

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Pricing Proceeding) DOCKET NO. UT-960369
 for Interconnection, Unbundled)
 Elements, Transport and Termination,)
 and Resale)
)

In the Matter of the Pricing Proceeding) DOCKET NO. UT-960370
 for Interconnection, Unbundled)
 Elements, Transport and Termination,)
 and Resale for U S WEST)
 COMMUNICATIONS, INC.)

In the Matter of the Pricing Proceeding) DOCKET NO. UT-960371
 for Interconnection, Unbundled)
 Elements, Transport and Termination,)
 and Resale for GTE NORTHWEST)
 INCORPORATED)

REBUTTAL TESTIMONY
 OF
 DONALD C. EACHUS

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WUTC DOCKET NO. UT 960369
 EXHIBIT NO. (T) 183
 ADMIT W/D REJECT

GTE NORTHWEST INCORPORATED

REBUTTAL TESTIMONY OF

DONALD C. EACHUS

WUTC UT-960369, 960370, 960371

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Donald C. Eachus. My business address is One GTE Place,
3 Thousand Oaks, California.

4 **Q. DID YOU PREVIOUSLY FILE DIRECT TESTIMONY IN THIS DOCKET?**

5 A. Yes. On March 27, 1997, I filed direct testimony (DCE-T), and Exhibit Ex.
6 ___ (DCE-1). I will refer to that exhibit in this testimony.

7 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

8 A. The purpose of my testimony is to respond to certain issues discussed in
9 the Direct Testimony of AT&T witness Julie Dodds, MCI Witness Tony
10 DiTirro and WUTC witnesses Paula M. Strain and Willaim W. Dunkel.
11 References to this testimony will be "Dodds Test."; "DiTirro Test."; "Strain
12 Test." and "Dunkel Test."

13 **Q. HOW IS YOUR REBUTTAL TESTIMONY STRUCTURED?**

14 A. I will first address AT&T's avoided cost study methodology and discount
15 proposal as discussed by Ms. Dodds. I will then address MCI's avoided
16 cost study methodology as discussed by Mr. DiTirro. The final section of

1 my testimony will address the avoided cost proposal and issues put
2 forward on behalf of WUTC by Ms. Strain and Mr. Dunkel.

3 **Q. WOULD YOU PLEASE SUMMARIZE YOUR UNDERSTANDING OF**
4 **AT&T'S POSITION REGARDING THE CALCULATION OF AN AVOIDED**
5 **COST DISCOUNT RATE FOR GTE NORTHWEST IN WASHINGTON?**

6 A. Yes. Ms. Dodds presents AT&T's position on GTE's avoided costs. Ms.
7 Dodds uses, as a starting point, the ARMIS data showing GTE's actual
8 costs as filed with the FCC. Ms. Dodds then relies, in part, on the now-
9 stayed provisions of the FCC's Part 51 Rules which set forth a
10 methodology to determine both the direct and indirect costs that can
11 reasonably be avoided. Ms. Dodds began by considering certain
12 rebuttable presumptions concerning the amount of avoided costs in
13 various ARMIS accounts: Product Management (6611), Sales (6612),
14 Product Advertising (6613), and Customer Services (6623). Ms. Dodds,
15 however, uses the 100% avoided costs presumption instead of the 90%
16 presumption specified by the FCC. She used a 100% avoided cost factor
17 for Call Completion (6621) and Number Services (6622) notwithstanding
18 GTE's claimed regulatory obligation to make these services available for
19 resale to all CLECs. Ms. Dodds adds several additional assumptions of
20 avoided direct costs that were not included in the FCC's analysis of
21 avoided costs: Depreciation/Operator Systems (6560), Plant Operations
22 Administration (6534), and Testing (6533). Ms. Dodds also computes an
23 avoided indirect cost factor. Ms. Dodds rejects the FCC's position when it

1 comes to the calculation of the indirect cost factor and uses an approach
2 which produces a higher discount rate. Finally, Ms. Dodds uses data
3 from another telephone company (Bell Atlantic) located in another state
4 (Pennsylvania) to support her analysis of an access and miscellaneous
5 rate adjustment.

6 In sum, AT&T does not present any proof that its avoided cost
7 presumptions and assumptions bear any reasonable relationship to
8 GTE's actual avoided costs. It is for that reason that AT&T proposes a
9 totally unrealistic and unfair avoided cost discount of 30.84%.

10 **Q. SHOULD THIS COMMISSION ADOPT AT&T'S AVOIDED COST**
11 **METHODOLOGY WHEN ESTABLISHING A DISCOUNT FOR GTE?**

12 A. No. AT&T has not conducted an in-depth analysis of GTE's work
13 activities or its actual costs. AT&T bases its "study" on arbitrary and
14 unrealistic presumptions and assumptions wholly unrelated to GTE's
15 business operations. Hence, the avoided cost discounts proposed by
16 AT&T's study are artificially high, and are not in any way representative of
17 the costs that reasonably can be avoided by GTE when services are
18 offered for resale. Therefore, AT&T's study cannot be used by this
19 Commission in setting resale rates in this proceeding.

