BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the	**)**	
	)	**DOCKET NO. UT-003013**
Continued Costing and Pricing of	**)**	**Part D**
Unbundled Network Elements,	**)**	
Transport, and Termination	**)**	

DIRECT TESTIMONY OF

TIMOTHY J. GATES

ON BEHALF OF

WORLDCOM, INC.

Dated: December 21, 2001

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I. WITNESS IDENTIFICATION AND CREDENTIALS

Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.

A. My name is Timothy J. Gates. I am a Senior Vice President at QSI Consulting, Inc., a consulting firm specializing in economics and telecommunications issues. My business address is 15712 West 72nd Circle, Arvada, Colorado 80007.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND WORK EXPERIENCE.

A. I received a Bachelor of Science degree from Oregon State University and a Master of Management degree in Finance and Quantitative Methods from Willamette University's Atkinson Graduate School of Management. I have also attended numerous courses and seminars specific to the telecommunications industry, including the NARUC Annual and Advanced Regulatory Studies Program.

Prior to joining QSI I was a Senior Executive Staff Member at MCI WorldCom, Inc. (“MWCOM”). I was employed by MWCOM for 15 years in various public policy positions. While at MWCOM I managed various functions, including tariffing, economic and financial analysis, competitive analysis, witness training and MWCOM’s use of external consultants. I testified on behalf of MWCOM more than 150 times in 32 states and before the FCC on various public policy issues ranging from costing, pricing, local entry and universal service to strategic planning, merger and network issues. Prior to joining MWCOM, I was employed as a Telephone Rate Analyst in the Engineering Division at the Texas Public Utility Commission and earlier as an Economic Analyst at the Oregon Public Utility Commission. I also worked at the Bonneville Power Administration as a Financial Analyst doing total electric use forecasts while I attended graduate school. Prior to doing my graduate work, I worked for ten years as a forester in the Pacific Northwest for multinational and government organizations. Exhibit TJG-2 to this testimony is a summary of my work experience and education.

Q. HAVE YOU EVER TESTIFIED BEFORE THE WASHINGTON COMMISSION?

A. Yes. I testified or provided comments in Docket Nos. U-88-2052-P, UT-96-0338, and UT-97-0325 on behalf of MCI.

II. ISSUE INTRODUCTION AND PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of this testimony is address the “branding” issue in this proceeding. Branding is an integral part of Qwest’s directory assistance (“DA”) and operator service (“OS”) offerings.

Q. PLEASE DESCRIBE "BRANDING" AS IT APPLIES TO TELECOMMUNICATIONS SERVICES.

A. In its simplest form, branding is the identification of service with a particular provider. In telecommunications, branding is associated primarily with OS and DA services. For instance, if I dial "555-1212" or "411" from my home phone, the first thing I hear is "Qwest Directory Assistance." When I dial "0", the first thing I hear is "Welcome to Qwest." When I dial "00", the first thing I hear is "MCI WorldCom." Branding can be accomplished by recordings or by live individuals.

Q. PLEASE DEFINE OS AND DA.

A. The FCC has defined operator services as "any automatic or live assistance to a consumer to arrange for billing or completion, or both, of a telephone call."[1] The FCC defined directory assistance as a service that allows "subscribers to retrieve telephone numbers of other subscribers."[2] Mr. Lehmkuhl of WorldCom addresses directory assistance and operator services in his testimony. Although branding is a part of both OS and DA services, I will specifically address branding in this testimony.

[1] *Local Competition Second Report and Order*, 11 FCC Rcd at, 19448, para. 110 (citing 47 U.S.C. § 226(a)(7)).
[2] Before the Federal Communications Commission; *Performance Measurements Notice,* 13 FCC Rcd at 12823, n. 14.

Q. WHY IS BRANDING IMPORTANT TO CONSUMERS?

A. Branding provides important information to consumers. It allows a consumer to know which company is providing the service and is one way for a consumer to determine whether their choice of a provider is still in effect. For instance, if a consumer has selected AT&T for long distance, but when he or she dials "00" and hears "Welcome to Sprint", it may be that their carrier selection was changed without their knowledge. As such, branding provides a way for consumers to determine whether "slamming" or some administrative error has occurred. Further, if there are problems with service or rates, or if the consumer wants to talk to the provider, branding provides the consumer with information on which company to contact.

Q. WHY IS BRANDING IMPORTANT TO SERVICE PROVIDERS?

A. Branding allows providers to remind their customers of their ongoing business relationship. It is a source of advertising, if you will.

