

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

**IN THE MATTER OF CONTINUED)
COSTING AND PRICING OF)
UNBUNDLED NETWORK ELEMENTS,)
TRANSPORT, TERMINATION, AND)
RESALE)**

**DOCKET NO. UT-003013
*Part D***

REBUTTAL TESTIMONY

OF

D. M. (MARTI) GUDE

ON BEHALF OF

QWEST CORPORATION

MARCH 7, 2002

TESTIMONY INDEX

	<u>Page</u>
EXECUTIVE SUMMARY	i
I. IDENTIFICATION OF WITNESS	1
II. PURPOSE OF TESTIMONY	2
III. ISSUES RELATING TO THE DIRECT TESTIMONY OF PETER J. GOSE	3
• Consistency of Cost Factor Development and Application	3
• Directly Attributed and Common Cost Components and Algorithms	5
• Merger-Related Cost Factor Issues	14
IV. FINAL CONCLUSIONS AND RECOMMENDATIONS	21

EXECUTIVE SUMMARY

D. M. (Marti) Gude is employed by Qwest Corporation. In her position as Director - Cost Accounting, she is responsible for various regulatory and management accounting functions. Her responsibilities include the development of TELRIC-based cost study factors, and preparing and analyzing embedded cost studies and information relating to cost studies that Qwest uses for purposes such as deregulation, cost accounting, and regulatory filings.

Her rebuttal testimony responds to the testimony of Mr. Peter J. Gose, on behalf of WorldCom, Inc., regarding the various issues he raises concerning TELRIC-based non-recurring cost studies that Qwest presented in its direct case. Ms. Gude's testimony clarifies the issues raised by Mr. Gose and sets forth rationale indicating why his testimony should be disregarded or considered moot.

She addresses Mr. Gose's:

- opposition to relying on previous Washington Utilities and Transportation Commission rulings relating to directly attributed and common cost factors and the reasonableness of allocating directly attributable and common costs in the preparation of non-recurring studies under review in this proceeding;
- factor development issues that deal with the inclusion of costs relating to product management and sales activities in TELRIC pricing and non-recurring studies and his misconceptions regarding the algorithms employed by Qwest in calculating non-recurring charges; and
- issues regarding post-merger Qwest operations and the base data employed in developing the cost factors used in this phase, and earlier phases, of this cost proceeding.

1 **I. IDENTIFICATION OF WITNESS**

2
3 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

4 **A.** My name is D. M. (Marti) Gude. My business address is 1314 Douglas-on-the-Mall,
5 Omaha, Nebraska.

6
7 **Q. PLEASE IDENTIFY YOUR EMPLOYER AND EXPLAIN YOUR POSITION AND**
8 **RESPONSIBILITIES.**

9 **A.** I am employed by Qwest Corporation, formerly known as U S WEST Communications,
10 Inc. ("U S WEST"). My title is Director - Cost Accounting and I am responsible for
11 various regulatory and management accounting functions, including the development of
12 TELRIC-based cost study factors and preparing and analyzing embedded cost studies for
13 use in connection with deregulation, cost accounting and regulatory filings.

14
15 **Q. WHAT IS YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL**
16 **EXPERIENCE?**

17 **A.** I received a Bachelor of Science degree in Business Administration, with a major in
18 Accounting, from the University of Nebraska – Lincoln, and a Master of Business
19 Administration degree, with honors, from the University of Nebraska at Omaha. I am also
20 a Certified Public Accountant, certified in the State of Nebraska as an inactive registrant.

21
22 I was a member of the audit staff of Arthur Andersen & Company for four years prior to
23 joining Qwest's predecessors (U S WEST and Northwestern Bell) in 1979. My experience

1 at Arthur Andersen included audits for companies in various industries, which included the
2 issuance of opinions on financial statements. At Qwest and its predecessors, U S WEST
3 and Northwestern Bell, I have held various positions in the Budget, Finance, Corporate
4 Accounting, and Cost Accounting departments. I have worked in the area of cost
5 accounting since January 1986.
6

7 **Q. HAVE YOU FILED TESTIMONY BEFORE THE WASHINGTON UTILITIES**
8 **AND TRANSPORTATION COMMISSION AND/OR TESTIFIED PREVIOUSLY**
9 **ON THE SUBJECT OF COST DISTRIBUTION, COST FACTOR**
10 **DEVELOPMENT AND/OR COST ACCOUNTING?**

11 **A.** Yes. Exhibit DMG-2 of my testimony provide a chronological listing of the dockets/cases,
12 by state, in which I have previously testified.
13

14 **II. PURPOSE OF TESTIMONY**
15

16 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

17 **A.** I am responding to the testimony of Mr. Peter J. Gose, provided on behalf of WorldCom,
18 Inc., and to various issues he raises concerning the cost study factors contained in Qwest's
19 TELRIC-based non-recurring cost studies presented in Part D of this cost proceeding. My
20 testimony is intended to show why the issues raised in Mr. Gose's testimony should be
21 disregarded or considered moot. I will first address Mr. Gose's opposition to relying on
22 previous Washington Utilities and Transportation Commission (WUTC or the
23 Commission) rulings relating to directly attributable and common cost factors and the

1 reasonableness of allocating these directly attributable and common costs in the
2 preparation of non-recurring studies under review in this proceeding.