20 **Q. IN SUMMARY, HOW DOES GTE'S POSITION ON THE AVOIDED COST**
21 **STUDY ISSUES DIFFER FROM THAT OF AT&T?**

22 A. GTE's position differs from that of AT&T in the following significant
23 respects:

1 (1) First, in determining its avoided cost discount, AT&T uses the
2 hypothetical construct that GTE will cease retail operations entirely and
3 instead provide all of its services through wholesale channels. This is not
4 a valid assumption. GTE will not exit the retail market and will continue
5 to offer retail services. In fact, a wholesaler will benefit if GTE maintains
6 its retail line of business because GTE will retain the incentive to bring
7 new and improved services to its customers. In turn, GTE will continue to
8 offer existing and new retail services on a wholesale basis. Any contrary
9 assumption results in an inflated avoided cost discount percentage in
10 Account 6611 (Product Management) and would encourage GTE to exit
11 the retail market, thereby undermining the competitive environment that
12 the Commission is striving to establish.

13 (2) For Accounts 6611 (Product Management), 6612 (Sales), 6613
14 (Advertising) and 6623 (Customer Service), AT&T asserts that 100% of
15 the expenses in these accounts are avoided based on the conclusory,
16 unsupported assumption of Ms. Dodds that "(w)holesale customers will
17 not require these services and therefore should not be required to pay for
18 them." (Dodds Test. 11-12.) But she offers no proof to support this
19 assertion. Ms. Dodds is comfortable relying on the summary GTE ARMIS
20 data in each of these accounts. She also seems comfortable in relying on
21 data from another company (Bell Atlantic) in another state (Pennsylvania)
22 but chooses to ignore (while not disputing the accuracy of) all the GTE
3 data that describe the costs for each of the functions within each of these

1 expense accounts that would permit her to calculate the correct avoided
2 cost discount. Ms. Dodds cannot accept GTE's data when it supports her
3 position, and ignore it when it does not.

4 (3) AT&T argues that operator services costs, including call
5 completion and number services (Accounts 6621 and 6622) and what
6 AT&T purports are its associated depreciation expense (Account 6560),
7 should be excluded for purposes of determining the indirect cost factor
8 and the overall wholesale discount since AT&T asserts that it does not
9 intend to use GTE's operators. However, the discount rate set by the
10 Commission is for all services and all CLECs, not just operator services
11 and AT&T.

12 Operator services have separate tariffed cost based rates and the
13 expenses associated with Operator Services are not included in the rates
14 for other retail services offered for resale. Hence, AT&T will "avoid"
15 paying the tariffed rates for operator services if it elects to provide its own
16 operator services and not subscribe to those offered by GTE. In turn,
17 GTE's revenues will decrease.

18 (4) AT&T argues, without any proof based on GTE's operations,
19 that a portion (20%) of testing and operations plant administration
20 expenses (Accounts 6533 and 6534) associated with the testing of
21 customer facilities will be avoided by GTE. AT&T is wrong. The facilities
22 which will be tested and the records which must be maintained to provide
23 the resold services will continue to be part of GTE's network in a

1 wholesale environment. There is not a different service standard for
2 wholesale services versus retail services. Thus, there will be no avoided
3 costs. AT&T does not provide any support in the record for its
4 assumption that 20% of these expenses will be avoided, and in fact, none
5 will be. Ms. Dodds also erroneously assumes a one-to-one relationship
6 between Testing expenses and Operations Plant Administration expenses
7 when in fact no such relationship exists.

8 (5) AT&T inflates the indirect expense factor of 22% by
9 incorrectly using only total direct expenses in the denominator rather than
10 total expenses. Dodds Test. 13-14. As discussed in my direct testimony,
11 the FCC (First Report and Order, ¶ 918), as well as GTE, correctly
12 calculated the indirect expense factor by including all expenses in the
13 denominator of expenses in that indirect expense account do not solely
14 support direct expenses.

15 (6) AT&T mistakenly identifies other expenses such as
16 depreciation and amortization for general support assets and return and
17 taxes as avoidable costs. Ms. Dodds justifies an adjustment of
18 depreciation and amortization for general support assets with the
19 rationale that "assets that were previously used to support the retail
20 business will not be required in their entirety for the provision of the
21 ILEC's wholesale business." (Dodds Test., 13-17) These adjustments
22 inflate the avoided cost discount and highlight the artificial construct
3 surrounding AT&T's methodology. GTE must maintain its investments.

1 Hence, calculating a return on investment discount for services inflates
2 the discount by including costs that will not be avoided, and it undermines
3 GTE's ability to recover its costs.