Q. MUST INCUMBENT LECS ("ILECS") PROVIDE BRANDING OR RE-BRANDING UPON REQUEST?

A. Yes. The FCC has found on several occasions that to the extent technically feasible, an ILEC must identify and re-brand the traffic it provides to its competitors.[3]

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[3]Before the Federal Communications Commission; In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996: CC Docket No. 96-98; FCC 99-239; THIRD REPORT AND ORDER AND FOURTH FURTHER NOTICE OF PROPOSED

Q. WHY IS BRANDING AN ISSUE IN THIS PROCEEDING?

A. Branding is required when a carrier utilizes the OS or DA services of the incumbent. In other words, if WorldCom resells the OS or DA services of Qwest, then Qwest would brand the services on behalf of WorldCom.

Q. DO CARRIERS ALWAYS UTILIZE THE OS/DA SERVICES OF THE ILEC?

A. No. When properly provisioned customized routing is available from the incumbent, competitive providers may utilize the traffic routing capability to get OS/DA traffic to their own OS/DA platforms, so they can provide these services themselves.

Q. PLEASE BRIEFLY EXPLAIN CUSTOMIZED ROUTING.

A. The FCC's UNE Remand Order describes customized routing as follows:

> Customized routing permits requesting carriers to designate the particular outgoing trunks associated with unbundled switching provided by the incumbent, which will carry certain classes of traffic originating from the requesting provider's customers. This feature would allow the requesting carrier to specify that OS/DA traffic from its customers be routed over designated trunks which terminate at the requesting carrier's OS/DA platform or a third party's OS/DA platform.[4]

If the incumbent does not provide customized routing that allows competitive LECs ("CLECs") to provide their own OS/DA services, then the incumbent provider must provide nondiscriminatory access to its OS/DA, pursuant to

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RULEMAKING; Released: November 5, 1999; at ¶ 443. Hereinafter referred to as the "*UNE Remand Order*."

Section 251(b) of the Telecommunications Act of 1996. Indeed, even if the incumbent does not provide customized routing, its obligation to provide nondiscriminatory access to its OS/DA remains.[5]

Q. ARE YOU TESTIFYING ON THE "CUSTOMIZED ROUTING" PROPOSALS OF QWEST IN THIS PROCEEDING?

A. No. Mr. Caputo of WorldCom is responding to Qwest's proposals on customized routing in this proceeding. Specifically, Mr. Caputo notes that Qwest's proposal to use dedicated trunks for customized routing is flawed. Dedicated trunks are not required to provide customized routing. My testimony is limited to the branding aspects of OS/DA as proposed by Qwest.

III. QWEST'S BRANDING PROPOSAL

Q. PLEASE DESCRIBE QWEST'S POSITION ON BRANDING IN THIS PROCEEDING.

A. Through the testimony of Ms. Million, Qwest states that the FCC's *UNE Remand Order* exempts OS and DA from TELRIC pricing as an unbundled element or UNE so long as Qwest provides CLECs with access to customized

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[4] *UNE Remand Order* n. 867.

[5] Id. at ¶442. See, also, *Implementation of the Telecommunications Act of 1996; Telecommunications Carrier's Use of Customer Proprietary Network Information and Other Customer Information, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Provision of Directory Listing Information under the Telecommunications Act of 1934, As Amended,* CC Docket Nos. 96-115, 96-98, 99-273, Third Report and order, Second Order on Reconsideration, and notice of Proposed Rulemaking, FCC 99-227, paras. 141-148 (rel. September 9, 1999).

routing.[6] Extrapolating this argument, Qwest then suggests that branding can be priced on an individual case basis ("ICB") at "market" rates without adherence to the TELRIC principles associated with UNEs and other interconnection services.

Q. WHAT RATES ARE BEING PROPOSED BY QWEST FOR BRANDING IN THIS PROCEEDING?

A. Qwest is proposing a nonrecurring charge ("NRC") of $10,500 for "Call Branding, Set-Up & Recording" and a NRC of $175 for "Loading Brand/Per Switch." These rates are proposed for both Directory Assistance, Facility Based Providers (Section 10.5 of SGAT) and for Toll and Assistance Operator Services, Facility Based Providers (Section 10.7 of SGAT). The specific rates are found in Sections 10.5.3, 10.5.4, 10.7.3, and 10.7.4. (See, Qwest Washington SGAT First Revision, Exhibit A; p 15)

IV. SUMMARY OF FINDINGS AND RECOMMENDATIONS

Q. PLEASE SUMMARIZE YOUR CONCLUSIONS AND STATE YOUR RECOMMENDATIONS.

A. The primary conclusions and recommendations of this testimony are as follows:

[6] See, Direct of Million at 33 and 34.