3
4 Next, I will address factor development issues raised by Mr. Gose that deal with the
5 inclusion of costs relating to product management and sales activities in TELRIC pricing
6 and non-recurring studies. I will conclude by addressing Mr. Gose's misconceptions
7 regarding the algorithms employed by Qwest in calculating non-recurring charges, along
8 with his issues regarding post-merger Qwest operations and the base data employed in
9 developing the cost factors used in this phase, and earlier phases, of this cost proceeding. I
10 had also planned to address any specific issues raised by Mr. Gose in the Supplemental
11 Testimony he indicated in his Direct Testimony that he would be filing. However, Mr.
12 Gose did not file any supplemental testimony for review.

13 14 **III. ISSUES RELATING TO THE DIRECT TESTIMONY OF PETER J. GOSE**

15 16 **Consistency of Cost Factor Development And Application**

17 **Q. WHAT PRIMARY CONCERN DO YOU HAVE REGARDING THE TESTIMONY** 18 **OF MR. GOSE?**

19 **A.** First and foremost, I disagree with Mr. Gose's suggestion that the Commission should
20 consider changing the cost factor values and/or calculation methodologies employed in
21 Qwest's cost studies filed in this phase of the cost docket. Changing cost factors from
22 those that were developed, reviewed, and applied in determining costs in the earlier phases
23 of this proceeding would create an unacceptable lack of continuity between Qwest's non-

1 recurring cost studies and those studies already addressed by the Commission.

2 Furthermore, Mr. Gose would have the Commission ignore the fact that attributed and
3 common cost factors are developed on the premise that they are applicable to all
4 investment-related and directly assigned costs. Changing the cost study calculation
5 methodology for Qwest's non-recurring studies in Part D of these proceedings, to exclude
6 the application of attributed and common costs to non-recurring costs, would result in
7 unwarranted inconsistencies with other studies and the development of other costs.

8 Making changes in this phase would give rise to an under recovery of costs, unless all
9 other studies are again revisited, and other costs adjusted, for cost elements Mr. Gose
10 would now exclude in calculating costs in this phase. This misguided approach must be
11 rejected.

12
13 Furthermore, the cost elements and the appropriateness of applying directly attributed and
14 common cost factors in Qwest's TELRIC studies were ruled on several times by the
15 Commission in earlier phases of this proceeding. In its previous orders, the WUTC set the
16 attributed and common factor values that were to be used by Qwest in its subsequent
17 filings.¹ Qwest has adhered to these Commission orders and Mr. Gose's attempt to revisit
18 cost factor issues in this proceeding is misplaced.

19

¹ See *In the Matter of the Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket Nos. UT-960369, et al., *EIGHTH SUPPLEMENTAL ORDER*, dated May 11, 1998, at page 5.

1 **Directly Attributed and Common Cost Components and Algorithms**

2 **Q. AT PAGE 3, LINE 14 OF HIS DIRECT TESTIMONY MR. GOSE EXPRESSES**
3 **CONCERN OVER CERTAIN COST COMPONENTS CONTAINED IN QWEST’S**
4 **COST FACTORS, AS WELL AS THE ALGORITHMS THAT WERE USED BY**
5 **QWEST IN DEVELOPING ITS NON-RECURRING RATES. ARE HIS STATED**
6 **CONCERNS VALID?**

7 **A.** No, they are not and I will explain why. But let me first reiterate again, that the
8 Commission has already previously ruled in this docket on the proper factors to use for
9 cost study purposes. The issues Mr. Gose raises now are merely a repeat of arguments
10 previously aired and dismissed by the Commission.

11
12 Mr. Gose first questions the cost elements included in directly assigned costs. His primary
13 issue is a repeat of arguments made by WorldCom in Part B of these proceedings, where
14 World Com contended that: “It seems strange that Qwest would have to provide for much,
15 if any, product management or sales expense for non-recurring charges.” Contrary to Mr.
16 Gose’s position, product management and sales costs for wholesale can be separately
17 identified, and thus directly assigned in cost study development. Therefore, it is proper to
18 recognize such costs in the development of TELRIC cost study factors. Furthermore,
19 including such costs in non-recurring cost factor development is consistent with prior
20 WUTC rulings regarding the development and application of cost factors in other cost

1 studies considered in previous phases of this proceeding.² Furthermore, I would point
2 out Mr. Gose erred in indicating that Qwest included advertising costs in preparing its
3 wholesale cost factors used in its TELRIC studies; Qwest has not done so. See, for
4 example, Qwest's non-recurring study filed as part of Exhibit No. TKM -27,
5 Supplemental, which shows a \$0 amount for advertising.³ Mr. Gose's position on
6 what costs to include in a non-recurring study, just like his implication that Qwest has
7 developed cost factors that include advertising costs, is without merit.