4 (7) AT&T did not conduct any analysis of costs that will - - or
5 can reasonably - - be avoided. AT&T must analyze more detailed data
6 than that available from the ARMIS reporting system to make reliable
7 judgments about specific work functions that will or will not be avoided.
8 GTE has presented the necessary detailed analysis to determine avoided
9 costs in the form of its Workcenter review. As with the computation of
10 GTE's ARMIS expense accounts, this was done on a national basis. This
11 was done on a national basis consistent with the way the underlying
12 activities are organized within the GTE system. AT&T's superficial
13 approach overlooks critical details. For example, AT&T ignores the fact
14 that Customer Service Expenses (Account 6623) includes substantial
15 expenses incurred for carrier access account maintenance. None of the
16 expenses associated with carrier access work functions can be avoided
17 as they already support a wholesale line of business (carrier access
18 services) which is not available for resale at wholesale rates. Yet, the
19 AT&T analysis, as well as that of the FCC, made no allowance for this fact
20 because its analyses use data that lack the necessary detail to make
21 informed judgments about what costs will be avoided. Although there are
22 a large number of Workcenter accounts which I will not attempt to
23 address individually at this time, one other example helps demonstrate my

1 point. GTE's study includes Workcenter detail (3/27 Att. 2A, p. 3) which
2 identifies costs associated with Billing Systems Support and End User
3 Billing (lines 77 and 80-82). These activities will not be avoided in a
4 wholesale environment since GTE will still have to provide a bill with
5 individual customer detail and send it to the CLEC. These activities
6 support the process of "producing" a bill (i.e., reviewing, monitoring, and
7 balancing billing data), bill production, and in turn the supporting
8 activities. Yet, AT&T's analysis improperly treats these expenses as
9 avoided from account 6623.

10 **Q. HOW DID GTE PREPARE THE WORKCENTER ANALYSIS FOR THE**
11 **INDIVIDUAL ARMIS ACCOUNTS RELIED UPON BY AT&T?**

12 A. As described in my March 27, 1997 testimony, pp. 20-22, GTE conducts
13 many of its operations through Workcenters that service more than one
14 state. Each Workcenter's expenses are recorded in compliance with the
15 section of the FCC rules and regulations which contain the standard chart
16 of accounts. GTE then allocates these expenses to individual states
17 according to an allocation manual approved by the FCC. GTE is required
18 by the FCC to report the four digit ARMIS data to the FCC. This data is
19 publicly available.

20 The ARMIS expense accounts include the four digit accounts used
21 by both AT&T and GTE in this proceeding (E.g., 6611, 6612 etc.). GTE's
22 avoided cost study breaks down these broad ARMIS accounts into an
23 analysis of the work actually done for these accounts and the expenses

1 associated with the functions (hereinafter "Workcenter expense
2 accounts"). The Workcenter level identification of expenses are kept in
3 the regular course of GTE's business and contain additional information
4 necessary to understand and analyze the expenses in the four digit
5 ARMIS data for the purpose of determining avoided retail costs.

6 **Q. HAS AT&T CORRECTLY IDENTIFIED THE PRODUCT MANAGEMENT**
7 **EXPENSE (ACCOUNT 6611) THAT GTE WILL AVOID IN A RESALE**
8 **ENVIRONMENT USING ALL AVAILABLE DATA?**

9 A. No. In her direct testimony, Ms. Dodds relies solely on her "presumption"
10 of 100% avoided costs and does not present any proof to support her
11 assertion. The Product Management expense account is comprised of a
12 number of Product Management Workcenter accounts as well as other
13 Workcenter accounts. The activities covered by the Product
14 Management Workcenters are detailed in 3/27 Att. 2A, page 2. The
15 majority of the expenses in this account, and the functions performed by
16 the Workcenters which support it, will not be avoided in a wholesale
17 environment. These primary functions are necessary to manage the life-
18 cycle of the products and services, forecast the demand of the services,
19 and price and tariff the services. These functions account for 91% of the
20 Product Management account (6611). Contrary to the claims of AT&T,
21 these functions and the other functions performed by the Product
22 Management Workcenters and their associated costs will not be avoided.

Included in this account are substantial dollars for Product Management expenses for servicing the interexchange carriers. These costs will not be avoided in the provision of retail services on a wholesale basis. In addition, these costs are not contained within the retail rates subject to resale. Ms. Dodds' study purports to adjust for all access and miscellaneous expenses through her 2% adjustment based on an analysis of Bell Atlantic data from Pennsylvania. Besides the problem of using non-GTE data, the calculation shown on Worksheet 2 of Exhibit JSD-3 fails to identify the costs contained in the numerator other than a single word description. AT&T's adjustment is unreasonable as it indicates that 2% of GTE's operations in Washington - or less than \$8 million in 1995 expenses - generated in excess of \$200 million in access and miscellaneous revenues. GTE's Workcenter analysis has the detail of the Workcenter activities that are recorded in each four digit account that allows for the proper identification of only those expenses associated with retail services that will be avoided.

Q. WHY SHOULD AT&T BE REQUIRED TO CONTRIBUTE TO THE EXPENSES IN THIS ACCOUNT IF THESE NEW PRODUCTS WILL BE SOLD IN THE FUTURE?

A. GTE is being required to make all of its retail services and products available to CLECs on a wholesale basis. The CLECs will use these services and products to capture and retain GTE's customers. It would be totally unfair to GTE to eliminate the expenses associated with the

1 development of these products and services in the calculation of a
2 wholesale discount. The CLECs cannot have it both ways. They cannot
3 insist on access to GTE's new products and services and at the same
4 time refuse to pay their fair share of the costs needed to develop them.

5 **Q. WHAT AVOIDED COST DISCOUNT HAS AT&T APPLIED TO**
6 **OPERATOR SERVICES AND DIRECTORY ASSISTANCE (OS/DA)**
7 **ACCOUNTS 6621 AND 6622?**

8 A. AT&T claims an avoided cost discount of 100% for account 6621 and
9 account 6622 assuming AT&T will self provision these services.

