BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of	DOCKET NO. 980696-TP
Determination of the cost of basic loca. telecommunications service, pursuant to Section Section 364.025, Florida Statutes.	

VOLUME 19

Pages 2163 through 2255

PROCEEDINGS:	HEARING
BEFORE:	CHAIRMAN JULIA L. JOHNSON COMMISSIONER J. TERRY DEASON COMMISSIONER SUSAN F. CLARK COMMISSIONER JOE GARCIA COMMISSIONER E. LEON JACOBS, JR.
DATE:	Thursday, October 15, 1998
TIME:	Commenced at 9:10 a.m.
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	MARY ALLEN NEEL, RPR

APPEARANCES: (As heretofore noted.)

I N D E X

WITNESSES - VOLUME 19

EXHIBITS - VOLUME 19

P R O C E E D I N G S

(Transcript follows in sequence from Volume 18.)

COMMISSIONER DEASON: One further question. Ignoring for the moment that there's argument that basic service doesn't pay its own way, if we just assume that right now basic service is paying its own way, am I to conclude from that then that 32 cents of every customer's monthly bill is to pay for those that don't their bills?

THE WITNESS: Yes, sir, based on that argument. Assuming that it covers all the revenues assigned to that item, that would be true.

COMMISSIONER DEASON: Has BellSouth -- has this been a historic number that has kind of held constant through the years, or has there been some recent change?

THE WITNESS: I'm just trying to remember. I've only had experience with it for just a couple of years, and I have seen it fluctuate some. Beyond that, I don't know that far back. But it does vary some by years.

COMMISSIONER DEASON: How does this compare -- do you have any idea how this compares to other companies in Florida or other companies

nationally?

THE WITNESS: I'm afraid I don't know that.

COMMISSIONER DEASON: Okay. Thank you.

One other. Has there been any change in BellSouth's deposit policies in the last few years?

THE WITNESS: Not in the last few. I think they've been fairly constant for the last couple of years.

COMMISSIONER DEASON: It just strikes me that's a large amount to ask other customers to pay for those that don't pay, and it looks to me like something's wrong, that perhaps that is just what is accepted in the industry and is considered fine. I don't have a feel for that. That's why I was asking you how it compares to others.

THE WITNESS: And I'm sorry. I haven't seen the others.

CHAIRMAN JOHNSON: AT&T?

MR. HATCH: I have a few questions. Thank you.

CROSS EXAMINATION

BY MR. HATCH:

Q Good morning, Ms. Caldwell. I'm Tracy Hatch. I'll be asking you a few questions on behalf

of AT&T.

A Good morning.

Q You are the witness for BellSouth who's responsible for all of the inputs to the BCPM in this proceeding; is that correct?

A Yes, sir, the user-adjustable inputs.

Q And one of the user-adjustable inputs would be your switching discount. And that number is proprietary, but it is shown on page 257 of your Exhibit DDC-1; is that correct?

A That's correct.

Q Is that number a mixed rate between new switching and growth switching?

A Yes, where there is a different discount. Some of the switches, for instance, the Northern Telecom normally has just one discount that's not a difference between replacement and growth, which is one of the ones we used. The other one is Lucent, and it does have a difference, and it's a meld.

MR. HATCH: Madam Chairman, I'm going to hand out some documents. These documents are documents provided to us in discovery by BellSouth. They consist of some highly proprietary confidential information exclusively to BellSouth, so I'm going to do my very best to avoid eliciting any information

that's contained in them that's proprietary. And I want to make sure and give BellSouth's counsel an adequate opportunity if it looks like I'm straying somewhere to jump in.

MS. WHITE: All right.

Q (By Mr. Hatch) Have you had a chance to look over the first four pages, five pages of that document yet, Ms. Caldwell? When you're done, let me know.

A Okay.

MR. HATCH: This may get kind of complicated, Madam Chairman, but could I have this document that I just handed out marked for identification, please.

CHAIRMAN JOHNSON: It's marked as 74.

MR. HATCH: And the short title would be BellSouth Switch Vendor Contract Extracts.

CHAIRMAN JOHNSON: Could you say that again?

MR. HATCH: BellSouth Switch Vendor Contract Extracts. This is just pieces of information. It's not the full contract.

CHAIRMAN JOHNSON: Okay.

(Exhibit 74 marked for identification.)

THE WITNESS: Okay.

BY MR. HATCH:

Q Now, with respect to the discount that is on page 257, I believe, of your DDC-1, could you turn to the third page in from the beginning of the document that I handed you?

COMMISSIONER CLARK: Tracy, you're not speaking loud enough. Is it the third page?

MR. HATCH: My apologies. I'll try and speak louder.

DDC-1, page 257, the proprietary version, shows BellSouth's switch vendor discount that they used for running their BCPM calculations. And if you look at the third page in on the document that I handed you, I'm going to be asking her a couple of questions comparing the two.

COMMISSIONER CLARK: Comparing what?

MR. HATCH: Comparing page 257 of DDC-1 with what's on the third page of the document that I handed out.

Q (By Mr. Hatch) Do you see the growth discounts set forth in the document that I handed you?

A Page --

Q May I approach the witness?

A The fourth in, page 9 of 19?

Q Yes, ma'am.

MS. WHITE: It's the fourth page in.

Q (By Mr. Hatch) It is the fourth page in. My apologies. It's 9 of 19. I didn't mean to confuse you.

A Okay. I'm with you.

Q Now, having reviewed this document, does this appear to be a BellSouth switch vendor contract with Lucent Technologies?

A Yes, it does.

Q Now, if you look in the upper right-hand corner, would this be the most recent contract that BellSouth would have with Lucent?

A To the best of my knowledge, it would be.

Q Now, if you look down at paragraph C on page 9 of 19 there and look at those growth discounts -- do you see those?

A Correct.

Q Each of those growth discounts are higher, meaning a better discount, than what's put forth in DDC-1; is that correct?

A I'm trying to be real careful not to say these numbers. No. If you look on 257 in DDC-1, 5E switches, under "Growth Discount Rate," there's a percentage. If you look on page 9 of 19 under C, come down one, two, three, four. And I don't know if I can

read the words beside that, so I won't. But that number corresponds, and we used that number based on information from our switch purchasing individuals.

MR. HATCH: May I ask a question of BellSouth's counsel? Do you see where we are on that document?

MS. WHITE: The one you handed out?

MR. HATCH: Yes, ma'am, paragraph C.

MS. WHITE: Yes, I do.

MR. HATCH: Do you see the dates under paragraph C?

MS. WHITE: Yes, I do.

MR. HATCH: Are those proprietary?

MS. WHITE: Yes, they are.

MR. HATCH: Okay.

Q (By Mr. Hatch) Ms. Caldwell, do you see the date on the first line?

A Yes.

Q That is a forward-looking date; is that correct? As of the --

A I'm sorry.

Q As of the time the contract was entered into.

A Yes.

Q Okay. I'm trying -- this is getting kind

of complicated.

A I know, and I'm trying to be real careful, because I'm real bad to say the numbers, and I'm --

Q The discount shown there for growth is higher than the growth discount that you show on page 257 of DDC-1; is that correct?

A I agree with that statement, but you have to look down farther. The other dates are even farther into the future. And the words I couldn't read beside the percentage explain why I believe we were told to use that number.

Q Now, if you take the second line down, which is a further out date, that discount is even higher than the previous date, which is still higher than the growth rate in DDC-1; is that correct?

A Yes, in terms of relationship. My explanation would be the same, if you look farther down.

Q And iff you look at the next line down, which is a date even further out, that discount for growth is still higher than the growth discount rate shown in DDC-1?

A That is true. I think it's significant that that number is less than the first two lines in the contract. And I still get to the point, you have

to look at the next number down and the words beside it.

Q And those words are a particular constraint on the contract performance; would that be a fair characterization?

A I wouldn't tie it to just the contract performance, but also maybe company needs. But, yes, I mean, in terms of -- it is a constraint, I would agree.

Q And the only way that your discount would match -- the discount in DDC-1 would match the discount on the fourth line down is if certain things didn't happen; is that correct?

A Yes.

Q Now, you're using those certain things not happening as the basis for your discount?

A Yes, we're using that assumption.

Q What is the probability that the criteria in the fourth line down will occur?

A I cannot give you a number. All I can say is that the conversations that we had with our individuals in the switching environment that handle these contracts said that would be the most probable number for us that would occur, so we should use that in our study.

Q So the most probable occurrence is where a sequence of events pursuant to your contract aren't going to happen that you assume will happen in order to get the other better discounts? I know that's complicated, and I wish we could do this another way.

A Well, I think in terms of what you said, that would be a true statement. But I think you also have to recognize that this discount is not that bad. I mean, this is a good discount in relationship to --

Q But it is not the best discount that you are eligible for pursuant to this contract, is it?

A Pursuant to this contract. And let me emphasize that this contract has some requirements on the number of lines you purchase and place and all of that, and these higher numbers represent like the best things that could ever occur.

Q Just for the growth portion?

A This is just the growth, that's correct.

Q Now, let's go over to the first page of that document. Do you see there in paragraph 7 the reference at the top right-hand corner to page 8 of 19? Do you see that?

A Okay. I'm on page 8 of 19. Can you give me the reference again? I'm sorry.

Q Okay. Page 8 of 19, which is the first

page of the document as I handed it out, paragraph 7.

A Paragraph 7. Okay.

Q That gives you a number that is not a pure discount, is that correct, in terms of a percentage discount?

A No, that is not a percent discount number.

Q And it is for a switch replacement?

A Yes, it is.

Q Okay. When you run your SCIS model, when it calculates a price per line, would the price per line calculated by SCIS as you have used it as an input to BCPM calculate a number higher or lower than that number in paragraph 7?

A I'm trying to follow your question.

Q Okay.

A All right. I think the answer is yes, but let me explain what's in there, and then we'll see if that -- if this lays down.

Q We'll see where it gets us.

A Yes, because it's really hard not to say these numbers.

The inputs to BCPM that we use are based on the regression analysis, but BellSouth did run SCIS to get our inputs to that regression analysis. So that's what I guess we're talking about, right, the S --

okay, the SCIS runs that generates numbers.

