15, 151/14
rating 51/15
rational 37/15
rationale 144/9
rattle 153/14
read 7/4, 10/5, 59/11, 149/15
reading 19/18
realities 129/21
reality 132/4
reason 13/12, 14/1, 20/25, 33/15, 38/8, 141/23, 144/18, 148/12
reasonable 34/6, 127/7, 127/8, 127/15, 127/17, 127/20, 127/24, 128/4, 129/13, 129/14, 135/3, 137/1, 137/3, 139/19, 139/23, 151/15
reasons 11/25, 16/12, 129/22, 138/17
rebalancing 136/10, 136/12
Rebuttal 6/10, 43/16, 43/18, 43/22, 44/3, 45/15, 46/6, 59/20, 59/21, 60/1, 60/5, 60/9, 60/13, 126/2, 146/23, 147/4
recall 39/5, 44/11
receive 9/8, 129/7
recognition 6/14, 41/25, 42/6, 42/19, 42/25, 43/1
recommend 137/17, 138/12
recommendation 10/6, 10/13
reconcile 128/15
reconsider 9/2, 9/20
Reconsideration 6/5, 9/4, 10/1, 10/11, 10/24, 27/22, 28/1, 29/11, 38/13, 38/21, 39/14
record 7/4, 38/2, 38/25, 40/22, 50/17, 51/18, 57/8, 59/8, 59/11, 60/13, 145/24, 149/15, 149/20
recover 127/20, 133/1, 134/22, 145/3, 148/16, 148/24
recovered 129/16, 129/17
recovery 127/21, 134/6, 134/10, 134/12, 134/23, 135/12, 137/6, 141/17, 142/22, 143/17, 144/20, 145/9
redo 143/14
reference 151/6
reflect 41/3, 58/12, 134/7, 136/13, 149/17
reflected 58/16, 58/21
reflecting 148/18
reflection 29/12
reflects 135/22
refresh 10/7
region 11/23, 21/18, 24/9
region-wide 140/18
regional 141/7
regions 141/2

Regulatory 5/10, 11/5, 129/21
reject 37/9
relate 147/4
related 58/7, 58/9, 135/4, 148/5
relates 53/14, 53/15
rely 21/3
relying 22/1
remaining 58/18, 130/9, 130/17
remedy 9/17, 33/18, 33/19, 34/9
remember 139/10, 141/6, 141/8
remits 20/3
remove 46/13
removed 58/7, 58/13, 60/4, 146/25, 147/9, 147/17, 148/6
rendering 10/17
rental 139/9, 139/13, 144/14, 145/6
Report 37/5
REPORTED 2/11
Reporter
represent 11/3
representation 21/5
represents 11/10
request 8/8, 9/1, 9/16, 9/20, 12/10, 18/10, 18/11, 51/12, 55/17
requested 53/16
requesting 12/9, 12/12, 30/13
requests 11/24, 20/23
require 142/3, 142/7
required 30/12, 127/5
requirement 134/7, 134/10, 134/12, 134/24, 139/17, 141/3, 141/13, 141/18, 144/20, 145/9
requirements 10/20, 130/12
requires 12/3, 12/5, 19/4, 127/16, 129/12, 136/25, 139/18, 139/20, 151/2, 151/14
resale 1/12, 1/17, 14/7
resemble 33/21
residence 136/19
residential 136/22
residual 134/6, 134/10, 134/12, 134/23, 135/12, 141/16, 141/17, 142/22, 143/17, 144/20, 145/9
resolution 30/18
resolve 60/15
resource 22/20
resources 16/18
respect 17/3, 20/18, 21/9, 36/9, 44/19, 54/19, 55/18, 146/14, 147/11
respond 23/2
responded 46/1
responding 9/14
response 40/3, 44/3
responses 46/20, 46/24, 47/6, 47/17, 48/3, 48/13, 48/22, 48/25, 49/7, 51/4
rest 131/22
result 38/22, 42/11, 43/4, 138/6
results 38/1, 39/10, 138/7
retail 136/11, 136/13, 136/15
return 142/6, 151/7
revenue 130/12, 141/16
review 32/8, 42/23
revised 57/17
revision 147/14
Revisions 6/24, 146/15, 146/18, 149/23
rhetorical 143/13
RICHARD 3/13, 8/11
rigid 129/22
Road 3/16, 4/8, 29/23, 35/18
Room 2/8, 4/6
ROSS 3/3, 7/19
round 19/17
RPR 2/11
RSB-6 41/2
RULE 4/2, 8/2, 18/13, 129/22
rulemaking 35/3
rules 37/12
run 50/19
RUTHE 2/11