10 **Q. WHAT IS GTE'S POSITION ON THE TREATMENT OF OPERATOR**
11 **AND DIRECTORY ASSISTANCE SERVICE COSTS (ACCOUNTS 6621**
12 **AND 6622) IN THE AVOIDED COST STUDY?**

13 A. Operator Services and Directory Assistance are offered by GTE on a
14 retail basis as discrete tariff items at cost based rates. GTE proposes to
15 offer tariffed operator services and directory assistance services for
16 resale on the same terms and at the same rates as the corresponding
17 retail offerings. There are no costs that can reasonably be avoided when
18 the services are offered for resale; the services are offered and provided
19 in the same manner whether provided on a wholesale or a retail basis.
20 The costs for these services are recovered through separate rates, and
21 are not included in the rates for other services offered for resale. As I
22 indicated in my direct testimony, the Workcenter expenses associated
3 with Secondary Distribution Costs is considered avoided in GTE's study.

1 This decision was based on the premise that the reseller will be charged
2 on a per directory basis for secondary distribution of directories.

3 Therefore, it is appropriate to reflect that 0% of the costs for Operator
4 Services and 24.26% of Number Services can reasonably be avoided.

5 **Q. WHY SHOULD OPERATOR AND DIRECTORY ASSISTANCE COSTS**
6 **BE INCLUDED IN THE WHOLESALE DISCOUNT CALCULATION IF**
7 **AT&T WILL NOT USE THESE SERVICES?**

8 A. This Commission is establishing a single discount factor to be applied to
9 all resale services for all companies for services requested now and in the
10 future. AT&T suggests that the "model" can be adjusted where the CLEC
11 does not intend to use these services (Dodds Test. 12). The Act directs
12 that all retail services be made available for resale at retail rates less
13 avoided cost. An adjustment could be appropriate only if the Commission
14 determined that Operator Services were not subject to resale. Even then,
15 the adjustment would not be to categorize the expenses as avoided but to
16 exclude the Operator Services revenues from the denominator of the
17 avoided cost calculation. If AT&T does not want to purchase these
18 services on a resale basis then it is not required to. However, it cannot
19 use any claimed avoided costs in this account to increase the wholesale
20 discount applied to other services purchased by AT&T and other CLECs.
21 This occurs because the model proposed by AT&T develops a factor that
22 is the ratio of avoided costs to total costs (including Operator Service
3 costs) and then applies the factor to retail revenues including the operator

1 rates which AT&T indicates it will not purchase. In effect, AT&T will avoid
2 the operator service costs once when it purchases other discounted retail
3 services and a second time when it self-provisions its own operator
4 services and does not purchase GTE's wholesale operator services
5 offering.

6 **Q. HOW HAS AT&T TREATED ACCOUNT 6623, CUSTOMER SERVICES?**

7 A. Ms. Dodds, on page 12 of her testimony, states that "costs in these
8 accounts are the direct costs of serving customers." Therefore, AT&T
9 claims an avoided cost discount of 100% for Customer Service account.
10 This claim is not supported by any empirical data whatsoever. AT&T's
11 position is based on a mistaken or superficial understanding of the
12 account. The expenses in Account 6623 are primarily associated with the
13 following Workcenters and Workcenter functions: Ordering Workcenters,
14 Billing and Collection Workcenters, Carrier Access Workcenters. (3/27
15 Att. 2A, p. 2). Together they represent over 80% of the expenses
16 recorded by GTE in Account 6623.

17 Through its Workcenter analysis, GTE's study correctly accounts
18 for the functions and related expenses in account 6623 that will be
19 avoided associated with Ordering Workcenters (including customer
20 contact, customer relations, customer support and service fulfillment
21 functions), by identifying all recurring retail costs in these Workcenters as
22 100% avoided. This leads to an overall avoided retail discount for all
23 Workcenters of 43.41% for account 6623. (See 3/27 Att. 2A, p.1)

1 Moreover, the costs associated with GTE's current wholesale line
2 of business (Carrier Access Workcenters and Billing and Collection
3 Workcenters) are also booked to account 6623. These costs will not be
4 avoided. GTE has correctly identified the costs associated with its
5 wholesale line of business in the Customer Service Account (6623) while
6 AT&T has not. In GTE's study the Carrier-related Customer Service
7 Account expenses amount to 13.2% of the total Customer Service
8 expenses. (3/27 Att. 2A, p.1) Ms. Dodds' Access and Miscellaneous
9 adjustment adds only \$1.003 million back for \$56.903 million of avoided
10 direct expenses or 1.76%, thus proportionally allowing only \$0.5 million in
11 Account 6623 for the existing wholesale activities not subject to resale
12 (Access and Public telephone) .

13 **Q. MS. DODDS CONCLUDES THAT SALES EXPENSES (ACCOUNT 6612)**
14 **ARE 100% AVOIDABLE. DO YOU AGREE WITH THIS OPINION?**

15 **A.** No, the sales account contains expenses for both the retail and wholesale
16 sales functions. GTE has correctly identified and removed all retail sales
17 expense from the sales expense account and computed a discount factor
18 of 64.46%. (3/27 Att. 2A, p. 1) Ms. Dodds does not account for the fact
19 that GTE currently has a "wholesale" sales force supporting its switched
20 and special access services. These sales expenses are included in
21 Account 6612 and will not be avoided. Therefore, Ms. Dodds' factor of
22 100% is an invalid assumption. The remaining 35.54% represent sales

1 expenses which support the carrier access wholesale function and will not
2 be avoided by GTE when its retail services are resold.