The SCIS runs are not based just on replacements. They are based on a meld of growth jobs and replacements. And the reason we do that is, this concept of this network dropping from the sky and being there today, that's just not realistic. I mean, even if you could do that, tomorrow you've got to have growth. So we use a meld. So our numbers from the meld relationship is going to be higher.

But there's another driving factor that you don't even see here. This number cannot just be assumed to be everything. There are other items that are not necessarily included in the number that's on this page that's in the handout. When you run SCIS, you have to include other things such as taxes and transportation, so we include those items.

And also, if you look at -- I've actually looked at some jobs in some other states where we had not this number, but the previous contract to this one that had a similar number. And if you look at that relationship, by the time the job is actually finished, you get the switch in, you get all the line modules, you get it up and running -- and I'm not talking about telco labor; I'm just talking about vendor prices that we pay -- get all the trunk lines

established, you will find in many cases it can be two to three times what this number is.

So you have to -- you can't just take this number at face value. You've got to look at what it physically -- absolutely everything it includes.

Q All other things being equal, this is a lower number than what you have used in your BCPM calculations to give you your switch investment; is that correct?

A That is correct, and I believe I explained the reasons why.

Q Now, let's go over to page -- the next page over. It would be page 1 of 10, paragraph 1.

A Okay.

Q Now, this is for new switches; is that correct? And then there is a price for new switches? The first sentence, paragraph 1.

A For a certain type replacement new switch, yes.

Q Right. And if you used that number in your BCPM calculations, that number is lower than what BellSouth has used in its BCPM calculations, is that correct, all other things being equal?

A That is the same. My explanation would be the same.

Q Turning over to the fifth page in, that would be a Nortel price sheet; would that be correct?

A Yes.

Q Now, Nortel does their pricing in a different way than Lucent; would that be a fair characterization?

A Yes. Pardon?

Q As you described earlier, Nortel does it a different way from the way Lucent does it?

A Yes.

COMMISSIONER CLARK: Excuse me. What page? The fifth page in?

MR. HATCH: It's the fifth page in, and it's a Nortel --

COMMISSIONER CLARK: Got it.

Q (By Mr. Hatch) Now, do these numbers appear to be Nortel's numbers for BellSouth's contract purposes?

A Yes.

Q Now, if you look at --

MR. HATCH: May I ask BellSouth's counsel a question? Would the line size designations talking about a particular category be proprietary? I understand. I'm just trying to be careful.

MS. WHITE: I would have to say yes.

Q Turning over to the fifth page in, that would be a Nortel price sheet; would that be correct?
A Yes.
Q Now, Nortel does their pricing in a different way than Lucent; would that be a fair characterization?
A Yes. Pardon?
Q As you described earlier, Nortel does it a different way from the way Lucent does it?
A Yes.
COMMISSIONER CLARK: Excuse me. What page? The fifth page in?
MR. HATCH: It's the fifth page in, and it's a Nortel --
COMMISSIONER CLARK: Got it.
Q (By Mr. Hatch) Now, do these numbers appear to be Nortel's numbers for BellSouth's contract purposes?
A Yes.
Q Now, if you look at --
MR. HATCH: May I ask BellSouth's counsel a question? Would the line size designations talking about a particular category be proprietary? I understand. I'm just trying to be careful.
MS. WHITE: I would have to say yes.

BY MR. HATCH:

Q Okay. If you start at the bottom of the line count column, line size, and you count four up.

A Okay.

Q Is that a typical switch size for line counts?

A I'm just trying to think about the different sizes. I mean, that would be one of the switches we deploy. I'm not sure it would be the most -- the one that we deploy the most. I don't know that. But it is a switch we deploy. I would have to look at the Florida data to see that, and I don't remember right off.

Q Would you happen to have an idea about an average Nortel switch size?

A No, I'm afraid not. I would have to look at the data.

Q Do you know whether the numbers in the far right-hand column were the numbers used by BellSouth in its BCPM calculations?

A Okay. Can you repeat the question? I wanted to get --

Q Right. Just looking at the far right-hand column, those numbers, were those the numbers that BellSouth used in its switch calculations for BCPM?

Were those the input values?

A I guess I'm a little bit confused here, because the way SCIS works, you don't input this number. What you have is, you have a material table that you apply the discounts on 257 to.

Q Does SCIS calculate a price per line?

A It's not one of the normal outputs. You can meld -- you can run a special report and do some melding based on lines and calculate that number.

Q Based on the SCIS that you used in this proceeding to generate an input to BCPM, was that number higher or lower than the numbers in the right-hand column generated here?

A That number is higher. But let me just --

Q Than the ones you used as an input?

A Yes, but let me just clarify. The number I remember in mind is the number that's the meld of both the 5E and the DMS, so it would be higher.

Q So you used essentially a weighted average between DMS and Nortel switches?

A Based on --

Q I mean Nortel and Lucent switches. I'm sorry.

A Based on the deployment in Florida, yes, and the planned deployment for the replacements, yes.

Q Did you happen to run any calculations that would show your switch investment if you ran just 5Es?

A Oh, we -- we have the calculation for the 5E switches. We did not rerun the whole State of Florida with only 5E switches, because we would always deplov at a minimum of two vendors.

Q If you're talking about a forward-looking, least-cost network designed from the ground up and built from scratch, could you get a least cost by running one particular switch type?

A Not in the long run you couldn't. If you tie yourself down to one vendor, it doesn't work. They no longer become least cost.

Q Did you make a run, or have you ever made a run looking at just what it would cost if you used Lucent switches, 5Es, for example?

A Not for the entire state.

Q Or for Nortel switches?

A Not for the entire state.

Q When you say not for the entire state, have you done it for any particular territory?

A No. What we've done is run where 5Es are deployed now and plan to be in the future, and then the same analysis for the DMS 100s.

Q Okay. Would you turn over past these

contract pages and look at -- in the upper right-hand corner you'll see Exhibit D handwritten in. This would be page 1 of 2 in the center of the bottom.

MS. WHITE: B as in boy?

MR. HATCH: B as in boy. I mean, D as in dog is the exhibit number, but it's past the contract pages. It's a series of spreadsheets.

THE WITNESS: Could you repeat that? You said Exhibit D?

MR. HATCH: Up in the right-hand corner it has handwritten in it Exhibit D.

THE WITNESS: Yes, I've got that.

MR. HATCH: Okay.

THE WITNESS: Page 1 of 1?

MR. HATCH: Yes. It's actually 1 of 2 is where I am at the bottom.

THE WITNESS: Okay. That's right. I'm sorry.

MR. HATCH: The print is kind of fuzzy.

Q (By Mr. Hatch) If you look at the right-hand column where it says "Lucent Contract Investments," do you see the investment amount there, and then total engineered lines per switch?

A Under the Lucent contract?

Q Yes, under the Lucent.

A Yes, I see those two numbers.
Q And then you see the contract price that we talked about earlier. Do you see that?
A Yes.
Q Then if you look over at Nortel, you'll see a similar comparison.
A Correct.
Q Now, if you look at the far right-hand side, do you see that investment per line number?
A Yes. Mine is kind of cut off, but I think I -- I can read the first three digits pretty well.
Q That investment per line number is higher than the investment per line number that you would get for either the Lucent contract or the Nortel contract price; is that correct?
A All right.
Q Under BC --
A The far right-hand number --
Q The far right-hand number.
A -- is higher than the number under Nortel and Lucent.
Q Right. Now, let me -- that's a correct statement; right?
A Yes.
Q Okay. Now, in the far right-hand column,

that's BellSouth's BCPM weighted investment if you assume 100 new lines. Would that look like an accurate number?

A (Examining document.)

Q Okay. Let's just do it this way. Do you have the investment per line for your weighted average?

A I have a pretty good idea what it is. I don't have it with me, but generally I know what it is.

Q Okay. The number in the right-hand column, is that pretty close to what your weighted average number is? Is it higher or lower than that number?

A It's in the neighborhood of that number, yes.

Q So your weighted average number is significantly different than the investment per line using Nortel or Lucent based on the prices in your Nortel and Lucent contracts; would that be correct?

A I'm sorry. I'm getting a little lost again.

If I'm understanding what you're saying, this number is higher because it is a meld of switches.

Q Right.

A All right. And I would agree with that, but I think I've clearly stated why you have to have a meld of switches. Remember, these contracts are generated with BellSouth with the knowledge that we have more than one vendor in the State of Florida. Well, i. this particular case, in the whole United States.

Q Now, if you ran BCPM based on the input switch values that you used, assuming new lines only, no growth, just assuming new, then would that number be the number in the right-hand column? Does that look like an accurate number?

A I'm sorry. I don't know where these numbers came from, so I'm having some difficulty there. I mean, we didn't generate these numbers, so I don't know how you calculated them.

Q Okay. You may not have the sufficient backup information in front of you. If you look at the Lucent column, and you see the first column under the big Lucent heading.

A Uh-huh.

Q It says "Switch Investment."

A Uh-huh.

Q Now, does that look like an appropriate amount of switch investment for BellSouth for Lucent,

based on total engineered lines, based on the price in your contract?

A All I can say about that is, if you take the investment line you have here and the engineered lines that you have here and made a calculation, it appears that it would be the number in your first column. I would not agree that that is representative of the Lucent vendor charge to BellSouth for placing of switches. It is simply if you assumed you replaced all those lines with a new switch, which I think I've explained is not realistic.

Q Right.

A And also, it's not the total cost. There are things that you don't have. But I do agree with your calculation.

Q Okay.

MS. WHITE: I'm going to object to any further questions along this page, and possibly the next one, from the standpoint that -- I assume this was an exhibit that AT&T put together, and Ms. Caldwell has not been given the basis of where the numbers came from or how it was put together, but she's being asked to agree with it. So I'm not quite sure how she can disagree or agree when she has no information about how it was put together.

MR. HATCH: She is free to agree or disagree.

CHAIRMAN JOHNSON: What was that, Mr. Hatch?

MR. HATCH: If Ms. Caldwell can't agree, then she can't agree.