- Qwest's customized routing offering is flawed. Specifically, the rates are excessive and Qwest has failed to offer the capability on a shared access basis, using Feature Group D trunks.

- Qwest's proposed NRCs for OS/DA branding are excessive and without cost support. Qwest should be required to price branding on a TELRIC basis and not on an ICB, market-rate basis.

V. GENERAL COSTING AND PRICING PRINCIPLES

Q. PLEASE DISCUSS THE GENERAL COSTING PRINCIPLES BY WHICH QWEST'S COST STUDIES AND RATES SHOULD BE EVALUATED.

A. In general, Qwest's cost studies should be reviewed in light of the FCC's TELRIC principles as defined in the FCC's Local Competition Order[7] and this Commission's own previous cost orders. In general, the TELRIC principles can be summarized as follows:

Principle # 1: *The firm should be assumed to operate in the long run. (¶ 677 & 692)*

Principle # 2: *The relevant increment of output should be total company demand for the unbundled network element in question. (¶ 690)*

Principle # 3: *Technology choices should reflect least-cost, most efficient technologies. (¶ 685)*

Principle # 4: *Costs should be forward-looking. (¶ 679, 682, 692)*

Principle # 5: *Cost identification should follow cost causation*. (¶ 691)

[7] In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; **FIRST REPORT AND ORDER**; CC Docket Nos. 96-98 and 95-185; Released August 8, 1996; hereinafter referred to as the "*Local Competition Order*."

In addition to these TELRIC principles, the FCC also noted that ILECs must prove to the state commissions the nature and magnitude of any forward-looking cost they seek to recover in the prices of interconnection and unbundled network elements.[8] While this most important of rules is unfortunately overlooked by some state commissions, the Washington Commission should put specific emphasis on this rule (and Qwest's obligation) so as to combat assumptions and inputs that may have a large influence on Qwest's ultimate costs and rates, yet are not supported with any corroborating evidence (specific examples will be provided later in this testimony). Finally, cost models should be transparent, open and verifiable by Commissions and intervenors.[9]

Q. WHAT BENEFITS ARE ASSOCIATED WITH TELRIC PRICING?

A. Consistent with sound economics, good public policy, FCC Orders and orders from this Commission, *prices for interconnection and UNEs should be set at forward-looking economic cost*. As generally accepted by economists – and as articulated by the FCC in various orders – prices (recurring and nonrecurring) that are set at cost send the right signals to

[8] Id. at ¶ 680.

[9] This Commission stated specifically that cost models should be open and transparent to aid competitors and other parties in their review of cost support. (Fifteenth Supplemental Order, Docket No. UT-950200 (April 11, 1996), at 86. Further, the FCC recently directed that in upcoming cases to be arbitrated by the FCC, computerized cost models "must be submitted in a form that allows the Arbitrator and the parties to alter inputs and determine the effect on cost estimates." Procedures Established for Arbitration of Interconnection Agreements Between Verizon, AT&T, Cox, and WorldCom, DA 01-270 (February 1, 2001), Paras. A.2.1.i; A.3.1.c.

all market participants and, as a result, promote efficient competition. As the FCC noted in its *Local Competition Order* at paragraph 679,

> Because a pricing methodology based on forward-looking costs simulates the conditions in a competitive marketplace, it allows the requesting carrier to produce efficiently and to compete effectively, which should drive retail prices to their competitive levels.

By contrast, when prices deviate from cost, a number of market distortions are introduced, which invariably harm the general economic welfare. For example, if the price for a UNE or service is set above forward-looking economic costs – as proposed here by Qwest for branding – then competition is diminished in a number of ways.

Q. HOW DOES ECONOMIC PRICING OF INTERCONNECTION, UNES AND OTHER SERVICES IMPACT THE MARKET AND CLECS IN PARTICULAR?

A. Service prices should accurately track the manner in which an efficient ILEC -- using equipment, facilities, and capabilities that are currently available -- would incur its costs on a long-run forward-looking basis. This is consistent with the TELRIC principles required by the FCC and this Commission. As such, the Commission should not allow Qwest to price on a market basis for services with market power. Neither should the Commission allow Qwest to assume inefficient equipment or procedures that artificially increase costs for CLECs. Prices based on long run, forward-looking costs are consistent with prices one observes in competitive markets -- prices which regulation should seek to mimic to the maximum extent possible.