3 **Q. DID AT&T IDENTIFY ANY OTHER EXPENSE ACCOUNTS AS DIRECT**
4 **AVOIDABLE EXPENSES?**

5 A. Yes. Ms. Dodds identified Accounts 6220 (Operator Systems Expenses)
6 and its associated depreciation in Account 6560 as 100% avoided.
7 Account 6620 includes Accounts 6621 (Call Completion), 6622 (Number
8 Services) and 6623 (Customer Services). I have discussed Account 6623
9 previously. 20% of Accounts 6533 (Operations Testing) and 6534
10 (Operations Plant Administration) are also determined by Ms. Dodds to be
11 avoided.

12 **Q. DO YOU AGREE WITH THE INCLUSION OF THESE ACCOUNTS AS**
13 **DIRECT AVOIDABLE EXPENSE ACCOUNTS?**

14 A. No, I do not. As previously discussed in regard to OS/DA in Accounts
15 6621 and 6622, except for Secondary Directory expenses, GTE will
16 experience no avoided costs in accounts associated with OS/DA and
17 therefore its associated depreciation Account 6560 should not be treated
18 as avoided.

19 Accounts 6533 and 6534 reflect expenses GTE will still incur
20 whether a service is offered on a retail or wholesale basis; therefore there
21 are no avoided costs. GTE will be required to maintain the same service
22 standards for its resold services as it does for its retail services. In order
23 to ensure these quality standards GTE must perform the same network

1 testing and plant operations administration as it would without resale.

2 Therefore, the same expenses will be incurred in a resale environment.

3 Any testing that AT&T will do will not replace the testing done by GTE.

4 The end-users contact that would be performed by AT&T is not recorded
5 in Account 6533.

6 **Q. DO YOU AGREE WITH MS. DODDS' CONCLUSION THAT THERE**
7 **SHOULD BE A 20% AVOIDED DISCOUNT FOR ACCOUNTS 6533 AND**
8 **6534 ?**

9 A. No. AT&T has not conducted any studies involving GTE's operations to
10 support this conclusion. There is not a different service standard for
11 wholesale services versus retail services. Thus, there will be no avoided
12 costs. AT&T does not provide any support in the record for its
13 assumption that 20% of these expenses will be avoided, and in fact, none
14 will be. Ms. Dodds also errors in assuming a one-to-one relationship
15 between testing expenses and operations plant administration expenses.
16 Operations plant administration expenses represent costs for supervising
17 plant operations, planning, coordinating and monitoring plant operations;
18 and performing staff work such as developing methods and procedures,
19 preparing and conducting training and coordinating safety programs. It is
20 incorrect to reduce Account 6534 expenses as Ms. Dodds does in her
21 avoided cost study. Moreover, as noted above, AT&T's calculation of a
22 20% discount is wholly speculative. It is based on AT&T's operations and
3 AT&T's erroneous assumptions. The introduction of electronic interfaces

1 so that AT&T will have computer access to GTE's operations support
2 systems will not reduce any of the customer related testing costs in
3 Account 6533 so long as GTE is providing the resale service. GTE will
4 still perform testing before rolling a repair truck to clear the trouble
5 because it is GTE's equipment and network being utilized.

6 **Q. WHAT IS THE IMPACT OF TREATING THESE EXPENSES AS**
7 **AVOIDED?**

8 A. Treating these expenses as avoided inflates the avoided cost discount in
9 two ways. First, by incorrectly identifying direct expenses as avoided, the
10 discount for direct expense is erroneously increased. Second, because
11 avoided direct expenses are the numerator for the calculation of the
12 indirect expense factor, this factor is erroneously inflated causing an
13 increase in the indirect avoided costs, thereby producing a further
14 overstated avoided cost discount.

15 **Q. IS AT&T'S INDIRECT FACTOR BASED ON THE FCC'S APPROACH?**

16 A. No, it is not. AT&T's factor is the ratio of avoidable direct expenses to
17 total direct expenses. This is inconsistent with the rationale stated by the
18 FCC that "indirect or shared costs, such as general overheads, *support all*
19 *of the LEC's functions.*" Order at ¶ 912 (emphasis added). For example,
20 The Human Resources department hires lawyers and accountants
21 (indirect expenses) as well as retail sales personnel (direct expenses)
22 and therefore the indirect expenses must be included in the denominator

1 of the indirect avoided cost factor. GTE's avoided cost study correctly
2 reflects that indirect expenses support all of the LEC's functions.