8
9 **Q. IS THE AMOUNT OF PRODUCT MANAGEMENT AND SALES COSTS**
10 **INCLUDED IN QWEST'S NON-RECURRING COST STUDIES LARGE?**

11 **A.** No. The actual amount of product management and sales costs included in each non-
12 recurring cost study is actually quite small. In real dollars it is only approximately \$.06 per
13 dollar of cost.

14
15 **Q. BRIEFLY EXPLAIN FOR THE RECORD WHY PRODUCT MANAGEMENT**
16 **COSTS ARE TREATED AS DIRECTLY ASSIGNED COSTS AND WHY THEY**
17 **ARE APPROPRIATELY INCLUDED IN QWEST'S NON-RECURRING STUDIES.**

² See *In the Matter of the Pricing Proceeding for Interconnection, Unbundled Element, Transport and Termination, and Resale*, Docket No. UT - 960369, et al. *TWENTY-FIFTH SUPPLEMENTAL ORDER*, dated May 19, 2000, page 22, ¶126, and *In the Matter of the Continued Costing and Pricing Proceeding for Interconnection, Unbundled Element, Transport and Termination*, Docket No. UT-003013, Part A, *THIRTEENTH SUPPLEMENTAL ORDER*; dated January 31, 2001 at page 6, ¶7 and pages 85-86, ¶¶260-261.

³ See Docket No. UT-003013, Part D, Qwest Exhibit TKM-27, Supplemental filed November 9, 2001, EXPENSE FACTOR MODULE - TELRIC 99V2.doc, dated December 1999, at page 25. The exclusion of advertising costs in Qwest's TELRIC cost studies is also illustrated in Qwest's Remote Terminal Study #5932 WA Docket WCP-Non-Recurring.xls Details Output, Line 11, Columns C and D (Exhibit TKM-35A).

1 **A.** Product management costs are discussed in Qwest’s Expense Factors Module – TELRIC
2 User Manual filed in support of its cost studies and, the wholesale nature of this type of
3 cost has already been discussed in earlier phases of this cost proceeding. Therefore, I
4 won’t revisit that entire discussion. Rather, I would just reiterate that a variety of Account
5 6611 - Product Management type functions are “wholesale” in nature and would be
6 required even if Qwest had no retail operations. For years, Qwest has employed product
7 managers to serve the wholesale access service needs of interexchange carriers. Today,
8 Qwest’s Wholesale - Carrier market unit is dedicated to serving the needs of interexchange
9 carriers and CLECs in order to provide these customers with wholesale switched and
10 dedicated access, as well as unbundled and resale products. CLECs are typically
11 sophisticated users of complex and evolving telecommunications products and services.
12 As a result, Qwest’s product teams are required to expend substantial resources in meeting
13 the various needs of CLECs. Recurring and non-recurring activities go hand-in-hand and
14 thus, it is appropriate to recover these costs from the pricing of recurring and non-recurring
15 cost elements. Actual “Marketing - Product Management” costs are recorded under the
16 FCC’s Part 32 accounting rules and Qwest’s cost factor development relating to Account
17 6612 Marketing – Product Management expense is based upon these recorded costs and its
18 actual experience for performing wholesale product management functions. Thus, as the
19 WUTC has already determined, it is appropriate to employ those costs in determining cost
20 factors employed in Qwest’s TELRIC recurring and non-recurring studies.

1 **Q. BRIEFLY EXPLAIN FOR THE RECORD WHY SALES COSTS ARE TREATED**
2 **AS DIRECTLY ASSIGNED COSTS AND WHY THEY ARE APPROPRIATELY**
3 **INCLUDED IN QWEST’S NON-RECURRING STUDIES.**

4 **A.** As was the case with product management costs, sales costs and their inclusion in cost
5 study development are documented in Qwest’s Expense Factors User Manual. Their
6 inclusion in cost study development is also supported by the fact that the Commission has
7 previously addressed and approved their inclusion in earlier proceedings. However to
8 briefly reiterate, I will note that in the wholesale environment, Qwest end-user costs are
9 replaced by costs relating to Qwest’s daily interactions with CLECs in providing wholesale
10 unbundled services. In servicing CLECs, Qwest must perform many of the same sales
11 functions it performs for its more sophisticated retail end-users. For example, Qwest sales
12 teams must negotiate contracts with the CLECs and respond to their service-related
13 inquiries and requests. As it was with product management costs, recurring and non-
14 recurring activities go hand-in-hand and thus, it is appropriate to recover these costs from
15 the pricing of recurring and non-recurring cost elements. Accordingly, TELRIC studies
16 should properly identify a sales cost factor that relates to unbundled and other wholesale
17 services for both recurring and non-recurring activities. Qwest’s cost factor development
18 relating to Account 6612 Marketing – Sales expense is based upon recorded costs and its
19 actual experience for performing wholesale sales functions.