CHAIRMAN JOHNSON: If you're looking at those numbers and you're confused and you don't know the basis and don't feel that you can respond, tell him that.

THE WITNESS: Okay.

MR. HATCH: No further questions on this.

CHAIRMAN JOHNSON: Is that all?

MR. HATCH: I'm done.

CHAIRMAN JOHNSON: Staff?

MR. COX: Good morning, Ms. Caldwell. Will Cox on behalf of the Commission Staff.

THE WITNESS: Good morning.

MR. COX: Before I begin, Chairman Johnson, I would ask at this time if we could mark for identification an exhibit. The exhibit has the identifier DDC-2 on it. It is the deposition transcript and Late-filed Deposition Exhibit Nos. 1 through 6 of Ms. Caldwell.

CHAIRMAN JOHNSON: It will be identified as

75.

(Exhibit 75 marked for identification.)

MR. COX: Thank you.

CROSS EXAMINATION

BY MR. COX:

Q Ms. Caldwell, for the purposes of the model inputs that BellSouth has put forward in this proceeding, is it correct to say that the telephone plant index, or the TPI, as it's known, is only used by BellSouth to adjust current dollars, whether they be for expenses or for investment, for inflation in the future?

A Yes, the TPIs. But I would like to say inflation or deflation.

Q Just so I'm clear, what exactly is the telephone plant index?

A The telephone plant indices that we use are account specific. They indicate the price change for material that will be anticipated.

In our particular study, we used three years, so each one of them is year over year. We use -- if you look at a '98, '99, 2000, you would have a TPI that would show the price change from '97 to '98, '98 to '99, and '99 to 2000. And what we've done in our study is, instead of using all three of them, we

tried to hit a midpoint of the time frame, and we took the three numbers and straight averaged them. So you had one TPI that would bring it to a representative midyear of that period.

And it is applied to material. That's the one we used.

Q And it's not used for replacement purposes, is it?

A Could I get you to define replacement?

Q Does BellSouth use the TPI to calculate the replacement cost of existing investment?

A No. We use it to take a material -- excuse me, a current material price off of a price list, and then expand that out a time frame.

Q Does BellSouth use any other type of index to adjust its actual numbers?

A The only other one that we use at all is a CC to BC factor. That stands for current cost to book cost. It is only used in one or two calculations, and it's for our factor calculation.

For instance, in the land -- and you don't see those in BCPM as much, but they're easier for me to explain. If you have land, buildings, pole, and conduit, you have a certain embedded investment today, so we take that embedded investment before we do our

A Okay.

Q Now, the table on the top of the page is for 24-gauge aerial cable; is that correct?

A Correct.

Q And this is copper cable?

A Yes.

Q Using 1,200-pair cable as an example, we see that there are several different types of fixed costs associated with the 1,200-pair cable; is that correct?

A Correct.

Q And these costs are per pair foot?

A Yes.

Q The first column shows a material cost of $6.46; is that correct?

A Correct.

Q You see the next column is exempt material, which is $6.35 per pair foot for this cable; is that correct?

A Excuse me just a minute. I need to look back at one other page for something.

Q Okay.

A I want to be sure that I answer this exactly right.

Q Okay.

A All right. Let me -- if I could, please, let me just back up.

Q Sure.

A The cost here is not per pair foot. That is just per foot. So you wouldn't multiply it by 1,200, in other words. It is per foot.

Q Okay. But the first column does show a material cost of $6.46? That was correct?

A That is correct. I agree with that. I think I just answered incorrectly as to what it was representative of.

Q Okay.

A Sorry.

Q And the next column is exempt material, and that's $6.35 per foot, not per pair foot; right?

A Right.

Q For this cable. Now, the exempt material is material that is expensed rather than capitalized, so it is not tracked separately; is that correct?

A That is correct.

Q Now, what might be an example of exempt material?

A One of the major items you have is any terminal that is 100 pair or smaller. That's probably the biggest example. You have splicing enclosures,

things of that type.

Q Now, the next column, taxes, is 39 cents per foot. Now, does this represent the sales tax paid by BellSouth on the cable?

A Correct.

Q And then the column after tax is telco, which is a cost per foot of $16.07; is that correct?

A Correct.

Q Now, what kind of cost does the telco include?

A This particular cable, this is aerial cable, and this is the installation labor. BellSouth employees actually install the aerial cable, so it's the installation labor associated --

Q So that's the labor and time, that sort of thing?

A Yes.

Q How is the cost calculated in this instance for the telco?

A For each one of these categories, we calculated it based on our in-plant factors. The in-plant factors give a breakdown -- if you start -- if you look at a material price and you pay so much, in this particular case, the $6.46 per foot, by the time that particular item of plant is engineered and

installed and actually closes into our capital accounts, it is a much greater number, because you add these particular items to it.

So what we've done is for our in-plant factor develop a relationship between what actually gets closed to the books as capital dollars and what the material price was. And we used the 1997 time frame for that calculation for the in-plant.

Q The column to the right of telco is titled "Contract."

A Yes.

Q And it shows a cost of $2.94.

A Yes.

Q Now, does this represent contractor labor?

A Yes, it does.

Q Is there anything else included in that?

A No. Excuse me. No.

Q And how is that cost calculated?

A It would be the same. Our in-plant factor is just the contract portion of it. See, the in-plant factor can be broken down into the categories across the top, exempt material, tax, telco, contract, and engineering.

Q Now, the next column, the engineering column which you just mentioned, shows a cost of

$2.57?

A Correct.

Q Does this represent the cost of BellSouth's engineers?

A Yes, it does.

Q Is anything else represented in that cost?

A No, it does not.

Q The total cost of the 24-gauge aerial cable then is $34.78, and that's per foot; correct?

A Correct.

MR. COX: Thank you, Ms. Caldwell. That concludes Staff's questions.

CHAIRMAN JOHNSON: Commissioners?

COMMISSIONER JACOBS: Ms. Caldwell, on page 9 of your testimony, you discuss how the telephone price indices are used, and I wonder if you could just walk me through. You indicated that in certain accounts you add inflation factors, and in others you use forecasts to lower the actual cost. Could you tell me how that's determined, how it's calculated?

THE WITNESS: Okay. If you look at copper cable, the material price of copper is just increasing, so for that particular item, your in-plant factor would be a little greater than 1. So that

would be an example of the inflation.

If you look at switching, the electronic switching, it's almost constant. It's almost 1.

And some of your digital loop carrier, since you have advances in electronics, that's going down, so those would be below 1.

So those are how we used ther. Every account has its own factor.

COMMISSIONER JACOBS: Okay. I notice in one of the GTE witnesses, I believe it was Mr. Tardiff, he had a trend table attached to his. Have you done any trending of these to see how they perform over time?

THE WITNESS: Yes, we have done some trending in the past to show that, and it supports just what I said, that copper is actually slightly increasing, switching has leveled out, and fiber and electronics is slowly going down.

COMMISSIONER JACOBS: And the calculations that you used for input to the model, they're the most recent, I think I heard you say; right?

THE WITNESS: Yes, they are.

COMMISSIONER JACOBS: Okay. Thank you.

CHAIRMAN JOHNSON: Redirect?

MS. WHITE: Yes, I just have a few.

REDIRECT EXAMINATION

BY MS. WHITE:

Q Ms. Caldwell, Mr. Melson asked you several questions comparing the inputs used by GTE and Sprint to those used by BellSouth. Could you tell me whether you believe it's appropriate to compare those inputs betweer the different companies?

A Not on an individual basis. I think I've said you have to look at the contract as a whole. If you look at just Sprint's buried cable and BellSouth's buried cable, you may get a distorted view. But if you look at poles and buried cable as a whole, you'll find that the overall contracts are what you really need to consider.

And in fact, if you look at Sprint's final investment on a per line basis that they filed in their testimony, you will find that it is within -- the overall investment is within a dollar or two of what BellSouth's is. So I think when you look at the overall impact, you'll see they're very close. Again, overall is what's important.

Q Okay. Mr. Melson also asked you about the per duct material cost for conduit of $2.24, I believe.

A Correct.

Q What is included with that $2.24?

A The $2.24 on that particular page was what we pay for the conduit. And if I could, let me just glance back at that sheet to be sure that I have everything that's in that. There are so many numbers.

Yes. I just wanted to verify for this particular item. The 2.24 includes the material as well as the installation of that particular material.

Q What would be the material?

A The material would be in this particular case the plastic PVC pipe that you run the cable through. The installation would be the actual physical placing in the ground of that conduit, which can be quite costly.

Q Mr. Cox asked you about the inclusion of nonrecurring costs in the cost of basic local service, and I believe your answer was that they should be included?

A Correct.

Q Have they been excluded from other expenses?

A There are no double-dipping in those expenses. That is the only place they are included, one and only one time.

MS. WHITE: Okay. Thank you. That's all

I have.

CHAIRMAN JOHNSON: Exhibits?

MS. WHITE: BellSouth moves Exhibit 73.

CHAIRMAN JOHNSON: Show that admitted --

(Exhibit 73 received in evidence.)

MR. HATCH: Madam Chair, this is going to be a little bit complicated, because what I would like to do as Exhibit 74 is move the first five pages. They are labeled Exhibit A through Exhibit C on those pages. Exhibit D and beyond, which is the spreadsheet, I am not moving as part of Exhibit 74. That's why I labeled it as Switch Vendor Contract Extracts.

CHAIRMAN JOHNSON: Tracy, I couldn't hear you.

MR. HATCH: Okay. So as not to completely confuse everybody, which I probably have, when I handed out the document, the switch vendor contract, the portions of that, I would like to move that exhibit.

MS. WHITE: Did you say you're going to move all that was in the red folder?

MR. HATCH: No. That's why I made sure that from Exhibit D, which is the spreadsheet, which is that, I am not moving.

MS. WHITE: Exhibit D you are not moving?

MR. HATCH: And Exhibit E to that I am not moving, just the contract pages.

MS. WHITE: Okay. All right. Thank you.

CHAIRMAN JOHNSON: All right. So Exhibits D and E are not being moved?

MR. HATCH: They're not included as part of Exhibit 74; that is correct.

CHAIRMAN JOHNSON: Show that admitted without objection.