3 **Q. HAS AT&T CORRECTLY IDENTIFIED OTHER EXPENSES SUCH AS**
4 **DEPRECIATION AND AMORTIZATION FOR GENERAL SUPPORT**
5 **ASSETS AND RETURN AND TAXES AS AVOIDABLE COSTS?**

6 A. No, AT&T incorrectly identifies other expenses such as depreciation and
7 amortization for general support assets and return and taxes as indirect
8 avoidable costs. Ms. Dodds erroneously assumes that all General
9 Support assets and therefore the resulting depreciation is related to direct
10 expenses. As shown in Exhibit JSD - 3, worksheet 1, General Support
11 Assets include the buildings that house GTE's central offices. Under Ms.
12 Dodds method the indirect avoided factor of 22% applied to the General
13 Support-related depreciation results in 22% of all the buildings expenses
14 being avoided. This result is clearly unrealistic. This adjustment inflates
15 the avoided cost discount and highlights the artificial construct
16 surrounding AT&T's methodology. Likewise, the calculation of return and
17 taxes is similarly erroneous as it is calculated based on the general
18 support assets.

19 **Q. DID AT&T TREAT UNCOLLECTIBLES CONSISTENTLY WITH THE**
20 **FCC ORDER?**

21 A. No, it did not. AT&T has chosen an arbitrary factor of 100% avoidable for
22 uncollectibles.

1 **Q. IS AT&T'S FACTOR BASED ON ACTUAL GTE UNCOLLECTIBLE**
2 **EXPERIENCE?**

3 A. No, it is not, nor is AT&T's factor derived in a manner consistent with the
4 purpose of the development of an avoided cost methodology: to remove
5 the avoided costs that GTE will experience in providing wholesale
6 services to resellers. AT&T either assumes that it will be the only reseller
7 doing business with GTE or it assumes that reseller-specific avoided cost
8 discounts are being calculated. Both are incorrect. GTE, however,
9 conducted an analysis of its actual uncollectible expense based upon its
10 books and records to derive an avoided factor of 78.08%. (Ex. ___ (DCE-
11 1) Attachment 1B).

12 **Q. HAS AT&T CORRECTLY ACCOUNTED FOR "ADDBACKS" FOR**
13 **ADDITIONAL COSTS ASSOCIATED WITH THE PROVISION OF**
14 **WHOLESALE SERVICES?**

15 A. No. AT&T's study does not account for any addbacks. At a minimum,
16 AT&T's methodology should be adjusted to reflect that the carrier access
17 line of business distribution costs are an appropriate substitute for
18 wholesale addbacks. The resale of local service is a new environment
19 and data are not yet available regarding the additional cost to provision
20 these services to CLECs. However, there will be costs associated with
21 the provisioning of services for resale and the cost causer - the CLEC -
22 should be responsible for them.

1 Q. HAVE YOU REVIEWED THE TESTIMONY OF ANTHONY J. DITIRRO
2 ON BEHALF OF MCI?

3 A. Yes, I have.

4 Q. COULD YOU PLEASE COMMENT ON MCI'S PROPOSAL?

5 A. Yes. Inherent in MCI study are some of the same flaws found in AT&T's,
6 such as the avoidable, rather than the avoided cost standard. Mr. DiTirro
7 has prepared an analysis for GTE which calculates the discount at
8 18.11%.

9 Q. HAS MR. DITIRRO CORRECTLY IDENTIFIED THE DIRECT COSTS
10 WHICH WILL BE AVOIDED BY GTE?

11 A. No. Mr. DiTirro's position generally follows with the now stayed
12 requirements stated in the FCC's Part 51 Rules, including the definition of
13 direct expenses that are to be included in determining avoided costs.

14 Q. SHOULD THE FCC REBUTTABLE PRESUMPTIONS APPLY FOR
15 ACCOUNTS 6611, 6612, 6613 AND 6623?

16 A. No. The FCC did not support its presumptions that direct expenses would
17 be avoided, nor its assumptions that the substitute costs for these
18 functions performed on a wholesale basis would amount to only ten
19 percent of retail costs. With respect to the latter, the FCC stated at
20 paragraph 928 of the First Report and Order: "Given the lack of evidence,
21 and the wide range of estimates that have been made by these states, we
22 find it reasonable to assume, for purposes of determining a default range
23 of wholesale discount rates, that ten percent of the costs in accounts

1 6611, 6612, 6613, and 6623 are not avoided by selling services at
2 wholesale.” (First Report and Order, ¶ 928) However, since GTE has
3 submitted evidence supporting its avoided cost percentages, there is no
4 reason to consider MCI’s presumption of 90% avoidance.

5 **Q. WHY IS MCI’S 90% FACTOR ASSOCIATED WITH PRODUCT**
6 **MANAGEMENT EXPENSE (ACCOUNT 6611) INAPPROPRIATE?**

7 A. Mr. DiTirro’s rationale that product management is a “(f)unction
8 specifically tied to determining the market demand for retail sales” is
9 inaccurate for numerous reasons. First, since the retail service is already
10 designed, when resold the reseller does not have to incur many of these
11 expenses (e.g., product and service identification and specification).
12 Second, because product management expenses include expenses for
13 wholesale services, Mr. DiTirro’s statement is simply untrue. Third, GTE
14 must maintain these offerings for itself and for all other CLECs and,
15 therefore, the majority of Product Management expenses will not be
16 avoided.