20
21 **Q. YOU INDICATED THAT THE COMMISSION HAS PREVIOUSLY ADDRESSED**
22 **AND RESOLVED THE TREATMENT OF PRODUCT MANAGEMENT AND**
23 **SALES COSTS IN THE DEVELOPMENT OF QWEST’S TELRIC COST**

1 **STUDIES. HOW DID THE COMMISSION INDICATE THAT THESE COSTS**
2 **WERE TO BE HANDLED?**

3 **A.** The appropriate inclusion of product management and sales costs in Qwest’s TELRIC
4 studies was originally addressed by the WUTC in Docket Nos. UT-960369, et al. In that
5 decision, the Commission determined that such costs were appropriately included as direct
6 costs of service. In that decision, the WUTC stated:

7 Therefore, we approve the use of the administrative, product
8 management, and business fee expense loaders in U S WEST’s
9 TELRIC studies.⁴

10 Qwest has complied with the Commission’s previous TELRIC study rulings regarding the
11 proper *inclusion* of product management and sales costs as a directly assigned cost of
12 service. Moreover, Qwest has appropriately considered such costs in developing its
13 directly attributed and common factors, and has consistently applied such factors
14 throughout all phases of these cost proceedings.

15
16 **Q.** **AT PAGE 5, LINE 1 OF HIS TESTIMONY, MR. GOSE ASSERTS THAT**
17 **QWEST’S COST STUDY ALGORITHMS CONTAIN A MATHEMATICAL**
18 **COMPOUNDING ERROR. IS HIS ANALYSIS AND ASSERTION CORRECT?**

19 **A.** No, it is not. Mr. Gose hypothesizes that, since the simple summation of Qwest’s directly
20 assigned, directly attributed and common cost factors produces a result that is less than the
21 applied value, that a “compounding” error has occurred. However, his simplistic analysis
22 is flawed. Mr. Gose apparently failed to review or understand Qwest’s cost factor

4 See *In the Matter of the Pricing Proceeding for Interconnection, Unbundled Element, Transport and Termination, and Resale*, Docket No. UT-960369, et al. *TWENTY-FIFTH SUPPLEMENTAL ORDER*, dated May 19, 2000, page 22, ¶126.

1 development documentation. Sequential application of cost factors does not lead to
2 erroneous mathematical compounding when factors are appropriately derived. Qwest's
3 Expense Factor User Manual, filed on November 9, 2001 in support of its cost studies,
4 explains the three major factor groups: Directly Assigned, Directly Attributed, and
5 Common.⁵ It describes that each of these major factors are "cumulative" in how they are
6 applied, and that the denominator of one factor is dependent on the denominator and
7 numerator of the previous factor, thereby lowering its effect. Thus, the costs resulting
8 from the sequential application of Qwest's factors do not erroneously compound, e.g.
9 inflate, the final cost result, as Mr. Gose would infer, and accordingly, Mr. Gose's
10 algorithm issue regarding the "compounding" of costs is without merit in this proceeding.

11
12 **Q. DID QWEST ACTUALLY USE THE DIRECTLY ATTRIBUTED AND COMMON**
13 **COST FACTORS THAT WERE DESCRIBED BY MR. GOSE AT PAGE 3 OF HIS**
14 **TESTIMONY IN PREPARATION OF NON-RECURRING STUDIES FILED IN**
15 **THIS PROCEEDING?**

16 **A.** No. The cost study factors employed by Qwest in the cost studies filed in this proceeding
17 reflect the Commission's previously ordered treatment of directly attributed and common
18 costs. Although cost factors developed from actual operating cost data were filed as part of
19 the Company's non-recurring cost study documentation in this docket, Qwest substituted

⁵ See Docket No. UT-003013, Part D, Qwest Exhibit TKM-27, Supplemental filed November 9, 2001, EXPENSE FACTOR MODULE – TELRIC 99V2.doc, dated December 1999 (e.g. pages 2, 16, and 24).

1 the percentage factors previously prescribed by the WUTC for recognition of directly
2 attributed and common costs.

3
4 **Q. WHY DID QWEST MAKE THIS COST FACTOR SUBSTITUTION?**

5 **A.** In prior cost proceedings, and in the early phases of this cost proceeding, the WUTC
6 ordered, and subsequently reaffirmed, the percentages of directly attributed and common
7 costs that should be included by Qwest in all TELRIC cost studies filed in the State of
8 Washington, including non-recurring studies. In its *Eighth Supplemental Order* in Docket
9 Nos. UT-960369, et al. the Commission ordered the following:

10
11 The Commission adopts U S WEST's non-recurring cost study,
12 a 19.65 percent additive for attributed costs, and a 4.05% additive
13 for common costs.⁶

14
15 In its *Seventeenth Supplemental Order* in Docket Nos. UT-960369, et al. the Commission
16 reaffirmed and continued the use of these cost factor percentages in the development of
17 Qwest's TELRIC cost studies. In that same order, the WUTC also stated the common cost
18 additive was to be applicable to all other network elements, not just the local loop.⁷

19 Although the Joint CLECs have previously sought to have the Commission limit the
20 inclusion of directly attributed and common costs to recurring charges, in order to

6 See *In the Matter of the Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket Nos. UT-960369, et al., *EIGHTH SUPPLEMENTAL ORDER*, dated May 11, 1998, at page 5. (Note: The 19.65% attributed cost percentage reflects a typographical error. Qwest's cost study, as approved by the Commission, actually employed a factor of 19.62% for attributed costs. Qwest's cost studies filed in this proceeding employ the 19.62% factor.)