(Exhibit 74 received in evidence.)

CHAIRMAN JOHNSON: We've admitted 73 and 74.

MR. COX: Chairman Johnson, Staff moves Exhibit 75.

CHAIRMAN JOHNSON: Show that admitted without objection.

(Exhibit 75 received in evidence.)

CHAIRMAN JOHNSON: Thank you.

THE WITNESS: Thank you.

CHAIRMAN JOHNSON: We're going to take a 15-minute break.

(Short recess.)

CHAIRMAN JOHNSON: We're going to reconvene the hearing. GTE?

MR. MITCHELL: Tom Mitchell for GTE. GTE calls Mike Norris. I do not believe that Mr. Norris has yet been sworn, nor Mr. Tucek, GTE's next witness.

COMMISSIONER JACOBS: It your mike on?

CHAIRMAN JOHNSON: If you've not been --

MR. MITCHELL: I'm sorry. Mr. Tucek is not here.

CHAIRMAN JOHNSON: Okay. Anyone in the room who will be testifying, if you're not been sworn, if you could stand and raise your right hand.

(Witness sworn.)

CHAIRMAN JOHNSON: You may be seated.

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MICHAEL R. NORRIS

was called as a witness on behalf of GTE and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. MITCHELL:

Q Mr. Norris, would you please state your full name and business address for the record, please.

A My name is Michael R. Norris. My business address is 600 Hidden Ridge, Irving, Texas, 75015.

Q You're employed with GTE?

A Yes, I am.

Q In what capacity?

A Cost, Manager of Cost Development.

Q In this proceeding, Mr. Norris, did you prepare or cause to be prepared direct testimony dated August 3, 1998, consisting of seven pages?

A Yes, I did.

Q Do you have any changes or corrections to make to that testimony?

A No, I do not.

Q And attached to your direct testimony, were there three exhibits designated MRN-1 through MRN-3?

A Yes.

Q Did you also cause to be filed revised exhibits to your direct testimony designated MRN-1 through MR -- excuse me, MRN-1R through MRN-3R?

A Yes, I did.

GTE FLORIDA INCORPORATED

DOCKET NO. 980696-TP

DIRECT TESTIMONY OF MICHAEL R. NORRIS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Michael R. Norris. My business address is 600 Hidden Ridge Drive, Irving, Texas, 75038.

Q. BY WHOM AND IN WHAT CAPACITY ARE YOU EMPLOYED?

A. I am employed by GTE Service Corporation as a Manager – Cost Models and Methods Development. In this capacity, I am responsible for developing cost models, methodology and analysis.

Q. BRIEFLY DESCRIBE YOUR EDUCATIONAL BACKGROUND AND WORK EXPERIENCE.

A. I received a Master of Business Administration degree from Southern Illinois University - Edwardsville in 1988 and a Bachelor of Science degree in Business Administration from Lindenwood College. I began my telecommunications career as a Staff Engineer with Contel in 1969. I became a GTE employee in 1991, when the companies merged. During my career, I have held various positions dealing with capital recovery, rate design, tariff development, toll settlements and cost studies, rate case preparation, regulatory accounting, and strategic planning. I accepted my current position in May 1997.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY STATE OR FEDERAL REGULATORY COMMISSIONS?

A. I have sponsored testimony before the state utility commissions of Arkansas, California, Hawaii, Indiana, New Mexico, Oklahoma, South Carolina and Texas.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The Florida State Legislature has directed this Commission to select a cost proxy model to estimate the total forward-looking cost of providing basic local service. My testimony discusses how the expense levels shown in GTE witness Mr. Olson's testimony were developed into inputs for use in the Benchmark Cost Proxy Model ("BCPM").

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. There are three types of expense inputs required within BCPM: capital-related expenses, expressed as a percent of investment; non-capital-related expenses, expressed on a per-line basis; and general support asset ratios. My testimony covers the development of each of these three areas of expense inputs into BCPM.

Q. PLEASE DESCRIBE GENERALLY THE PROCESS OF DEVELOPING BCPM OPERATING EXPENSES INPUTS.

A. The starting point for developing BCPM expense inputs is the ARMIS adjusted expenses described in the testimony of GTE witness Mr.

Olson. For purposes of BCPM, the adjusted ARMIS expenses discussed by Mr. Olson are further adjusted to remove expenses associated with non-recurring costs, billing and collection costs associated with toll and access, and directory costs. These adjusted expense amounts are then mapped to cost pools. Finally, the expense information mapped to the cost pools is used to calculate the three types of expense inputs required by BCPM.

Q. PLEASE EXPLAIN IN MORE DETAIL THE ADJUSTMENTS YOU MADE TO THE ARMIS ADJUSTED EXPENSE DATA.

A. As mentioned previously, there are three adjustments made to the ARMIS levels of expense provided by Mr. Olson. The first adjustment removes incurred costs that are associated with the provision of non-recurring activities. These costs are recovered through non-recurring charges associated with service order activity and as such must be removed so as not to recover the same expense twice.

The second adjustment removes operating expense associated with toll and access billing and collection activities, because these activities are not related to the provision of basic local telecommunications service.

The third adjustment removes expense associated with the provision of directory services from the cost pool analysis. GTE develops its expense for FCC purposes and this adjustment is made to recognize

that the FCC does not include directory listing in its definition of supported services for universal service purposes. GTE witness Mr. Tucek, however, separately identifies the per-line cost of the listing in his testimony, in order to accommodate the Florida statute's inclusion of a directory listings in its basic service definition. In calculating the size of the universal service fund, GTE witness Mr. Seaman has, likewise, included directory listing cost.

Q. WHY DOES GTE UTILIZE THE COST POOL MAPPING PROCESS TO DETERMINE THE ASSIGNMENT OF OPERATING EXPENSES?

A. This process allows GTE to better align its costs with those parts of GTE's network or operations from which the costs are generated. Better assignment of cost to the elements of the network or operations allows for a more accurate assignment of costs to the products and services that GTE provides.

Q. PLEASE EXPLAIN THE COST POOL EXPENSE ASSIGNMENTS IN MORE DETAIL.

A. The starting point for assigning expense and investment to cost pools is state-specific, 1997 USOA ARMIS data. The ARMIS account data, at a budget center level of detail, is then assigned to work centers, which are, in turn, assigned to the cost pools.

Budget centers are the organizational units used to track costs. Budget centers are aligned with the hierarchical and functional

structure of GTE. A workcenter is a collection of budget centers that perform similar activities or functions. The GTE Finance Organization performed the budget center to workcenter mapping.

Workcenters are assigned to cost pools based on the Finance Organization's analysis of the functions performed in the workcenters. There are 20 different cost pools--pole, buried cable metallic, aerial cable metallic, billing and collection, and common are a few examples.

The attached Exhibit MRN-1 shows the detailed results of the expense account cost pool assignment process. Exhibit MRN-2, also attached, summarizes cost pool assignments into BCPM-required input format.

Q. HOW ARE INPUTS FOR EXPENSES RECOVERED AS A PERCENT OF CAPITAL-RELATED INVESTMENT DEVELOPED FOR BCPM?

A. Expense to capital-related investment ratios associated with ten designated capital accounts (which include costs related to Central Office and Transmission Equipment, Poles, Conduit, and Aerial, Underground and Buried Cable) are developed utilizing the results of the cost pool assignment process described earlier. Expenses used in the numerator, to calculate expense to capital-related investment factors, are taken from the relevant expense developed by cost pool. The denominator in the calculation is taken from the respective

investment cost pool after being adjusted by the C.A. Turner index. Expense as a percent of capital-related investment inputs are applied to the network plant investment developed within BCPM.

Q. PLEASE EXPLAIN THE C.A.TURNER INDEX AND WHY IT IS USED WITH THE CAPITAL ACCOUNTS.

A. The C.A.Turner Telephone Plant Index is published by AUS Consultants, the successor company to Associated Utility Services, Inc. These indices are applied to each vintage year of a plant account to determine the reproduction cost of embedded plant, (i.e., the cost in today's dollars). By utilizing the C.A.Turner Index in the development of capital-related expenses, we are better able to model the relationship of expense levels to the investment levels produced within BCPM.

Q. HOW WERE EXPENSE INPUTS FOR NON-CAPITAL RELATED EXPENSES DEVELOPED?

A. Non-capital-related expense inputs to BCPM are expressed on a per-line basis. There are eight non-capital expense categories: Network Support, General Support, Network Operations, Marketing, Customer Services, Executive & Planning, General & Administration, and Uncollectibles. GTE develops the non-capital-related cost inputs from the expense data assigned to the consumer, business and common cost pools. These amounts are then multiplied by the local direct cost percentage (i.e., the percentage of local calls to total calls) to

determine the portion of the expense associated with local services. These amounts are then divided by access lines to determine the monthly per-line expense that is input into BCPM.

Q. HOW WERE THE SUPPORT RATIO INPUTS FOR GENERAL SUPPORT ASSETS DEVELOPED?

A. There are six accounts of general support assets. These accounts are Motor and Special Purpose Vehicles, Furniture, Computers, Office Equipment, Garage Equipment, and Other Work Equipment. The percentage inputs for these accounts are a ratio of each of the respective general support asset accounts to the total Plant in Service for GTE Florida. The amounts used to calculate these ratios are the investments from the 1997 ARMIS reports as adjusted by the C.A. Turner Index.

Q. HAVE YOU PROVIDED AN EXHIBIT THAT SUMMARIZES THE RESULTS OF THESE CALCULATIONS AND DETAILS THE BCPM INPUTS?

A. Yes, the inputs and results are reflected in attached Exhibit MRN-3 This information is also included in GTE witness Mr. Tucek's Exhibit DGT-1, page 11.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

Q (By Mr. Mitchell) Mr. Norris, have you prepared a summary of your direct testimony?

A Yes, I have.

Q Would you please give that at this time?

A Yes.

Good morning. Of the many input requir ents of proxy models, operating expenses are one of the primary components of cost models. The purpose of my testimony is to provide for the development of the GTE company-specific operating expense inputs that are required within BCPM.