17 **Q. HAS MCI CORRECTLY CALCULATED THE FACTOR ASSOCIATED**
18 **WITH SALES EXPENSE (ACCOUNT 6612)?**

19 A. No. Mr. DiTirro’s analysis does not account for the fact that many of the
20 Workcenters associated with Sales (e.g., Advanced Network Products
21 Group, Branch Field Services, Branch Market Response) support both
22 GTE’s current retail and wholesale product lines. Therefore, these
23 Workcenter costs are not 100% avoided. I calculate they are 63%

1 avoided based on the relationship between carrier access and retail sales
2 as a percentage of revenue. The calculation of 63% is shown on
3 Attachment 2B of GTE's Avoided Cost Study. Together with other
4 Workcenters that record activity to Account 6612, the overall avoided
5 factor is 64.46%. (3/27 Att. 2A)

6 **Q. HAS MCI CORRECTLY CALCULATED THE AVOIDED COST FACTOR**
7 **FOR ACCOUNT 6623?**

8 A. No. Mr. DiTirro assumes that 90% of the expenses associated with
9 service orders will be avoided. Mr. DiTirro's position is incorrect for the
10 same reasons discussed previously with respect to Ms Dodds' 100%
11 assumption. Even Mr. DiTirro recognized that Account 6623 includes
12 costs for interexchange carrier billing and collection services.

13 **Q. DID MCI CORRECTLY CALCULATE THE AVOIDED COST FACTOR**
14 **FOR ACCOUNT 6621 CALL COMPLETION?**

15 A. No. The 100% avoided cost factor proposed by MCI was the same as the
16 FCC presumption. Because these costs are not included in the retail rate
17 for local exchange service, but rather in separate OS/DA tariffed rates, it
18 is not correct to include these costs as avoided. Mr. DiTirro also utilized
19 the same incorrect FCC presumption of 100% for Account 6622, Number
20 Services.

21 **Q. DID MCI CALCULATE ITS INDIRECT EXPENSE FACTOR**
22 **CONSISTENT WITH THE FCC?**

1 A. No. Like AT&T, MCI incorrectly calculated the indirect expense factor.
2 Although Mr. DiTirro indicates that the "avoided indirect costs are
3 calculated by determining the ratio of directly avoided costs to total costs"
4 (Exhibit T-____ (AJD Testimony) page 6 line 5), the 18.11% factor in
5 (Exhibit T-____ (AJD Testimony)), Appendix I is actually the ratio of
6 avoided expenses (both direct and indirect) to total expenses. This
7 incorrectly overstates the avoided cost and increases the avoided cost
8 discount. For the reasons discussed above with respect to AT&T, the
9 correct indirect expense factor should be calculated as the ratio of
10 avoided direct to total expenses.

11 **Q. HAVE YOU REVIEWED THE TESTIMONY OF PAULA M. STRAIN ON**
12 **BEHALF OF THE COMMISSION'S STAFF?**

13 A. Yes, I have.

14 **Q. COULD YOU PLEASE COMMENT ON MS. STRAIN'S PROPOSED**
15 **METHODOLOGY?**

16 A. Yes. Ms. Strain has presented an avoided cost methodology which
17 consists of reviewing the models filed earlier by parties to this proceeding
18 and recommending the following parameters:

- 19 - Embedded Data
- 20 - Intrastate Separated Results
- 21 - Indirect as the ratio of avoided direct to total direct
- 22 - discount as the ratio of avoided costs to retail revenues

- 1 - Separate Wholesale Discounts for Operator Services and
- 2 Directory Assistance
- 3 - Wholesale Costs should be Recognized in Developing
- 4 Discount

5 **Q. IS THE USE OF INTRASTATE SEPARATED RESULTS NECESSARY IN**
6 **DETERMINING THE AVOIDED COST DISCOUNT FACTOR TO APPLY**
7 **TO INTRASTATE SERVICES AVAILABLE FOR RESALE?**

8 A. No. It is unnecessary to use intrastate separated results. Applying the
9 avoided cost discount factor to unseparated results, results in virtually the
10 same discount.

11 **Q. IS THE 'SEPARATE WHOLESAL DISCOUNTS' APPROACH TO**
12 **AVOIDED COST DISCOUNTS NECESSARY IN REGARD TO**
13 **OPERATOR SERVICES AND DIRECTORY ASSISTANCE?**

14 A. No. The separate wholesale discounts approach is conceptually
15 unnecessary because when CLECs choose to not self-provision OS and
16 DA, their end-user generates the same switch and billing activity that
17 GTE's retail customers generate in today's environment.

18 **Q. DID MS. STRAIN CALCULATE AN INDIRECT EXPENSE FACTOR**
19 **CONSISTENTLY WITH THE FCC?**

20 A. No. Like AT&T, Ms. Strain proposes that the indirect expense factor be
21 calculated as a ratio of avoided direct expenses to total direct expenses.
22 For the reasons discussed above with respect to AT&T, the correct

1 indirect expense factor should be calculated as the ratio of avoided direct
2 to total expenses.

3 **Q. HAVE YOU REVIEWED THE TESTIMONY OF WILLIAM DUNKEL ON**
4 **BEHALF OF THE COMMISSION?**

5 A. Yes, I have.

6 **Q. COULD YOU PLEASE COMMENT ON MR. DUNKEL'S PROPOSED**
7 **AVOIDED COST DISCOUNT?**

8 A. Yes. Mr. Dunkel calculates a discount of 10.89% for GTE assuming that
9 a CLEC purchases GTE's Operator Services and Number Services, and
10 calculates a discount of 11.38% if the CLEC self-provisions these same
11 services.