S

safe 132/3
Sams 3/13, 8/12
satisfied 20/18
schedule 49/17, 148/6
scheduled 126/11
search 128/3, 128/4
seated 8/15
second 9/24, 30/8, 39/19, 39/21, 46/25, 47/6, 47/15, 47/17, 48/23, 48/25, 54/21, 55/3, 55/6
Section 151/17, 153/11, 153/22, 154/1
sections 32/8, 153/18
SEEGER 4/7
select 34/8
SELF 3/8, 3/9, 7/21, 7/22

sell 127/5
sensible 132/22
separate 35/25, 38/24, 39/8, 39/17
separated 131/21
sequentially 59/14
served 126/23
SERVICE 1/1, 5/4, 8/19, 11/11, 13/8, 16/9, 18/3, 18/20, 19/8, 26/18, 35/2, 126/19, 130/7, 136/12, 138/9
Services 1/14, 5/5, 8/14, 126/20
SESSION 1/19
set 7/6, 12/5, 16/3, 18/24, 19/5, 20/19, 21/4, 23/16, 23/18, 24/5, 24/11, 24/17, 24/25, 25/3, 25/6, 26/5, 29/3, 29/25, 32/12, 32/13, 32/20, 35/19, 36/23, 45/11, 46/25, 47/6, 47/17, 48/4, 48/23, 48/25, 49/8, 51/4, 129/3, 130/1, 130/10, 130/25, 133/22, 134/3, 136/23, 137/2, 140/10, 144/8
Sets 48/14
setting 12/13, 12/24, 14/11, 15/6, 15/13, 18/4, 24/16, 28/24, 29/6, 126/10, 129/22, 130/5, 135/7, 145/1
settled 28/17
Seventeenth 4/10
Seventh 48/4
share 35/8, 35/17
shared 127/22
sharing 126/15
sheet 146/14, 147/3, 149/14
short 48/8, 48/18, 49/17, 50/18, 53/7, 149/22
show 9/24, 40/3, 53/12, 138/22
Shumard 5/5
signify 39/22
Sims 3/3
single 39/13, 39/14
siphon 136/19
sit 34/4
situation 19/9, 29/10, 29/15, 51/17
six 46/19
Sixth 48/3
slog 128/1
small 145/5, 145/12
Smith 3/14, 8/12
sole 14/19
solution 12/16
sort 17/8, 46/7, 126/13, 138/13, 147/2
sound 129/5
South 3/3, 3/9, 4/14, 7/22, 13/5
southeast 24/9
Southern 1/9, 4/3, 4/12
space 131/21, 132/5, 132/6, 132/8, 139/9, 139/13, 144/14, 145/1, 145/2, 145/6
specify 51/13
spending 13/15
spent 29/7
splitting 14/22, 15/5
sponsor 11/12
sponsored 43/7
spread 141/21, 141/24
Sprint 36/16
Staff 5/7, 6/15, 6/16, 6/17, 6/18, 6/19, 6/20, 6/23, 8/19, 11/14, 29/17, 41/23, 42/9, 46/19, 47/13, 48/8, 48/18, 49/14, 51/2, 51/10, 145/22, 146/6
Staff's 6/21, 9/1, 9/16, 10/6, 10/13, 47/24, 48/3, 48/14, 48/22, 48/23, 48/25, 49/4, 49/8, 49/11, 50/5, 51/4, 53/7
stage 10/2, 39/16
stand 22/18, 43/19, 44/25, 56/17, 56/24, 59/9, 60/14
standard 130/20, 139/20
standards 153/7, 153/12, 153/23
standpoint 25/10, 35/23
start 27/1, 150/2
started 20/17, 43/3
starts 26/23
state 30/17, 30/20, 31/7, 36/7, 36/11, 37/7, 57/7, 137/20, 141/4, 141/9
state-specific 141/6
States 1/9, 4/3, 4/12, 12/2, 13/4, 13/10, 24/8, 26/11, 28/12, 140/20, 140/25, 142/10, 142/11
status 9/5, 22/17
statute 19/19
statutory 23/13, 23/17
stay 18/18
stepped 152/17
Stip 53/14, 53/15
Stip-1 6/15, 46/23, 47/5, 47/14
Stip-2 6/16, 47/16, 47/24
Stip-3 6/17, 48/2, 48/8, 48/10
Stip-4 6/18, 48/13, 48/18
Stip-5 6/19, 48/21, 49/4
Stip-6 6/20, 49/7, 49/11
stipulate 19/24
stipulation 40/22, 52/25, 53/1, 53/12
Stipulation-4 51/2
stop 27/18
Street 3/3, 3/5, 3/9, 3/18, 4/5, 4/10, 4/15, 4/18, 7/22,