BCPM allows for operating expense inputs in two ways, first, expense as a percent of investment. These expense inputs are development in the calculations to be based on operating expense related to network plant components.

The second input provides for expense on a per line basis. The expenses that are input on a per line basis are related to network and general support and administrative type functions.

The level of operating expenses used in the development of BCPM inputs is based on GTE's actual expense incurred for 1997 as reported in ARMIS. I have made adjustments to these in three areas. First, I have removed expenses associated with nonrecurring

services. Second, I have removed operating expense associated with billing and collection activities related to toll and access. And third, I have removed operating expense associated with directory services. These adjusted expenses are then used to develop expense-to-investment ratios and expense per line inputs as required by BCPM. These expenses are based on GTE's actual cost experience for 1997 and provide a reasonable representation of the level of operating expenses of GTE of Florida.

Thank you.

MR. MITCHELL: Madam Chairman, at this time I would move for the admission of Mr. Norris's direct testimony into the record.

CHAIRMAN JOHNSON: It will be admitted.

(Prefiled testimony of Mr. Norris inserted at page 2203 for the convenience of the record.)

MR. MITCHELL: And I would also asked that the revised exhibits to Mr. Norris's testimony be marked for identification, that is, Exhibits MRN-1R through MRN-3R.

CHAIRMAN JOHNSON: They will be marked as stated and identified as 78.

MR. MITCHELL: Thank you. Mr. Norris is available for cross examination.

MR. COX: Chairman Johnson, before we begin cross examination, Staff would ask that we mark as an exhibit the deposition transcript of Mr. Norris, which is identified as MRN-4.

CHAIRMAN JOHNSON: It will be marked as 79.

MR. COX: I think we may be one number off.

CHAIRMAN JOHNSON: Oh, we're two numbers off. I went from -- the first one should have been 76. I'm sorry. So GTE's first exhibit, MRN-1R through MRN-3R, is Exhibit 76, and Staff's will be 77.

MR. COX: Thank you.

(Exhibits 76 and 77 marked for identification.)

CHAIRMAN JOHNSON: The witness has been tendered?

MR. MITCHELL: Yes, he has.

MR. COKER: Thank you.

CROSS EXAMINATION

BY MR. COKER:

Q Mr. Norris, my name is Gene Coker. I represent AT&T.

You had mentioned that you made some adjustments to the expense inputs that you've suggested.

First of all, what you're doing is taking

the expense levels generated by Mr. Olson and converting them into an expense input to BCPM; is that correct?

A Generally that's true, yes.

Q And you adjusted -- in making the adjustments that you made, one of the adjustments is to remove the nonrecurring costs; is that correct?

A That's true.

Q Now, why is it appropriate to remove nonrecurring costs from your calculations?

A Well, generally nonrecurring costs are recovered through other rates. And in Mr. Seaman's calculations, it's my understanding at least, he did not include the revenue streams from nonrecurring costs in his calculations; thus, we removed the operating expenses associated with nonrecurring services from our calculations.

Q In response to -- I believe it was Interrogatory 36, GTE filed a large document. I think it's commonly referred to as a Bates stamped document. Are you familiar with those?

A Yes.

Q Do you have a copy of those with you?

A Of No. 36?

Q Well, I'm particularly interested in Bates

stamped document 0002225.

A 2225?

Q Yes, sir.

A Yes, I have that.

Q Now, is that -- in that document in the -- there's a column labeled "Nonrecurring Expenses." Are those the specific nonrecurring expenses that you eliminated from your calculation?

A Yes, they are.

Q About the middle of the page, item 6423, buried cable expense, can you tell me why you eliminated nonrecurring expenses associated with that?

A Generally I can tell you that we have a group of people who prepare nonrecurring cost studies, and through their process of identifying costs associated with their nonrecurring cost studies and the costs that they've identified that are part of that determination, these are the costs that they have included in those calculations. As to the specifics of what they have done in their nonrecurring cost studies, I could not address that, no.

Q All right, sir. If I inquired about all of those entries that you have there, your answer would basically be the same; is that right?

A It would be the same, yes.

Q I would like to talk just a minute about the expenses recovered as a percent of capital. This calculation uses embedded investment adjusted by the C. A. Turner index; is that correct?

A Yes.

Q And can you tell me what the C. A. Turner index is?

A The C. A. Turner index is an index that's developed by the Associated Utilities Services, I think now known as AUS. That factor -- those indices are developed by them from their analysis and the valuation of plant over years of their observances, and the factors are designed to bring plant levels up to a current replacement level of value.

Q So what you've done here in your calculation is to take the embedded plant and express it in today's dollars?

A Essentially, yes.

Q Isn't a cost model supposed to produce a forward-looking cost based on the most recent and currently available technology?

A Yes.

Q Is there anything in the Turner index that would adjust for new technologies that are introduced into the network, or is it just an update of

historical dollar values?

A I'm not specifically knowledgeable about the AUS indices, but it's my understanding that essentially they take into account some of the effects of changes on technology.

The way we are using this is to develop a level of plant from the book levels of investment that essentially are equivalent to today's current dollars that then match up with the investments, the forward-looking investments that are generated out of BCPM.

Q Would it be fair to say then that the application of this Turner index is more of an accounting adjustment than a recognition of new technology?

A I wouldn't necessarily characterize it as an accounting adjustment, no. It's designed to restate investment levels from your books to a current replacement level. And we then utilize it to divide into our operating expenses to develop the expense-to-investment ratios that go into BCPM that are then applied to the investments that are developed within the BCPM model.

Q Do you have any idea what the Turner index is for switching equipment in general?

A That we applied?
Q Yes.
A The factor that we used in our calculation was a composite factor for digital switching of .7025.
Q And what does that mean, that particular factor mean? Can you translate that into simple terms tha' I could understand?
A Well, essentially what that says is that the investment level that is calculated from using that would be about 70% of whatever your book value is.
Q Now, other than bringing the embedded investment up to today's dollar values, what other steps did you take to make your proposed inputs forward-looking?
A In addition to the C. A. Turner?
Q Yes.
A We removed any electromechanical and analog operating expenses. We removed any aerial wire expenses.
Q Is that all?
A Yes.
Q You have included in your operating expense input product advertising as a portion of the marketing expense, haven't you?

A Yes.
Q And is that related to a specific account?
A Yes, it is.
Q Which account is that?
A Account 6613.
Q And does that particular account identify advertising expenses associated only with the provision of basic local exchange service?
A No, it does not.
Q Did you make any adjustment to reflect the advertising for only basic local exchange service?
A In the sense that as you get into our common costs, or the cost that we include in our common cost pool, and those things that ultimately end up in those factors, we had done a calculation to identify those expenses that are associated with local services on the basis of the relationship of local calls to total calls.
Q In your deposition, do you recall stating that it was appropriate to include this expense because there was some advertising, some instructional advertising on how to use basic local service?
A Yes.
Q And do you remember the example that you used?

A I think what I said was that we do advertising today, and it is related to informational or instructional. I don't remember a specific example now.

Q Do you recall using Star-69 as an example?

A Yes, I believe that's true.

Q Is that part of basic local exchange service, or is that an optional service for which an additional fee is paid?

A It would be a vertical service.

Q So that really wouldn't be part of basic local exchange?

A I don't believe so, no.

Q Are you aware of any advertising that is limited solely to the provision of basic local exchange service?

A Specifically?

Q Yes, sir.

A No.

Q Again I would like to ask a question about an item that came up in your deposition. Do you recall -- in speaking about operating expenses, do you recall saying something to the effect that GTE doesn't foresee any change in the way it operates or it will operate over the foreseeable future, meaning the next

three to five years?

A Yes.

Q And by that did you mean that you anticipated your operating expenses to remain relatively flat?

A Yes, I did. I think what I said was that given the fact that GTE had just gone through a fairly extensive process of re-engineering effort and had re-evaluated the systems and processes related to its operations, that I didn't see any change in the way that GTE does business today over the next three to five years, and that those expenses would remain relatively flat.

Q To the extent that your operating expenses remain flat and your access lines continue to grow, won't that result on a per unit basis in a decline in expenses?

A It will not create a decline in expenses. It will create a -- assuming that access lines in fact would increase over time, you would see -- and operating expenses do remain flat, you would see a decrease in expense per line, yes.

Q Okay. That's what I meant by a per unit basis. Expenses per line, that would decline?

A You would see that occurring. I thought

what you said was would you see operating expenses decline, and I'm saying that I would not necessarily expect operating expenses to decline.

Q But just by virtue of having the number of lines increase and the expenses stay flat, the math ends up with an expense per line in a downward trend?

A Yes, as the opposite would happen if access lines would decrease.

Q Would you agree that one of the benefits of competition is lower costs?

A I don't know that I -- that's a little beyond the scope of my testimony. I don't know that I would be the one to answer that.

Q Well, let's -- for purposes of my question, we'll make it a hypothetical, and I would ask you to assume that that is one of the benefits of competition. Would you agree that based on that assumption, that as competition develops more intensely that the pressure to be more cost-efficient grows as well?

A Generally I would say that's true.

Q Based on your testimony a few minutes ago that your operating revenues will remain flat -- they have been flat over the last couple of years; is that correct?

A Operating expenses?
Q Yes.
A Yes.
Q And your opinion or GTE's opinion that it's going to remain that way for the next three to five years, could we conclude from that that the level of competition has not and will not change over that p riod of time for basic local exchange service?
A I don't know that you could conclude that, no.
Q Can you draw any conclusions from the fact that your operating expenses are going to remain flat for three to five years and have been flat the last couple of years, and compare that to the hypothetical situation where as competition develops, the pressure to decrease costs are going to become greater?
A Well, again, GTE has just gone through and re-evaluated its systems and its processes, and has those things in place since 1996, and I would not expect even the introduction of competition to affect that, generally that operations over the next three to five years.
Q Well, I thought you told me a few minutes ago that based on the assumption that one of the benefits of competition is lower costs, that the

greater the degree of competition, the greater the pressure to reduce costs.

A Well, I said generally I would agree with that statement, yes.

Q Well, isn't that in conflict with what you just told me?

A I don't believe so.

Q And why is that?