7 See *In the Matter of the Pricing Proceeding for Interconnection, Unbundled Element, Transport and Termination, and Resale*, Docket Nos. UT-960369, et al., *SEVENTEENTH SUPPLEMENTAL ORDER*, dated September 23, 1999, at page 56, ¶206, and page 106, ¶435.

1 improperly exclude such costs from the development of non-recurring charges, the
2 Commission has ruled against such an approach. In the Commission's *Thirteenth*
3 *Supplemental Order* in Docket No. UT- 003013, the WUTC re-enforced the percentage
4 factors it had previously established for attributed and common costs, as well as their
5 applicability to non-recurring charges.⁸ Qwest used these previously established cost
6 factors in this phase of the Washington cost docket in order to maintain consistency in the
7 cost data and uniformity in cost recovery determination methods.

8
9 **Q. MR. GOSE HAS STATED THAT THE APPLICATION OF FACTORS FOR**
10 **DIRECTLY ASSIGNED COSTS DO NOT COMPORT WITH TELRIC**
11 **PRINCIPLES SET FORTH IN FCC RULE §51.505. IS HIS INTERPRETATION**
12 **CORRECT?**

13 **A.** No, it is not. The FCC's First Report and Order rules at §51.505 deal with, and allow for,
14 the inclusion of a reasonable portion of shared (attributable) and common costs in TELRIC
15 pricing. Mr. Gose appears to suggest that the non-recurring cost studies under review in
16 this phase of the cost docket should be based only on direct investment based costs,
17 exclusive of directly assigned costs, and that these costs should be the only costs loaded
18 with an allocation of forward-looking attributable and common costs. However, directly
19 assigned costs (e.g. the product management and sales costs he questions at page 3 of his
20 testimony) are very much a part of the TELRIC elements to which attributable and
21 common costs apply. Qwest's ICM costing methodologies employ an approach that

⁸ See *In the Matter of the Continued Costing and Pricing Proceeding for Interconnection, Unbundled Element, Transport and Termination*, Docket No. UT-003013, Part A, *THIRTEENTH SUPPLEMENTAL ORDER*, dated January 31, 2001 at page 6, ¶7 and pages 85-86, ¶260-261.

1 directly identifies wholesale product management and sales costs incurred and these costs,
2 along with investment-based costs, must be both loaded with attributable and common
3 costs. The shared nature of these loaded costs and this methodology is reinforced by the
4 FCC's TELRIC pricing guidelines. In regard to these types of attributable and common
5 costs, the FCC stated in its First Report and Order that:

6 Directly attributable forward-looking costs also include the incremental
7 costs of shared facilities and operations. More broadly, certain
8 shared costs that have conventionally been treated as common costs (or
9 overheads) shall be attributed directly to the individual elements to the
10 greatest extent possible. The forward-looking costs directly attributable
11 to local loops, for example, shall include not only the cost of the installed
12 copper wire and telephone poles but also the cost of payroll and other
13 back office operations relating to the line technicians, in addition to other
14 attributable costs.⁹
15

16 Mr. Gose's approach to exclude directly attributable and common costs, related to directly
17 assigned costs, would violate the directives given by the FCC.

18
19 Given the FCC's position regarding these costs, WUTC's prior rulings on this issue, and
20 Qwest's compliance with these rulings in filing its non-recurring cost studies in this
21 proceeding, Mr. Gose's issues regarding the development and application of directly
22 attributed and common cost factors to directly assigned costs in Qwest's cost studies must
23 be disregarded.
24

⁹ See FCC 96-325, the First Report & Order, *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, Section VII. Pricing Of Interconnection And Unbundled Elements, at ¶682.

Merger-Related Cost Factor Issues

1
2 **Q. AT PAGE 8 OF HIS TESTIMONY MR. GOSE EXPRESSED CONCERN OVER**
3 **QWEST'S USE OF COMMISSION-ORDERED DIRECTLY ATTRIBUTABLE**
4 **AND COMMON COST PERCENTAGES, IN LIGHT OF QWEST'S HIGHLY**
5 **PUBLICIZED POST-MERGER RELATED EMPLOYEE REDUCTIONS. IS THIS**
6 **CONCERN VALID?**

7 **A.** No, as I discussed earlier in my testimony, Qwest has appropriately adhered to the
8 Commission's prior orders for handling TELRIC-related costing issues and, in doing so
9 Qwest has produced consistent results and ensured continuity between the various phases
10 of this cost proceeding. On the other hand, Mr. Gose has erroneously interpreted post-
11 merger activities and thus he overreaches in his suggestion to further reduce Qwest's cost
12 factors, which would artificially and inappropriately restrict or prohibit Qwest from
13 recovering its costs of providing wholesale services in this phase of the cost proceeding.