8/3, 8/6, 57/10
stricken 44/15, 44/18, 45/15, 45/23, 58/2, 146/20,
147/7, 148/4
strike 42/13, 43/5, 43/13, 43/16, 43/21, 43/22, 44/5,
44/7, 45/20, 60/15, 148/5, 149/7
striking 43/14, 45/25, 59/25
struck 46/1
studies 29/25, 30/2, 30/3, 36/19, 127/3, 130/4,
138/21, 143/19
study 20/19, 128/3, 139/12, 139/14
subject 60/14, 146/25, 147/18
subloop 132/11, 133/17, 133/18
submit 38/3, 50/5
sufficient 18/14
suggestion 12/20, 45/14, 46/10
Suite 3/3, 3/5, 3/15, 4/4, 4/10, 4/18
summaries 49/20, 49/22, 49/25
summarize 45/20, 46/5, 50/3
summary 46/5, 49/16, 50/18, 50/24, 56/25, 126/2,
137/13
support 42/14, 43/6, 129/9, 136/19
supportable 37/16
surgery 11/8
surreal 132/19
SUSAN 2/2
suspend 12/21
Sutherland 3/17
Swafford 11/6
swear 56/18
switching 144/22
sworn 56/20, 57/3
system 148/25
Systems 1/5, 3/12, 7/24, 42/14, 43/6

