

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Pricing Proceeding )  
for Interconnection, Unbundled )  
Elements, Transport and Termination, )  
and Resale )

DOCKET NO. UT-960369

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In the Matter of the Pricing Proceeding )  
for Interconnection, Unbundled )  
Elements, Transport and Termination, )  
and Resale for U S WEST )  
COMMUNICATIONS, INC. )

DOCKET NO. UT-960370

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In the Matter of the Pricing Proceeding )  
for Interconnection, Unbundled )  
Elements, Transport and Termination, )  
and Resale for GTE NORTHWEST )  
INCORPORATED )

DOCKET NO. UT-960371

REBUTTAL TESTIMONY  
OF  
ALLEN E. SOVEREIGN

April 25, 1997

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COMMUNICATIONS

WUTC DOCKET NO. UT-960369  
EXHIBIT NO. (7) 80  
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**GTE NORTHWEST INCORPORATED**

**REBUTTAL TESTIMONY OF**

**ALLEN E. SOVEREIGN**

**WUTC UT-960369, 960370, 960371**

1 **Q. PLEASE STATE YOUR NAME, ADDRESS AND PRESENT POSITION.**

2 A. My name is Allen E. Sovereign. My business address is 700 Hidden Ridge,  
3 Irving, Texas 75038. I am employed by GTE Telephone Operations as  
4 Manager - Capital Recovery.

5 **Q. HAVE YOU PREVIOUSLY PROVIDED TESTIMONY IN THIS DOCKET?**

6 A. Yes, I provided direct testimony in this docket on economic depreciation  
7 rates for use in forward-looking cost studies.

8 **Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?**

9 A. The purpose of this testimony is to reply to the comments of various parties  
10 who filed testimony in this proceeding on or about March 28, 1997.  
11 Specifically, I will reply to the claims by AT&T/MCI witness Mr. John Klick  
12 and Public Counsel witness Mr. William Dunkel that currently prescribed  
13 depreciation lives are appropriate for use in forward-looking cost studies.  
14 I will also comment on the testimony of Washington Independent Telephone  
15 Association ("WITA") witness Mr. Tom Kruse and the testimony of  
16 Commission Staff witness Mr. Thomas Spinks.

1 Q. WHAT IS THE METHODOLOGY THAT AT&T/MCI WITNESS KLINK AND  
2 PUBLIC COUNSEL WITNESS DUNKEL RECOMMEND FOR  
3 ESTABLISHING DEPRECIATION LIVES FOR USE IN THIS  
4 PROCEEDING?

5 A. Neither Mr. Klick nor Mr. Dunkel recommend a methodology for determining  
6 appropriate depreciation lives for use in forward-looking cost models.  
7 Instead, both Mr. Klick and Mr. Dunkel recommend the use of previously  
8 prescribed state and federal depreciation lives in such models.

9 Q. IS THE USE OF PREVIOUSLY PRESCRIBED DEPRECIATION LIVES  
10 APPROPRIATE FOR USE IN FORWARD-LOOKING COST MODELS?

11 A. No. As I explain in my direct testimony, "economic lives" must be used in  
12 forward-looking cost models, not prescribed lives. An "economic life" is the  
13 period of time over which an asset is used to provide economic value to  
14 GTE. In a competitive environment, such as the one resulting from the  
15 passage of the Telecommunications Act, the economic life of an asset  
16 shortens relative to the life of an asset under regulation. Prescribed lives,  
17 however, were established under a regulatory regime, and fail to account for  
18 the effect that competition in the telecommunications marketplace has on an  
19 asset's useful life.

20 In the GTE Depreciation Docket, this Commission recently recognized  
21 that competition and technological change may affect the useful life of

1 assets.<sup>1</sup> This Commission also noted that previous depreciation lives were  
2 prescribed without considering the impact that competition will have on an  
3 asset's useful life.<sup>2</sup> Despite the clear fact that competition and technological  
4 change will shorten the useful life of an asset, and the equally clear fact that  
5 State and FCC prescribed lives were established without considering  
6 competition, AT&T, MCI, and Public Counsel are content in asking this  
7 Commission to use previously prescribed lives in forward-looking cost  
8 studies.

9 **Q. DOES STAFF WITNESS SPINKS CONCUR THAT NEITHER THE**  
10 **CURRENT FCC LIVES OR THE CURRENT WUTC LIVES ARE**  
11 **APPROPRIATE?**

12 **A.** Yes. Staff witness Spinks indicates in his testimony that depreciation lives  
13 prescribed before the passage of the Telecommunications Act are outdated  
14 and must be revised before they can be used in forward-looking cost  
15 studies.<sup>3</sup>

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<sup>1</sup> In the Matter of the Petition of GTE Northwest, Incorporated For Depreciation accounting Changes, Washington Utilities and Transportation Commission, Docket No. UT-961632, Third Supplemental Order Accepting Review of Interlocutory Order; Denying Request to Reverse Interlocutory Ruling; Denying Petitions to Intervene, March 28, 1997, p. 8.

<sup>2</sup> Id. at 10.

<sup>3</sup> Testimony of Thomas Spinks at 13-14.

1 Q. MR. KLICK, ON BEHALF OF AT&T AND MCI, REFERENCES  
2 CALIFORNIA ECONOMIC LIVES. DID THE CALIFORNIA COMMISSION  
3 REJECT THE USE OF FCC LIVES AS FORWARD-LOOKING?

4 A. Yes. In a recent ruling, the California Public Utilities Commission ("CPUC")  
5 rejected the use of prescribed lives in cost studies and instead endorsed the  
6 use of economic lives.<sup>4</sup> The CPUC concluded that the economic lives used  
7 by LECs for external financial reporting purposes were the appropriate lives  
8 for use in forward-looking cost studies. The CPUC rejected the suggestion  
9 by AT&T and others that FCC prescribed lives, which were established prior  
10 to the passage of the Telecommunications Act and prior to the emerging  
11 competitive market, are forward-looking.