14
15 **Q. HAS MR. GOSE PROPERLY PORTRAYED THE EMPLOYEE CHANGES THAT**
16 **OCCURRED AS A RESULT OF THE MERGER?**

17 **A.** No. In his critique of Qwest's employee changes post-merger, Mr. Gose appears to have
18 misunderstood or misrepresented the net change in employees. Either Mr. Gose's source
19 information was incorrect or he improperly evaluated Qwest's merger-related employee
20 changes and thus, his suggestion that Qwest had 80,000 employees at merger and that it
21 reduced that number post-merger by 24,800 is false. U S WEST had approximately
22 62,500 employees at the time of the merger; merging with Qwest initially added about
23 10,300 more bringing the total to approximately 72,800. By the end of year 2001, Qwest

1 had announced and implemented employee reductions of approximately 9,000 (5,000 in
2 2000 and 4,000 in 2001). Qwest has also announced its plan to reduce another 7,000
3 employees in 2002. Upon implementation of the latest publicized reduction Qwest has
4 indicated that it plans to have a work force of approximately 55,000 employees, net of
5 increases incurred in certain areas of the business. Although this final number corresponds
6 to Mr. Gose's final tally, his derivation ignored the original employee increase of 10,000,
7 misstated the number of employee reductions, which was 16,000, and thus, he misstated
8 the change, which is approximately a "net" 6,000, not his implied 24,800.

9
10 In his assessment of the U S WEST/Qwest merger, Mr. Gose also fails to acknowledge
11 that the employee statistics he uses are applicable to Qwest's "Total Company,"
12 telecommunication in-region, out-of-region, and international operations. Thus, not all of
13 the reductions would ever implicate activities associated with Qwest's wholesale
14 telecommunications operations.

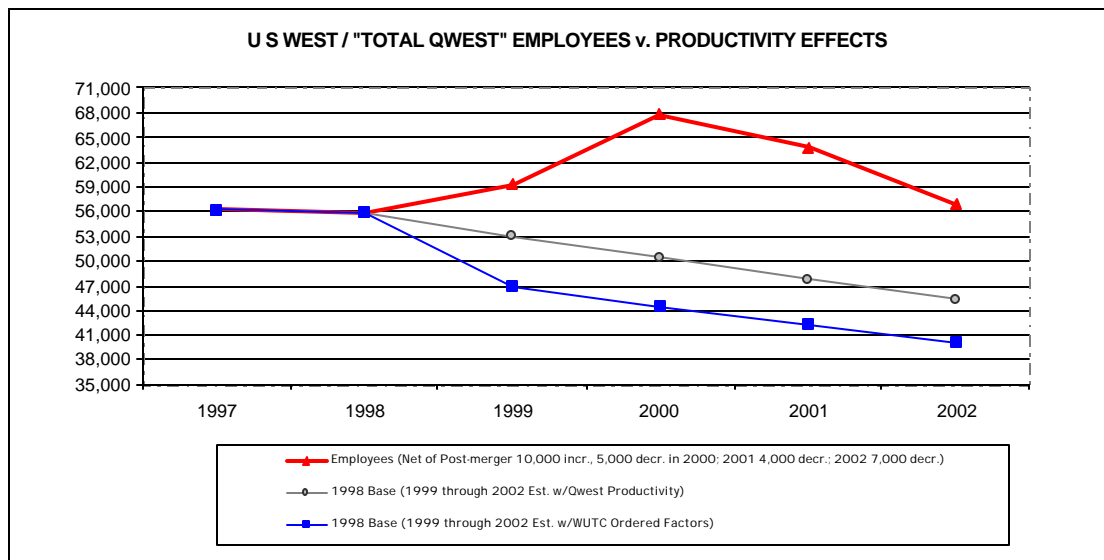
15
16 **Q. DO YOU AGREE WITH MR. GOSE'S ASSESSMENT AND IMPLIED**
17 **CONCLUSIONS REGARDING THE MERGER'S IMPACT ON QWEST'S**
18 **TELECOMMUNICATIONS OPERATING COSTS?**

19 **A.** No, I do not. Even if merger-related changes in employee levels and/or costs were an issue
20 regarding Qwest's telecommunications operations and cost study development (which they
21 were not due to the use of a 1998 base year), only a portion of the initial merger increase
22 and subsequent reductions would be applicable to Qwest's telecommunications operations.

1
2 Further limiting any concern regarding post-merger telecommunications operations is the
3 fact that Qwest has applied the Commission's directly attributed and common cost
4 percentage factors. These factors already provide a cost reduction of 32–35% from
5 Qwest's supported cost study factors for directly attributed and common costs. Whether
6 employing Qwest's cost factors for directly attributed and common costs, which reflect
7 productivity and inflation values, or using the percentage factors previously ordered by the
8 Commission, the factors are applied in this proceeding to 1998 base year data, which is
9 pre-merger. As a result, neither the initial increase in employees or operational cost
10 changes as a result of the U S WEST/Qwest merger, nor the subsequent employee
11 reductions and cost savings publicized by Qwest, have any effect on the modeled costs in
12 the cost studies presented to the Commission in this proceeding. Using a 1998 base year
13 and compounding the productivity and inflation factors produces cost trend lines which are
14 declining, unaffected by increases or decreases relating to the merger, and below that
15 which would be produced if post-merger costs were employed.