12 **Q. DID MR. DUNKEL CALCULATE THE TWO AVOIDED COST**
13 **DISCOUNTS CORRECTLY?**

14 A. No. Mr. Dunkel proposes that the calculation consist of intrastate avoided
15 costs in the numerator and intrastate revenues in the denominator. This
16 is not correct because it appears to include revenues not subject to
17 resale. Mr. Dunkel used \$419.820 million in the denominator to produce
18 a discount of 10.89%.

19 **Q. HAS MR. DUNKEL CORRECTLY IDENTIFIED THE MARKETING**
20 **EXPENSE (ACCOUNT 661X) AND CUSTOMER SERVICE EXPENSE**
21 **(ACCOUNT 6623) THAT GTE WILL AVOID IN A RESALE**
22 **ENVIRONMENT USING ALL AVAILABLE DATA?**

1 A. No. In his direct testimony, Mr. Dunkel relies solely on a "presumption" of
2 90% avoided costs and does not present any proof to support this
3 assertion. The Product Management expense account is comprised of a
4 number of Product Management Workcenter accounts which will not be
5 avoided in a wholesale environment as discussed previously with respect
6 to AT&T's position. For the same reasons discussed previously, GTE's
7 study accurately identifies the costs that will be avoided and should be
8 used in setting the avoided cost discount.

9 **Q. HAS MR. DUNKEL INCORRECTLY IDENTIFIED OTHER EXPENSES**
10 **SUCH AS DEPRECIATION AND AMORTIZATION FOR GENERAL**
11 **SUPPORT ASSETS AND RETURN AND TAXES AS AVOIDABLE**
12 **COSTS.?**

13 A. Yes. Mr. Dunkel incorrectly identifies other expenses such as
14 depreciation and amortization for general support assets and return and
15 taxes as indirect avoidable costs. Mr. Dunkel, like Ms. Dodds,
16 erroneously assumes that all General Support assets and therefore the
17 resulting depreciation is related to direct expenses. This is not logical
18 because as the FCC indicated "indirect or shared costs, *such as general*
19 *overheads, support all of the LEC's functions.*" Order at ¶ 912 (emphasis
20 added).

21 **Q. WHAT ARE THE CONSEQUENCES OF AN OVERSTATED AVOIDED**
22 **COST DISCOUNT?**

1 A. If the avoided cost discount is overstated, competition will be impaired in
2 Washington. Resellers will reduce their cost for activities the reseller
3 need not duplicate thereby gaining a competitive advantage. Facilities-
4 based providers will not be incented to build facilities to compete with the
5 resellers or the areas where such an incentive remains will only be tightly
6 concentrated business districts. Similarly, GTE will not be inclined to
7 make additional investment in Washington or to offer new services as the
8 reseller will always have a price advantage for the exact same service.
9 An overstated discount also encourages inefficient competition.
10 Therefore, only with appropriately set avoided cost discounts, that is, a
11 discount based on actual GTE costs, will competition in Washington
12 flourish.

13 **Q. PLEASE SUMMARIZE GTE'S VIEW OF THE POSITIONS TAKEN BY**
14 **THE PARTIES IN THIS PROCEEDING.**

15 A. AT&T's proposed discount of 30.84% is artificially high and is not in any
16 way representative of the costs that reasonably can be avoided by GTE
17 when services are offered for resale. AT&T has made a fundamental
18 incorrect assumption that GTE will exit from its retail line of business.
19 AT&T has not performed the analysis necessary to determine GTE's
20 avoided cost, despite the GTE specific detail provided in the study and
21 through discovery. AT&T has used arbitrary assumptions in their study
22 which are not GTE specific, and has utilized the rules of the FCC order
23 only when it causes the avoided cost discount to increase. Therefore,

1 AT&T's study results are of no use to this Commission in setting resale
2 rates in this proceeding.

3 MCI's proposed discounts of 18.11% is also based on many of the
4 same flawed assumptions. While producing a lower proposed discount
5 than AT&T's proposal, MCI has still failed to accurately identify the costs
6 that GTE will avoid by using arbitrary judgements in identifying avoided
7 cost factors for direct expense accounts. Accordingly, MCI's proposal
8 should also be rejected by the Commission.

9 Mr. Dunkel's proposed discount of 10.89% does not comply with
10 the Act. It does not determine wholesale rates on the basis of the rates
11 for retail services available for resale and does not accurately identify the
12 costs that GTE will avoid.

13 GTE's proposed discount of 12.87% is based on the in-depth,
14 detailed analysis necessary to identify costs that will be avoided. GTE
15 analyzed every Workcenter in the Company when determining the costs
16 that will be avoided and determined the avoided costs on a Washington-
17 specific basis. GTE's analysis takes into account how GTE runs its
18 business including its current retail and wholesale offerings. This study
19 accurately reflects those costs that GTE will avoid in a resale environment
20 and should be adopted by this Commission.

21
22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

23 **A. Yes, it does.**