A Well, again, for the most part, as competition starts to enter GTE's area -- we're talking about the operations of GTE, and as competition starts to enter the area, those people that deal with our retail services today would start to deal with the wholesale sides of the services. I would not expect then the level of -- overall level of operating expenses to change over time.

Q So is it -- just so I'm clear on this, is it your opinion that an increasing level of competition will have no effect on GTE's level of operating expenses over the next three to five years?

A I don't believe it will, no.

Q Mr. Norris, isn't it true that it has been reported that there's going to be a $2 billion cost synergies over the next -- over a three-year period as a result of the GTE-Bell Atlantic merger?

A That's what I understand, yes.

Q Have you taken that into account in making your adjustments?

A No, I have not.

MR. COKER: Madam Chairman, that's all I have.

CHAIRMAN JOHNSON: MCI?

MR. HENRY: We have no questions.

CHAIRMAN JOHNSON: Okay. Staff?

MR. COX: Staff has no questions.

CHAIRMAN JOHNSON: Commissioners?

COMMISSIONER JACOBS: Mr. Norris, is it true that -- well, let me ask it this way. In your opinion, would you expect that there would not be any cost -- economies of scale or cost efficiencies that would occur through the development of second lines, the greater deployment of second lines in homes in local service?

THE WITNESS: I'm sorry. I'm having a little bit of difficulty hearing you. Are you saying that --

COMMISSIONER JACOBS: As second lines become more prevalent in local service, you don't see any cost economies that derive from that?

THE WITNESS: For second lines?

COMMISSIONER JACOBS: Yes.

THE WITNESS: Generally I would say probably not. A line is kind of a line that is part of the network, and the cost to maintain a second line into a home is generally, I would say, going to be about the same as the cost of the first line.

COMMISSIONER JACOBS: So you're going to have duplicate -- you're going to simply double the cost for a second line?

THE WITNESS: I'm sorry?

COMMISSIONER JACOBS: In your example, you would double the cost for a second line?

THE WITNESS: I would not.

COMMISSIONER JACOBS: You would not?

THE WITNESS: No.

COMMISSIONER JACOBS: Okay. So there will be some economies? As more second lines are deployed, will there not be some economies there?

THE WITNESS: Are you speaking relative to a cost per line decreasing?

COMMISSIONER JACOBS: Yes, yes.

THE WITNESS: Yes. As you add second lines, the cost per line would in fact decrease, yes. I would agree with that.

COMMISSIONER JACOBS: Okay. Thank you.

COMMISSIONER JOHNSON: Redirect?

MR. MITCHELL: No redirect.

CHAIRMAN JOHNSON: Exhibits?

MR. MITCHELL: GTE would offer and ask that what has been marked as Exhibit 76 be inserted into the record.

CHAIRMAN JOHNSON: Show it admitted without objection.

(Exhibit 76 received in evidence.)

MR. COX: Staff moves Exhibit 77.

CHAIRMAN JOHNSON: Show that admitted without objection.

(Exhibit 77 received in evidence.)

CHAIRMAN JOHNSON: Thank you.

MR. MITCHELL: GTE's next witness is David Tucek.

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DAVID G. TUCEK

was called as a witness on behalf of GTE and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. MITCHELL:

Q Good morning, Mr. Tucek. Would you please state your full name and business address?

A My name is David G. Tucek. My business

address is 1000 GTE Drive, Wentzville, Missouri.

Q Mr. Tucek, where are you employed and in what capacity?

A I'm employed by GTE as Staff Manager of Economic Issues. In this capacity, I'm responsible for supporting GTE's incremental cost studies.

Q Mr. Tucek, in this proceeding did you prepare direct testimony dated August 3rd that is 12 pages long?

A Yes, I did.

Q Do you have any corrections or changes to make to that direct testimony?

A I have three minor corrections.

Q What are they?

A On page 3 of the direct at line -- excuse me. Yes, on page 3 of the direct at line 3, the number $33.08 should be $32.67. On line 7 of that same page, the number 40 cents should be 34 cents.

Q Do you have any other changes?

A Yes, thank you. On page 7 at line 3, the value 86.0% should read 85.5%.

Q Is that all?

A That's all the changes to the direct.

Q Mr. Tucek, with those changes in mind, if I asked you the same questions that are in your direct

testimony, would your answers be the same as they exist and as you've changed them?

A Yes, they would.

Q Mr. Tucek, did you also cause three exhibits to be filed with your direct testimony marked DGT-1 through DGT-3?

A Yes, I did.

Q Have you also caused to be filed revisions to those three exhibits that are marked DGT-1R through DGT-3R?

A Yes, I did.

Q Mr. Tucek, did you also file rebuttal testimony in this proceeding?

A Yes, I did.

Q Rebuttal testimony dated September 2, 1998, consisting of four pages?

A That's correct.

Q Any changes or corrections to make to that testimony?

A I have one change. On page 2 at line 9, the sentence beginning with the word "additionally" should be stricken. And that's all the changes to the rebuttal testimony.

Q There are no exhibits to your rebuttal testimony?

A No, there are not.

MR. MITCHELL: Madam Chairman, at this time I would move for the admission of Mr. Tucek's direct and rebuttal testimony into the record.

CHAIRMAN JOHNSON: It will be inserted.

GTE FLORIDA INCORPORATED

DIRECT TESTIMONY OF DAVID G. TUCEK

DOCKET NO. 980696-TP

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is David G. Tucek. My business address is 1000 GTE Drive, Wenizville, Missouri.

Q. BY WHOM ARE YOU EMPLOYED, AND IN WHAT CAPACITY?

A. I am employed by GTE as Staff Manager - Economic Issues. In this capacity, I am responsible for supporting GTE's incremental cost studies.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE.

A. I have a Bachelor of Science Degree in Mathematics and Economics from Southeast Missouri State University, and a Master of Arts Degree in Economics from the University of Missouri. I also have a Master of Business Administration from St. Louis University. I began my career in the telecommunications industry as a Senior Cost Analyst with Contel Service Corporation in 1979. I became an employee of GTE in 1991, at the time of the merger between the two companies. During the course of my career, I have held various positions dealing with cost analysis and modeling, rate design, tariff

development, carrier billing, and demand analysis. I assumed my present position in August of 1996.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY STATE OR FEDERAL REGULATORY COMMISSIONS?

A. I have testified as an expert witness before the state utility commissions in Alabama, Arkansas, Hawaii, Illinois Iowa, Kentucky, Michigan, Missouri, New Mexico, Nebraska, North Carolina, Pennsylvania, and Washington. I have also sponsored expert testimony before the Interstate Commerce Commission.

2231

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony presents GTE-specific inputs that should be used to populate the Benchmark Cost Proxy Model ("BCPM") in lieu of the default inputs provided by the model sponsors. I also present the results of the BCPM run using these inputs.

Q. WHAT EXHIBITS ARE YOU SPONSORING?

A. I am sponsoring the following exhibits, which are appended to my testimony:

1. Exhibit DGT-1 GTE's Company-Specific Inputs for BCPM;
2. Exhibit DGT-2 A CD-ROM containing BCPM Populated with GTE's Company-Specific Inputs; and
3. Exhibit DGT-3 A Binder Containing the BCPM Model Run Results.

Q. WHAT WAS THE RESULT OF THE BCPM RUN?

A. Based on the inputs described below, the cost of basic local telecommunications service produced by BCPM is $33.08 per line, per month. This figure excludes the cost of a standard white page directory listing, which is included in Florida's statutory definition of "basic local telecommunications service." (Fla. Stat. sec. 364.02(2).) GTE estimates the directory listing cost to be $0.40 per line, per month.

Q. PLEASE IDENTIFY WHAT TYPES OF INPUTS GTE HAS DEVELOPED FOR USE IN BCPM.

A. GTE changed BCPM's default values for the following inputs:

(1) cost of money;

(2) depreciation lives and salvage values;

(3) wire center line counts;

(4) tax rates and lives;

(5) fill factors;

(6) structure mix assumptions;

(7) structure sharing assumptions;

(8) spacing assumptions for poles, manholes, and guy wires and anchors;

(9) special access line factor.

GTE also changed the following inputs related to switching and transport costs:

(1) percent local calls;

(2) percent residence lines;

(3) switch percent line fill;

(4) land and buildings loading factors;

(5) processor-related investment by wire center;

(6) MDF and protection investment by wire center;

(7) line port investment by wire center;

(8) line CCS investment by wire center;

(9) trunk CCS investment by wire center;

(10) SS7 investment by wire center;

(11) usage inputs dealing with calls per line, CCS per line, and CCS per trunk;

(12) line-to-trunk ratio;

(13) percent of local calls that are interoffice;

(14) call completion fraction; and

(15) maximum number of nodes on a SONET ring.

Additionally, GTE's BCPM inputs are based on GTE-specific input prices for the following items: (i) manholes; (ii) conduit systems; (iii) poles; (iv) guy wires and anchors; (v) NIDs and drops; (vi) cross-connect boxes; (vii) copper cable; (viii) fiber cable; and (ix) Digital Loop Carriers ("DLCs"). Finally, GTE utilized ARMIS and general ledger data for 1997 to develop the inputs for network support ratios and for operating expenses. All of the GTE company-specific inputs for BCPM are presented in Exhibit DGT-1.

Q. HOW DID GTE DETERMINE WHICH COMPANY-SPECIFIC INPUTS TO PROPOSE IN LIEU OF THE BCPM DEFAULT VALUES?

A. The company-specific inputs GTE proposes in lieu of the BCPM default values were selected based on:

(1) the materiality with which the inputs affect costs, and

(2) GTE's ability to develop the company-specific inputs in the format required by BCPM in the time allowed.

For example, the cost of money, depreciation, line counts and the various expense factors are inputs which affect all aspects of the network and which are easily understood. Likewise, the inputs for structure mix, sharing, and the prices of cable and the other outside plant components largely determine the cost of the loop, which makes up roughly 73 percent of the total cost per line. GTE changed these inputs because of their relative importance to overall costs. Similarly, GTE used company-specific inputs for switching costs because they account for roughly 14 percent of the total cost per line. At this point in time, GTE has not been able to develop company-specific values for every model input and GTE reserves the right to introduce additional input values in any future proceedings.