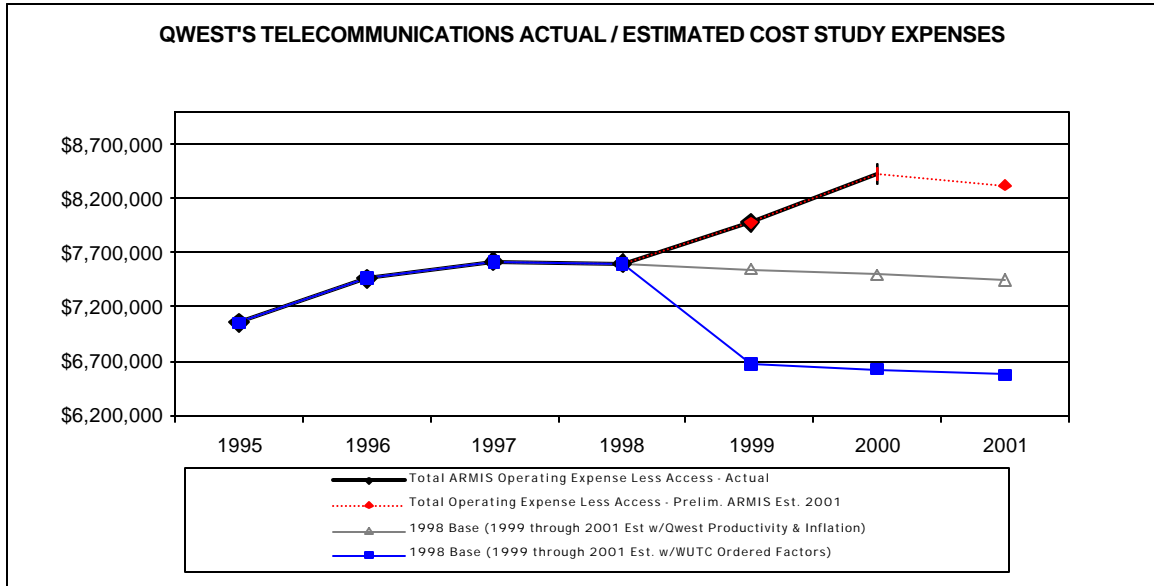
16
17 **Q. HAVE YOU PREPARED ANY MATERIAL THAT ILLUSTRATES THE**
18 **CHANGES IN QWEST'S EMPLOYEE LEVELS AND OPERATING EXPENSES**
19 **AND THEIR IMPACT ON QWEST'S COST STUDY FACTORS?**

1 A. Yes, I have. In order to illustrate the trend of employees/expenses inherent in Qwest's filed
2 cost studies I first applied Qwest's productivity assumptions to employee levels in order to
3 approximate the equivalent employee reductions inherent in the studies presented.
4 Applying Qwest's productivity assumptions would yield an equivalent reduction of
5 approximately 8,000 employees between 1998 and 2001; adjusting these values to further
6 reflect the Commission's ordered directly attributed and common cost factor reductions
7 would push that number to more than 13,000. As the following chart depicts, Qwest's cost
8 studies filed in this proceeding already reflect equivalent employee levels that are far
9 below the actual number of Qwest's employees.
10



11
12 In assessing actual operating expenses, I created a chart that depicts the application of
13 Qwest's productivity and inflation assumptions to Qwest's 1998 total operating expense
14 base data. I also developed a trend line on this chart that reflects the Commission's
15 ordered treatment of attributed and common. This second chart demonstrates that the

1 application of cost study factors to 1998 actual expense levels produces trend lines that are
2 well below actual expense levels.



3
4 Although Mr. Gose states in his testimony that: "The company known as Qwest today has
5 changed dramatically since this factor was determined. . . . which radically changed the
6 organization upon which the former USWC's prior cost studies were based"; this is not so.
7 The ARMIS operating expense data depicted in the chart above indicates that there really
8 hasn't been much change in the expense trend from the old U S WEST to the new Qwest.
9 Furthermore, it was wrong for Mr. Gose to confuse the "total Qwest corporate entity" with
10 the "telecommunications" portion of Qwest. The chart above clearly shows that
11 U S WEST/Qwest actual telecommunications operating expenses have been on an upward
12 trend since 1995, and that this trend has continued post-merger.