T

talk 17/6, 36/11, 51/5, 152/11
talking 13/13, 14/20, 17/12, 19/6, 33/5, 144/13,
153/22
talks 153/23
Tallahassee 2/9, 3/4, 3/10, 3/14, 4/4, 4/15, 5/5, 7/23,
8/3, 11/19
tariff 130/2, 130/7, 130/8, 137/17, 137/20, 137/22,
137/23, 137/25, 138/1, 138/19, 138/20, 138/25, 139/12,
139/13, 140/16, 140/17, 140/18, 140/19, 140/24, 141/2,
143/24, 144/2, 144/9
tariffs 139/16, 140/12, 141/4, 141/7, 141/10
technology 128/10
Telecom 127/3, 129/12, 129/13
telecommunication 18/3, 18/20, 19/7
Telecommunications 1/6, 1/7, 1/11, 1/12, 1/13,
1/16, 1/17, 3/7, 3/19, 7/20, 8/13, 16/9, 23/11, 25/7,
51/15, 57/3, 57/13, 127/2
telephone 26/23, 126/18, 126/19, 127/4
tendered 146/9
Tennessee 4/18, 11/9, 11/10, 11/11, 13/4, 26/19,
26/21
terms 1/7, 1/10, 1/15
TERRY 2/2
testified 57/4
testify 43/8
testimonies 49/16
Testimony 6/9, 6/10, 6/25, 15/24, 22/11, 34/19,
40/21, 41/1, 41/9, 42/13, 43/6, 43/13, 43/15, 43/16,
44/8, 45/4, 45/15, 45/17, 46/2, 46/5, 49/21, 52/6, 52/9,
52/23, 52/25, 57/15, 57/17, 57/21, 57/25, 58/2, 58/8,
58/9, 58/14, 58/18, 58/25, 59/3, 59/7, 59/20, 59/22,
60/1, 60/4, 60/6, 60/9, 60/13, 126/3, 126/7, 126/9,
127/13, 139/25, 146/16, 146/20, 146/22, 146/23,
146/24, 147/4, 147/6, 149/23
Thank 10/25, 11/17, 17/20, 36/1, 39/18, 40/16,
40/17, 43/3, 43/10, 51/21, 53/5, 53/20, 55/25, 59/18,
131/5, 137/14, 145/16, 149/25
theirs 43/24
they've 24/10, 38/8, 151/22
third 30/22, 37/10, 47/17, 48/1, 48/3, 48/14, 51/4,
54/3, 54/12, 54/23, 55/3, 55/5, 55/10
third-party 36/17
THOMAS 3/15, 4/9
three 21/19, 29/20, 34/18, 40/20, 41/13, 143/7
three-day 20/5
TIME 2/6, 4/19, 5/11, 6/4, 7/6, 7/12, 8/25, 9/3, 9/5,
9/7, 9/11, 9/13, 9/16, 10/4, 10/10, 10/15, 10/23, 11/4,
11/5, 11/10, 12/20, 16/5, 16/21, 17/12, 17/16, 17/17,
20/7, 20/11, 20/12, 21/18, 22/17, 23/14, 23/23, 25/11,
25/13, 28/5, 29/7, 29/23, 31/5, 32/14, 34/15, 34/21,
34/22, 35/6, 35/12, 35/16, 35/23, 38/3, 38/14, 39/9,
41/9, 41/11, 41/19, 41/23, 42/3, 42/20, 43/7, 43/18,
46/18, 46/22, 49/17, 50/2, 50/7, 56/18, 56/21, 126/18,
136/11, 140/2, 141/6, 145/24, 146/11, 154/5
title 48/8, 48/18, 53/7, 149/22
Tom 8/5, 8/15
touch 146/23

town 44/23
tracking 44/13
TRACY 4/2, 8/2
transcript 53/2, 146/2
transcripts 53/4
Transmission 1/14, 8/14
triple 141/18
true 54/7, 130/13, 130/14, 133/7
trump 26/6
TSLRIC 143/19
Tuesday 9/10, 10/6
Tuesday's 9/3
turn 59/19, 136/6
turned 38/24
two 22/9, 24/20, 25/1, 27/20, 27/25, 30/21, 34/18,
37/25, 39/7, 39/9, 39/10, 50/15, 56/3, 57/21, 138/3,
141/20, 142/6, 142/9
TWOMEY 3/5, 7/19
type 13/17, 18/15, 128/12, 151/10

U

unanimous 10/14
unanimously 9/25, 40/3
unbundled 12/13, 14/11, 15/1, 15/7, 22/23, 126/8,
128/20, 129/2, 132/13, 136/9, 136/14, 136/16, 151/2,
151/21, 151/23, 152/3, 152/4, 152/5, 152/20, 153/4,
153/5, 153/6, 153/7, 153/23, 154/1
unbundling 132/12, 133/17
understandable 126/24
unfairly 136/19
uniformity 36/12
Union 4/17
United 36/16
universal 13/8, 26/18, 35/2, 136/12
unsound 129/23
unwilling 33/21
update 41/4
updates 41/2
upheld 31/1
users 135/7, 137/9
utilizing 136/1, 136/2, 136/4