2234

Q. WHAT COST OF CAPITAL DID GTE USE?

A. GTE used a risk-adjusted, forward-looking rate of return of 12.65 percent. Development of this value is presented in the testimony of GTE witness James H. Vander Weide.

Q. WHAT DEPRECIATION LIVES AND SALVAGE VALUES WERE USED?

A. The lives and salvage values used are those sponsored by the testimony of GTE witness Allen E. Sovereign.

Q. WHAT WIRE CENTER LINE COUNTS DID GTE USE?

A. GTE used its actual wire center line counts as of year-end 1997. In addition to single-party business and residence lines, the line counts include multi-line business, special access, private lines and multiple residential lines.

2235

Q. WHAT TAX RATES AND TAX LIVES WERE USED?

A. The tax rates of 35.0% federal, 5.50% state, 1.17% *ad valorem*, 0.02% other, and 3.03% gross receipts tax were used for Florida. The BCPM default values for tax lives were used for all accounts except for Motor Vehicles, Special Purpose Vehicles, Furniture, and Office Support. For these accounts, tax lives of 5, 5, 7, and 7 years were used, respectively.

Q. WHAT FILL FACTORS WERE USED FOR FEEDER, DISTRIBUTION AND SWITCHING?

A. Values of 65 and 98 percent were used for feeder and distribution plant, respectively. The 65 percent value represents a GTE-specific upper limit for the average feeder fill, based on GTE's operations across the country. For GTE's Florida operations, the actual average

feeder fill is 52.7 percent. The 98 percent factor for distribution reflects the need for administrative spare. For switching, the GTE national average value of 86.0 percent was used, which is comparable to GTE's 85.7 percent state average for Florida.

Q. WHAT STRUCTURE MIX INPUTS WERE USED?

A. GTE replaced the default values of BCPM for the mix of aerial, buried and underground plant with the actual percentages of plant mix for Florida based on the density of GTE wire centers.

2236

Q. WHAT STRUCTURE SHARING INPUT VALUES DID GTE USE?

A. GTE has used structure sharing inputs based upon GTE's actual experience in Florida. GTE's pole sharing input for normal and soft rock placement is 53.58 percent; for hard rock placement, the sharing input is 54.52 percent. These percentages are based on the number of poles to which GTE attaches, and on whether or not GTE is the only utility using the pole. The sharing and price inputs for poles represent a composite of 30 foot non-shared poles and 40 foot shared-use poles. There is no distinction between normal and soft rock placement because GTE's existing vendor contracts for pole placement do not make this distinction. Likewise, the sharing inputs of 100 percent for buried placement and 97.18 percent for conduit and manholes reflect GTE's current experience in Florida and the assessment of GTE operating personnel in Florida.

Q. WHY IS IT APPROPRIATE FOR GTE'S COST INPUTS TO REFLECT SHARING PARAMETERS BASED ON GTE'S ACTUAL OPERATING ENVIRONMENT?

A. Unless these parameters are based on GTE's actual operating environment, then the resulting cost estimates will not reflect the long-run forward-looking costs GTE expects to incur. In other proceedings, it has been my experience that some parties have attempted to justify levels of sharing that substantially exceed actual experience based on the conclusory statement that opportunities for sharing will be greater in the future. Such proposals conveniently overlook the fact that GTE's network is in place today. They assume that GTE (or other utilities) would have the foresight to install poles and conduit systems that were large enough to accommodate these greatly expanded levels of sharing. With respect to buried cable, these parties apparently believe that GTE will dig up its existing cable in order to immediately rebury in a shared trench. Even if one takes the position that it is the costs of some hypothetical new entrant that is going to rebuild the entire network that should be modeled, greatly increased levels of sharing still cannot be supported. Even under this hypothesis, the required coincidence of wants in space and time among the sharing utilities must be assumed as well. However, there is no hypothetical new entrant that will completely rebuild the electric power and cable TV networks in GTE's serving areas. Like GTE, their networks are already in place along with sharing arrangements that made sense at the time.

2237

Q. WHAT SPACING ASSUMPTIONS WERE MADE FOR POLES, MANHOLES AND GUY WIRES AND ANCHORS?

A. GTE selected spacing inputs that are consistent with its actual engineering practices. A pole spacing interval of 175 feet was used, which falls between the BCPM defaults of 250 and 150 feet. For manholes, a longer spacing of 750 feet was used rather than the proposed defaults of 550 and 725 feet. A spacing interval of every tenth pole was used for guy wires and anchors, which is a wider interval than specified by the BCPM defaults.

2238

Q. HOW WAS THE SPECIAL ACCESS LINE FACTOR DEVELOPED?

A. This input is based on GTE Florida's 1997 year-end data. The input equals 12.28 percent.

Q. HOW WERE THE SWITCHING AND TRANSPORT INPUTS LISTED ABOVE DEVELOPED?

A. The percent of local calls and the percent of residence lines were based on actual 1997 data for GTE Florida. These values were 84.63 and 71.40 percent, respectively. As noted above, the switch percent line fill is based on the national average value for GTE. The land and buildings loading factors are based on the ratio of the corresponding 1997 ARMIS account balances to digital switching investment, where these numbers have been adjusted to replacement values using C.A. Turner indices where available. The investments by wire center for each category listed above are based on SCIS and Costmod runs for

representative model offices in GTE's network, and on the switch type and number of lines in each Florida wire center. These investments reflect the pricing GTE obtains for initial switch placements and for capacity additions. The investments include telco engineering and installation costs, as well as common equipment and power. Accordingly, the BCPM inputs for these factors have been set to zero. The usage inputs, line-to-trunk ratio, the percent of local calls that are interoffice, and the call completion fraction were set to values consistent with the SCIS and Costmod runs. The maximum number of nodes on a SONET ring was set to eight.

2239

Q. WHAT INPUT PRICES FOR LABOR AND MATERIAL CHANGED FROM THEIR DEFAULT VALUES?

A. As indicated above, GTE has developed company-specific values for those material and labor inputs that deal primarily with the loop: (1) manholes; (2) conduit systems; (3) poles; (4) guy wires and anchors; (5) NIDs and drops; (6) cross-connect boxes; (7) copper cable; (8) fiber cable; and (9) DLCs. These material and labor inputs are based on the prices that GTE currently pays for these inputs in Florida. In Exhibit DGT-1, the inputs have been presented on a combined material and labor basis, in order to preserve the confidentiality of the data.

Q. WOULD IT BE CORRECT TO BASE GTE'S COST ESTIMATES ON THE LOWEST INPUT PRICES FROM AMONG ALL OF THE

PRICES PROPOSED BY THE PARTIES TO THIS PROCEEDING?

A. No. Only company-specific inputs reflect each company's current contracts with various material, construction and other service vendors. It would be inappropriate to select the lowest inputs from among all those offered, or from among the proxy model default inputs, for the simple reason that the resulting set of prices would likely not be attainable by any one company. The contract prices negotiated by a company are very often a package deal, covering a variety of products and at times specifying minimum volume requirements. It is not possible to mix and match the terms of different contracts to develop a set of pricing inputs that will represent the costs that any company will expect to incur. Consider the analogy of a customer choosing between two different calling plans offered by two different providers of toll service. Suppose that the plan offered by the first toll provider has a relatively low rate per minute, and that it also requires a recurring payment of $5 per month. Suppose also that the plan offered by the second carrier has a relatively higher rate per minute, but has no recurring monthly charge. Is it realistic to believe the customer can obtain the lower per-minute charge from the second provider, or that the first provider will drop the fixed monthly charge? The answer is "No." Similarly, it is not realistic to believe that any local exchange carrier can mix and match input prices from a variety of vendors--whether these input prices result from market-based transactions or are based on the "expert" judgement of an engineering team.

2240

Q. HOW WERE GTE'S EXPENSE INPUTS TO BCPM DEVELOPED?

A. The expense inputs are of three types: capital related expenses, which are expressed as a percent of investment; non-capital related expenses, which are input to BCPM on a per-line basis; and the support ratios for general support assets. GTE witness Michael R. Norris addresses these expense inputs.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

GTE FLORIDA INCORPORATED

REBUTTAL TESTIMONY OF DAVID G. TUCEK

DOCKET NO. 980696-TP

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is David G. Tucek. My business address is 1000 GTE Drive, Wentzville, Missouri.

Q. ARE YOU THE SAME DAVID G. TUCEK WHO PREVIOUSLY FILED DIRECT TESTIMONY IN THIS PROCEEDING?

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A. Yes, I am.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to the direct testimony of MCI witness James Wells concerning the pole costs GTE provided to the FCC in August, 1997. GTE provided this information in response to an FCC data request and, while Mr. Wells has accurately reported the Florida information that GTE filed with the FCC, his use of this information in his direct testimony is completely inappropriate.

Q. WHY IS MR. WELLS' USE OF GTE'S RESPONSE TO THE FCC INAPPROPRIATE?

A. At pages 14 through 18 of his testimony, Mr. Wells attempts to make

use of the responses by GTE and other local exchange companies to support the HAI default input value for the cost of a pole. His testimony is inappropriate because the HAI national default value of $417 purports to represent the installed cost of a pole. On November 13, 1997, Mr. Wells testified in Kentucky Administrative Case No. 360 that this cost would include such items as the costs of guy wires and anchors, inventory costs, and installation and engineering labor. The number reported by GTE to the FCC for the price of a pole does not include any of these costs. Additionally, the labor cost reported to the FCC represents only the cost of installation and does not include any engineering labor. Consequently, Mr. Wells has made a classic "apples to oranges" comparison in his attempt to support HAI's default input for the cost of a pole.