13

1 **Q. IN HIS DISCUSSION OF MERGER ISSUES, MR. GOSE INDICATED THAT HE**
2 **INTENDED TO FILE SUPPLEMENTAL TESTIMONY ONCE HE HAD**
3 **ANALYZED QWEST'S POST-MERGER COST LEVELS. DID HE EVER FILE**
4 **THIS TESTIMONY?**

5 **A.** No, he did not.
6

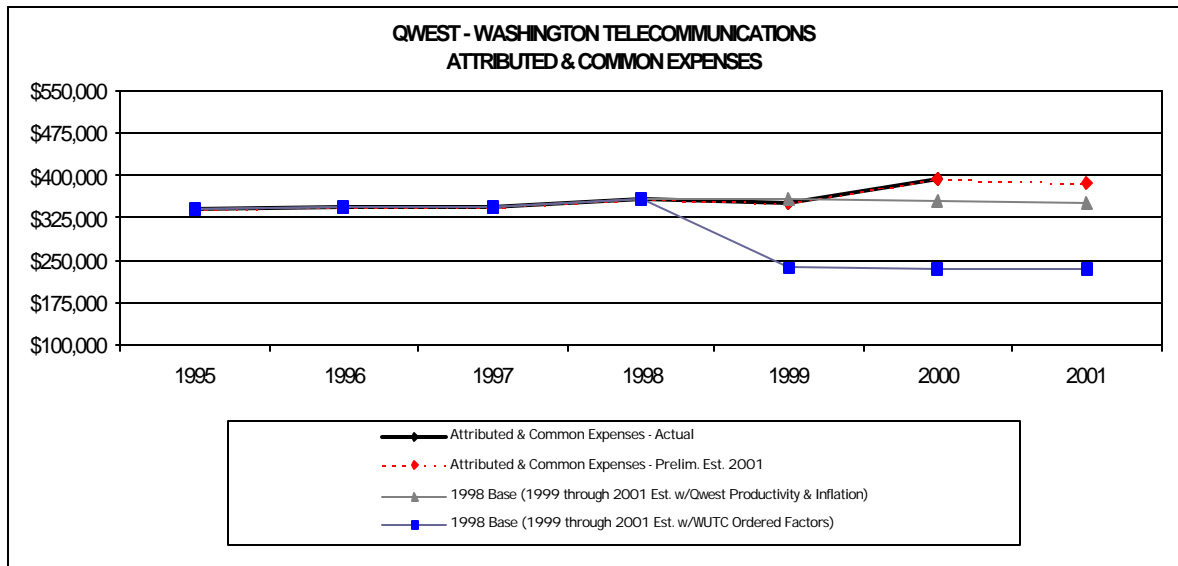
7 **Q. HAVE YOU REVIEWED QWEST'S POST-MERGER ATTRIBUTED AND**
8 **COMMON COSTS IN THE STATE OF WASHINGTON IN LIGHT OF MR.**
9 **GOSE'S UNSUPPORTED STATEMENTS REGARDING THE MERGER AND**
10 **SUSPECTED COST CHANGES?**

11 **A.** Yes, I have performed a review of the Washington attributed and common expenses post-
12 merger in order to assess Mr. Gose's issue. However I must reemphasize my earlier
13 testimony that, it would be inconsistent and inappropriate to follow Mr. Gose's suggestion
14 to consider changing attributed and common cost factors in this phase of the cost docket,
15 regardless of whether an analysis of post-merger operations indicates an increase or
16 decrease in the expenses used in setting cost factors ordered for use in earlier cost docket
17 phases.
18

19 **Q. WHAT DID YOUR REVIEW OF WASHINGTON POST-MERGER COSTS**
20 **INDICATE?**

21 **A.** My analysis of Washington's expenses was quite similar to the analysis I performed for
22 Total Qwest. As the following chart depicts, the total attributed and common expense trend

1 lines look very similar to those produced from Total Qwest actual expense data. That is,
2 the cost study trend lines are substantially below the actual expense levels.



3

4 **Q. WHAT CONCLUSIONS DID YOU REACH FROM THIS ANALYSIS OF POST-**
5 **MERGER ATTRIBUTED AND COMMON COSTS?**

6 **A.** I concluded that Mr. Gose's unsupported assertions regarding the effects of the merger
7 were false. My analysis clearly indicates that employing the Commission's directly
8 attributed and common cost factors produces cost levels that are below actual cost. And,
9 since Qwest has filed its studies in compliance with the Commission's prior rulings
10 regarding directly attributed and common cost factors, the cost studies in this proceeding
11 more than adequately addresses any post-merger employee or cost level concerns raised by
12 Mr. Gose.

13

1 **IV. FINAL CONCLUSIONS AND RECOMMENDATIONS**

2

3 **Q. WHAT FINAL CONCLUSIONS AND RECOMMENDATIONS DO YOU HAVE**
4 **REGARDING THE TESTIMONY PROVIDED BY MR. GOSE IN THIS**
5 **PROCEEDING?**

6 **A.** The issues raised in Mr. Gose's testimony were either misguided or moot. Therefore, I
7 recommend that the Commission disregard completely the issues raised in his testimony
8 and reaffirm the cost factors previously employed by Qwest in the other phases of this cost
9 proceeding and in its preparation of its non-recurring cost studies under review in this
10 phase of the cost docket.

11

12 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

13 **A.** Yes, it does.