V

values 37/2
VARNER 6/8, 6/25, 57/1, 57/9, 59/12, 131/2, 131/6,
133/13, 133/16, 133/21, 134/5, 134/15, 134/18, 134/22,
135/12, 135/15, 135/17, 135/19, 137/18, 137/21, 138/4,
138/7, 138/10, 138/16, 139/4, 139/7, 139/18, 140/1,
140/6, 140/14, 141/5, 141/14, 141/17, 141/23, 142/19,
142/23, 143/2, 143/4, 143/8, 143/18, 143/23, 144/2,
144/6, 144/12, 148/1, 148/7, 149/23
Varner's 44/8
vary 141/25
Vice 5/10
vice-president 11/5, 21/17
view 21/11, 49/16, 139/23
violate 16/6, 19/10
virtual 129/25, 130/3, 137/16, 137/23, 138/11,
138/22, 143/22, 143/23, 144/4, 144/10, 151/11
Virtue 130/1
voice 24/13, 24/23, 35/13
VOLUME 1/20, 6/2, 6/6, 6/12
voluminous 48/24
voluntarily 149/8
vote 10/14

W

walk 46/11, 139/2
walks 56/24
Warner 4/19, 5/11, 7/13, 9/5, 9/7, 9/11, 9/17, 10/4,
10/15, 11/4, 11/6, 11/10, 16/5, 16/21, 20/7, 20/12,
21/18, 25/14, 31/5, 34/22, 38/14
Warner's 6/4, 9/3, 9/13, 10/10, 10/23, 22/17, 38/3
Warners 35/12
Washington 8/7
waste 17/16, 25/11
week 20/5, 20/11, 22/8, 25/13, 25/14, 25/15, 27/1
weeks 24/20, 25/1
WELCH 4/16, 7/14, 7/17, 11/8
Wells 52/7, 52/24, 55/6
Wells' 53/2
West 57/10
WHITE 3/2, 7/18, 44/2, 44/6, 44/20
Wilkinson 4/14
willing 21/20
wire 144/22
wished 134/24
withdrawn 58/20
witness 28/6, 40/23, 40/24, 40/25, 45/12, 52/8, 52/24,

53/2, 54/2, 54/9, 54/15, 54/18, 55/3, 55/6, 55/9, 56/22,
57/2, 131/2, 131/6, 133/13, 133/16, 133/21, 134/5,
134/15, 134/18, 134/22, 135/12, 135/15, 135/17,
135/19, 137/18, 137/21, 138/4, 138/7, 138/10, 138/16,
139/4, 139/7, 139/18, 140/1, 140/6, 140/14, 141/5,
141/14, 141/17, 141/23, 142/19, 142/23, 143/2, 143/4,
143/8, 143/18, 143/23, 144/2, 144/6, 144/12, 145/22,
146/8, 148/1, 148/7, 152/8
WITNESSES 6/6, 22/13, 34/19, 40/21, 41/14, 41/18,
43/7, 44/13, 49/24, 50/3, 50/6, 50/7, 52/6, 52/23, 53/3,
54/1, 56/4, 56/16, 56/20, 126/11, 126/15, 147/3
witnesses' 49/16
wonder 34/20
Wood 55/3
work 31/20, 46/9, 152/2
working 44/17
works 46/11, 56/7
WorldCom 3/11, 7/9, 7/23, 8/1, 15/14
WorldCom's 46/24, 47/6, 54/2
worry 144/23
written 27/8

X

X 6/1

Y

year 20/17, 20/21
years 21/19, 27/15, 126/22
York 51/16

Z

Zarakas 45/11