2243

Q. SHOULD MR. WELLS HAVE KNOWN HE WAS MAKING SUCH A COMPARISON?

A. Yes. On February 26, 1998, I filed supplemental rebuttal testimony in the Kentucky proceeding that pointed out the mismatch between the HAI default value and the pole costs provided to the FCC. In that testimony I noted that, in addition to his Kentucky testimony, Mr. Wells had filed similar testimony before the North Carolina Utilities Commission in Docket No. P-100, Sub 133b. I also noted that, in response to Mr. Wells' North Carolina testimony, GTE witness Terry Robinson filed rebuttal testimony stating that the pole costs filed by GTE in response to the FCC data request excluded the costs that I

identified above. Finally, I noted that Mr. Robinson's testimony was filed on January 30, 1998, more than two weeks before Mr. Wells filed his supplemental direct testimony in the Kentucky proceeding. I cannot understand how Mr. Wells can continue to make the same inappropriate comparison between the HAI default pole cost inputs and the FCC data request, given that he has been advised of his error twice in the last five months.

Q. IS THE POLE COST UTILIZED IN GTE'S SUBMISSION OF BCPM VERSION 3.1 DIRECTLY COMPARABLE TO THE HAI DEFAULT VALUE?

A. No, it is not. The HAI default pole price is for a 40-foot pole and includes a loading for anchors and guys in the labor component of the default value. The pole cost used in GTE's submission in Florida is an average of the cost of a 30- and 40-foot pole, and excludes anchors and guys.

Q. IS IT POSSIBLE TO EXPRESS GTE'S POLE COST SO THAT IT IS ON THE SAME BASIS AS THE HAI INPUT?

A. Yes, it is. The comparable installed cost of a 40-foot pole is $854.38, without anchors and guys. With anchors and guys, the cost increases to $997.43 per pole. Based on the assumption that anchors and guys are placed once every 10 poles, the average cost is $868.69 per pole. This is more than 100 percent greater than the HAI national default input of $417 for pole costs. Additionally, for

Florida, the HAI sponsors have adjusted the labor component of the national default downward by 32 percent. Consequently, the resulting HAI pole cost input for Florida is only $381.20 per pole. The correct value for GTE is more than 125 percent greater. Put another way, the HAI input for Florida falls short of GTE's cost by 56 percent.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes, it does.

BY MR. MITCHELL:

Q Mr. Tucek, have you prepared a summary of your testimony?

A Yes, I have.

Q Would you please give that now?

A Good morning. My name is Dave Tucek. As you know, I'm appearing here on behalf of GTE Florida.

In my summary I'm going to briefly address three issues. First, I'm going to discuss the GTE-specific inputs that I sponsor in my testimony for use in BCPM. Second, I am going to talk about comparing GTE's inputs for materials and labor with those inputs offered by other parties. And finally, I will talk about whether this Commission should select one set of inputs for all local exchange carriers in Florida or if the Commission should select inputs that are specific to each company.

The inputs that I and Mr. Norris are sponsoring reflect GTE's network characteristics, operating practices, and most important, the prices for labor and material that GTE is both currently able and expects to obtain in operating its network in Florida.

I'm sometimes asked how many BCPM inputs is GTE populating with company-specific values. In

response, I say that counting the inputs we have populated is really a futile endeavor. What is significant is that we have populated the most important inputs.

These include inputs that affect costs overall, such as the cost of capital, tax rates, depreciation lives, and expenses. These include inputs that affect the most important parts of network, the local loop and the switch. Together the loop and the switch represent about 85% of the total cost of basic local service. Roughly 70% is the loop and 15% is the switch. Included in these inputs are things like structure mix and structure sharing assumptions, as well as the cost of network components such as poles and cable and digital loop carriers. And, of course, the cost of the switch is utilized in GTE's network.

I note that with respect to switching, GTE has entered the cost at the wire center level and that we have also input a value into BCPM for switch line fill of 85.5%. I also note that the value we've put in for the line fill factor did not affect the results that come out of BCPM for GTE. I know this because I reran the model, or the folks in Texas actually reran the model with a 100% line fill, and we saw that there

was no change in the monthly expense.

That's important, because there are witnesses in this proceeding who said that we've somehow double-dipped by inputting a line fill input into the switching models underlining the wire center cost and then inputting the same factor into BCPM.

The second issue that I will address is the question of whether any conclusions can or cannot be reached when you compare GTE's inputs for network components with those submitted by other parties.

In a nutshell, very little can be concluded from looking at the differences among various sets of inputs. Just like trying to count the number of inputs we've populated in BCPM, it's a futile endeavor to search for meaning in the differences between the inputs proffered by the parties in this proceeding. The reason for this is that for any such comparison to be meaningful, the inputs must include the same types of costs.

GTE's inputs for poles, cables, and the other network components start with the base price we pay the vendor and also include freight, sales tax, minor materials, provisioning expense, and engineering and installation labor. Just like the base price for material, the installation labor reflects the prices

that we currently pay our contractors.

I don't know if other parties have included these costs in their corresponding inputs, even when the inputs are called by the same name.

I gave an example of the need for consistency in cost input development when making comparisons in my rebuttal testimony. There I pointed out that Mr. Wells' reliance on GTE's response to the FCC data request on poles was inappropriate, and the reason for that was that all the costs that he agrees should be in the installed cost of a pole were not included in GTE's response to the FCC.

For example, the GTE response to the FCC excluded anchors and guys and excluded provisioning expense, even though the HAI default value ostensibly includes these costs. When you take GTE's current pole costs and put them on the same basis as the HAI default, a very different conclusion than the one reached by Mr. Wells results.

The lesson we can learn from my rebuttal testimony is that it is very important to make sure there's no mismatch in what each company has included in like named inputs before trying to assign meaning to the differences. Any comparison of these data rely on the unproven assumption that the inputs that are

called by the same name are developed on the same basis. We've already seen this to not be the case with something as basic as a pole.

I would also note that one needs to investigate what goes into the development of the input for a network component before making broad generalizations, such as, GTE and the other carriers must have included loadings for huts or environmentally controlled vaults in their small DLC costs. I can assure you that GTE's DLCs do not include huts or environmentally controlled vaults. I can also assure you that only Sprint and BellSouth can testify to what their costs for DLCs or any other network component includes.

Finally, I would like to turn to the issue of company-specific inputs versus one size fits all.

First off, I would suggest that if this Commission wants the cost model and the cost model inputs to result in meaningful estimates of forward-looking cost, it is important that we estimate the forward-looking cost of providing local service on each carrier's own network. The reason for this is that the supported services are likely to be provided primarily out of the incumbent's network for the foreseeable future, if not indefinitely.

In particular, this means that the inputs for the purchase and placement of network components, cable, poles, and switches, must reflect the prices that each company is able to obtain and expects to pay. If a single "one size fits all" set of input prices is chosen, say like picking the lowest proffered input value for each component, the result is likely to be a set of input prices that no company is able to obtain, and the resulting cost estimates will be meaningless.

Likewise, the other inputs, such as those relating to sharing or to fill factors, must reflect the operating characteristics of each company.

On Monday in his presentation, Mr. Wood characterized the scorched note assumption as an exception to the concept of forward-looking cost. I would submit that the assumption is not an exception, but is a recognition of the fact that these cost models and their inputs must be rooted in reality. Unless they're rooted in reality, the resulting estimates will have no meaning.

It is incorrect, for example, to claim that the concept of forward-looking cost or the scorched note assumption means that we are assuming or we must assume that the network is completely being

rebuilt from the ground up and that the opportunities for structure sharing will therefore be greatly enhanced.

Now, I don't deny that both models proffered in this proceeding design a network as if it is being built at once, but it's not because it's a requirement for forward-looking cost. The reason is that there's no other alternative. In the real world, the network is built and evolves through time as demand qualities change. Neither model has the capability of modeling a network dynamically, with demand growing in both time and space.

The best they can do is design the network in one fell swoop, as Ms. Caldwell said, the fall from the sky network, and they design it to serve the entire existing market. This does not mean that we will have opportunity to rebury plant that's in the ground today or to resize existing conduit system or pole lines across the state in order to take advantage of greatly expanded sharing opportunities assumed by the HAI sponsors.

Now, some parties are going to say, "Tucek, you're wrong. We should not try to estimate the forward-looking cost of providing local service out of the existing carriers' networks. The correct standard

of what we ought to be estimating is the cost of an efficient provider."

I don't want to argue about the standard here. I just want to consider the implication that often accompanies that assertion, that the existing carriers are inefficient, because they have yet to face the rigors of competition, so it is incorrect to look to their actual experience in selecting inputs. So let's examine that implication.

At one time, every carrier in this state was subject to traditional rate of return regulation by this Commission.

MR. COKER: Madam Chairman, I think I'm going to assert an objection here. This is well beyond the scope of his redirect or rebuttal testimony.

CHAIRMAN JOHNSON: Response?

MR. MITCHELL: Madam Chairman, it certainly is not. Mr. Tucek explains in his direct testimony his approach to this forward-looking cost concept, and this is just an explanation of how he went about approaching that issue.

CHAIRMAN JOHNSON: Let me direct the witness that you need to -- if this is a summary, you need to be summarizing what was filed and stay within

what was filed as you provide your summary.

THE WITNESS: Okay. May I ask if I'm allowed to talk about the deposition?

CHAIRMAN JOHNSON: Is that a part of your summary?

THE WITNESS: Well, I'm going to refer to it here, yes. I don't want to --

CHAIRMAN JOHNSON: It's not in your prefiled testimony?

THE WITNESS: No.

CHAIRMAN JOHNSON: Then I would suggest that you not provide it as a summary. The summary process is --

THE WITNESS: Let me conclude that it has been offered that there's no evidence or no reason to believe that the existing incumbents are inefficient, and if anybody would care to ask me, I would explain why. And that ends my summary.

CHAIRMAN JOHNSON: Thank you. We didn't mark his exhibits.

MR. MITCHELL: Not yet. Madam Chairman, I would ask that the revised exhibits to Mr. Tucek's testimony identified DGT-1R through DGT-3R be marked as identification.

CHAIRMAN JOHNSON: We'll identify those as

Exhibit 78.

(Exhibit 78 marked for identification.)

MR. MITCHELL: Thank you. Mr. Tucek is available for cross examination.

CHAIRMAN JOHNSON: We're going to recess for lunch, a 30-minute lunch. We'll reconvene at 12:30.

(Proceedings recessed at 11:55 a.m.)

(Transcript continues in sequence in Volume 20.)

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