12 Q. WHAT DID THE CPUC ORDER CONCLUDE?

13 A. In its order, the CPUC commented:

14 We agree with Pacific that the schedules formally adopted in  
15 the represcription proceeding reflect the previous paradigm of  
16 the regulated monopoly environment, and so are difficult to  
17 justify in a cost study that looks forward to an environment in  
18 which there is local exchange competition. We also see little  
19 merit in the Coalition's original suggestion that we use FCC  
20 schedules. These schedules also reflect "the previous  
21 paradigm"; moreover, they are based on different assumptions  
22 and applied in different ways than our own.<sup>5</sup>  
23

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<sup>4</sup> California Public Utilities Commission Decision, No. D.96-08-021  
Adopted August 2, 1996, in Rule Making R.93-04-003, I.93-04-002.

<sup>5</sup> Id. at 52. The coalition mentioned in this passage includes AT&T,  
MCI, California Cable Television Association, California Association of Long  
Distance Carriers, and others.

1 It also seems to be the case, however, that Pacific is now  
2 using these schedules in financial reports it is required to file,  
3 and thus for purposes of these cost studies, the schedules  
4 also appear consistent with generally accepted accounting  
5 principles. The schedules also appear realistic for a firm  
6 having to operate in a competitive environment, as Pacific will  
7 soon have to do. Accordingly, we will approve their use in this  
8 proceeding.<sup>6</sup>

9 **Q. DID THE CPUC MAKE A SIMILAR FINDING WITH RESPECT TO GTE?**

10 A. Yes. The California Commission ordered GTE to use economic lives as well:

11 We find GTEC's arguments to be persuasive, and will  
12 therefore order GTEC to modify the depreciation rates used in  
13 the cost studies it has submitted only to the extent of the eight  
14 technology accounts...<sup>7</sup>

15  
16 Further, as explained in the rebuttal testimony of Mr. David Tucek, the lives the  
17 CPUC ordered GTE to adopt for these eight accounts are the same as, or are  
18 shorter than, the corresponding lives GTE has proposed in this proceeding.

19 **Q. DOES GTE RECOMMEND USING THE SAME ECONOMIC LIVES FOR**  
20 **COST STUDIES AND DEPRECIATION THAT IT IS USING IN ITS**  
21 **FINANCIAL BOOKS?**

22 A. Yes. The economic lives used in GTE's financial books are more reflective  
23 of a firm that anticipates operating in a competitive market. These same  
24 lives are what GTE proposes this Commission use in forward-looking cost  
25 studies.

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<sup>6</sup> Id. GTE is also using economic lives for financial and regulatory reporting.

<sup>7</sup> Id. at 75.

1    **Q.    PLEASE COMMENT ON MR. SPINKS STATEMENT THAT THE LIVES**  
2           **THAT STAFF WILL BE RECOMMENDING IN THE UPCOMING**  
3           **DEPRECIATION DOCKET ARE THE APPROPRIATE LIVES TO BE USED**  
4           **FOR FORWARD-LOOKING COST STUDIES.**

5    A.    While I generally agree with the premise that "updated" lives must be  
6           utilized, it remains imperative that the lives used in forward-looking cost  
7           models be the economic lives GTE is proposing. Using recommended lives  
8           that are longer than the economic lives GTE proposes will cause GTE's  
9           costs to be understated. The same result will occur if the depreciation  
10          docket concludes with an order forcing GTE to use asset lives that are  
11          longer than GTE's economic lives. Utilizing asset lives in forward-looking  
12          cost models that are not reflective of GTE's economic lives would violate the  
13          Telecommunication Act and prevent efficient competition from taking hold in  
14          the Washington local exchange market.

15   **Q.    PLEASE COMMENT ON THE ECONOMIC LIVES MR. TOM KRUSE**  
16          **REFERENCES IN HIS TESTIMONY ON BEHALF OF WITA.**

17   A.    Mr. Kruse references economic lives resulting from studies undertaken by  
18          Pacific Telecom, Inc. ("PTI") on behalf of WITA. These PTI studies provide  
19          further evidence as to the reasonableness of GTE's proposed economic

1 lives.<sup>8</sup> The chart below is a comparison of PTI's lives with GTE's proposed  
2 economic lives:

	PTI	GTE
3		
4	<b>Metallic Cable</b>	
5	Aerial	15
6	Underground	15
7	Buried	15
8		
9	<b>Nonmetallic Cable</b>	
10	Aerial	20
11	Buried	20
12	Underground	20
13		
14	Digital Switching	10

15 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

16 A. Contrary to the testimony of AT&T, MCI, and Public Counsel, current FCC  
17 and Washington state prescribed asset lives are outdated and inappropriate  
18 for use in establishing depreciation expense inputs in forward-looking cost  
19 models. Staff witness Mr. Spinks, as well as this Commission, agree that  
20 current depreciation lives are outdated and must be revised. In making  
21 such a revision, it should be recognized that economic lives are the  
22 appropriate lives to be used in all forward-looking cost models. Indeed, the  
23 economic lives proposed by GTE should be utilized. Failure to adopt and  
24 use economic lives at least as short as the lives GTE proposes will  
25 understate GTE's costs and prevent the introduction and development of  
26 efficient competition in the Washington local exchange market.

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<sup>8</sup> See Exhibit TK-2 of Mr. Kruse's direct testimony. By referring to this exhibit, GTE wishes only to cite the economic lives PTI recommends as evidence of the reasonableness of GTE's proposed lives. GTE neither agrees with nor endorses several of the other PTI study results.



1 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

2 A. Yes.