Q. DO THE TELRIC PRINCIPLES APPLY TO NONRECURRING AS WELL AS RECURRING PRICES?

A. Yes. Non-recurring costs ("NRCs") should be based on forward-looking economic cost assumptions as well.

Q. HOW DO OVERSTATED PRICES – RECURRING OR NONRECURRING -- IMPACT THE MARKET, CONSUMERS AND CLECS IN PARTICULAR?

A. Overstated prices create market distortions that harm the public interest and the development of competition. For instance, overstated NRCs create significant barriers to local competition by making it more expensive for end users to choose a CLEC to provide their telecommunications services. The potential for NRCs to act as a barrier to entry makes it critical that the Commission and the parties have the opportunity to carefully scrutinize any claimed cost justifications for such charges.

Q. HOW DO NRCS ACT AS A BARRIER TO ENTRY?

A. A barrier to entry is a factor that prevents or impedes a potential entrant from actually entering a market. Barriers to entry arise whenever a new entrant faces costs that the incumbent does not face. These added costs mean that a would-be entrant must expect higher prices than it would otherwise need before it would otherwise need before it will be willing to enter the market.

Because NRCs are assessed up-front, by their very nature, they tend to act as barriers to entry. The higher the up-front charge, the higher the barrier to entry. Thus Qwest has a powerful incentive to argue for the highest possible NRCs

VI. NO SUPPORT FOR BRANDING RATES

Q. HAS QWEST PROVIDED ANY SUPPORT FOR ITS BRANDING NRCS?

A. No. Qwest argues that it has the right to price these NRCs at market rates.[10] As such, Qwest has failed to provide any cost support for these rates.

Q. IF WE ASSUME, FOR ARGUMENT SAKE, THAT TELRIC STUDIES ARE NOT REQUIRED FOR BRANDING, WOULD YOU STILL RECOMMEND THAT THE COMMISSION ESTABLISH TELRIC RATES FOR THIS SERVICE?

A. Yes. The TELRIC principles discussed above were designed to encourage competition and to benefit the public interest. The Commission should require that the branding NRCs be based upon TELRIC principles. The fact that branding is not a UNE does not mean that this Commission cannot require TELRIC cost support for the proposed rates. As this Commission found in the May 11, 1998 order, "The FCC's interconnection Order provides guidance on many costing and pricing issues, but its recommendations are largely non-binding."[11] In a proceeding in 1996, the Commission noted, "For consumers to have competitive choice, the U S WEST network must be opened up at terms that are fair to both U S WEST and new entrants. A key part of that process is determining the costs and prices for U S WEST's services."[12] Proposed rates at these levels with no cost support do not comport with this Commission's prior decisions on rate development. The branding rates need to be just, reasonable and nondiscriminatory and applying the TELRIC principles will ensure that those standards are met.

Q. QWEST PROPOSES A $10,500 NRC FOR "CALL BRANDING, SET-UP AND RECORDING." IS THIS A REASONABLE PRICE?

A. It is impossible to determine whether this price is reasonable because Qwest has failed to provide any cost support. Nevertheless, given the nature of the work required for this service, the price seems grossly overstated. For instance, developing a call brand requires only a few steps – find a voice, write a script, record the message on a high quality

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[10] Direct of Million at 33-34.
[11] Before the Washington Utilities and Transportation Commission; Eighth Supplemental Order Interim Order Establishing Costs for Determining Prices in Phase II; and Notice of Prehearing Conference; Docket Nos. UT-960369, UT-960370, UT-960371; at 8.
[12] Before the Washington Utilities and Transportation Commission; Fifteenth Supplemental Order, Docket No. UT-950200, at 9 (Dated April 11, 1996).

digital recording device. Even if Qwest developed a dozen tapes for the CLEC to choose from, I can't understand how this cost would be incurred in the process. As I described earlier in this testimony, the messages are only a few words and are not complicated. I cannot conceive of a process that would result in a cost of $10,500.

Q. IS QWEST PROPOSING THE SAME $10,500 NRC FOR BOTH DA AND OS?

A. Yes. This is especially troubling since the recording would be the same or only differ by perhaps a word. It would be wrong to assess this large NRC twice, when the same recording/tape could be used for both services.

Q. IS THE "LOADING BRAND/PER SWITCH" NRC OF $175 SIMILARLY OVERSTATED AND UNSUPPORTED?

A. Yes. Again, Qwest provides no cost support for this rate element. The process of loading this message into the switch is very simple and could not possible require a cost of $175.

Q. WHAT IS YOUR RECOMMENDATION TO THE COMMISSION REGARDING THE NRCS DISCUSSED ABOVE?

A. I recommend that the Commission require Qwest to provide TELRIC cost studies to support the proposed NRC rates for both "Call Branding, Set-up & Recording" and "Loading Brand/Per Switch" for DA and OS.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.