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1 BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION
2 COMMISSION

3 WASHINGTON UTILITIES AND)
TRANSPORTATION COMMISSION,) DOCKET NO. UT-950200
4)
Complainant,) VOLUME 23
5)
vs.) Pages 2540 - 2805
6)
U S WEST COMMUNICATIONS, INC.,)
7)
Respondent.)
8 -----)

9 A hearing in the above matter was held at
10 8:45 a.m. on January 17, 1996, at 1300 South Evergreen
11 Park Drive Southwest, Olympia, Washington
12 before Chairman SHARON L. NELSON, Commissioners
13 RICHARD HEMSTAD, WILLIAM R. GILLIS and Administrative
14 Law Judge C. ROBERT WALLIS.

15

16 The parties were present as follows:

17 U S WEST COMMUNICATIONS, by EDWARD SHAW and
18 DOUGLAS OWENS, and MOLLY HASTINGS, Attorneys at Law,
1600 Bell Plaza, Seattle, Washington 98191 and JAMES
19 VAN NOSTRAND, Attorney at Law, 411 - 108th Avenue
Northeast, Bellevue, Washington 98004.

20 WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION STAFF, by STEVEN W. SMITH and GREGORY
21 TRAUTMAN, Assistant Attorneys General, 1400 South
Evergreen Park Drive Southwest, Olympia, Washington
22 98504.

23 FOR THE PUBLIC, DONALD TROTTER and ROBERT
MANIFOLD, Assistant Attorneys General, 900 Fourth
24 Avenue, Suite 2000, Seattle, Washington 98164.

25 Cheryl Macdonald, Court Reporter

1 APPEARANCES (CONT.)

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9 TRACER, by ARTHUR A. BUTLER, Attorney at
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16 94404-2467.

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I N D E X

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WITNESSES:	D	C	RD	RC	EXAM
3 SIEVERS	2543	2545	2578	2580	2577
KARGOLL	2581	2583	2648	2649	2643
4 FARROW	2652	2660	2707		2704
EMMERSON		2714	2756		2743
5 COPELAND	2760	2780	2802	2803	2802

6

EXHIBITS:	MARKED	ADMITTED
7 475T, 476-479	2543	2544
8 480T	2581	2583
481T	2581	2583
9 482C	2581	2621
483	2581	2631
10 485C	2652	
486, 487	2652	2678
11 488C	2652	
362		2722
12 355T, 356T, 357, 358		2761

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1 P R O C E E D I N G S

2 JUDGE WALLIS: Let's be on the record,
3 please, for our Wednesday, January 17, 1996 session in
4 the matter of docket UT-950200, U S WEST
5 Communications. At this point Sprint has called Mark
6 Sievers to the stand.

7 Whereupon,

8 MARK SIEVERS,
9 having been first duly sworn, was called as a witness
10 herein and was examined and testified as follows:

11 JUDGE WALLIS: In conjunction with Mr.
12 Sievers's testimony the following documents have been
13 prefiled and are marked as indicated. The direct
14 testimony of Mark P. Sievers is designated Exhibit
15 475T for identification. Document designated MPS-2,
16 his resume, is 476 for identification. MPS-3 is 477
17 for identification. MPS-4 access subsidies is 478 for
18 identification, and MPS-5 is 479 for identification.

19 (Marked Exhibits 475T, 476, 477, 478 and
20 479.)

21 DIRECT EXAMINATION

22 BY MS. LEHTONEN:

23 Q. Good morning, Mr. Sievers.

24 A. Good morning.

25 Q. Could you please state your name and

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1 business address for the record?

2 A. My name is Mark Sievers. My business
3 address is 8140 Ward Parkway, Kansas City, Missouri.

4 Q. Did you cause testimony to be filed in this
5 proceeding identified as Exhibits 475T through 479?

6 A. Yes, I did.

7 Q. And are there any changes you wish to make
8 to this testimony at this time?

9 A. No, there are not.

10 Q. Is this testimony true and accurate to the
11 best of your knowledge?

12 A. Yes, it is.

13 Q. And do you now adopt this testimony for
14 this proceeding?

15 A. Yes, I do.

16 MS. LEHTONEN: The witness is available for
17 cross.

18 JUDGE WALLIS: Do you want to offer the
19 exhibits now?

20 MS. LEHTONEN: Yes. We would like to offer
21 those exhibits into the record.

22 JUDGE WALLIS: Is there any objection? Let
23 the record show that there is no objection, and the
24 exhibits are received.

25 (Admitted Exhibits 475T, 476 through 479.)

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CROSS-EXAMINATION

3 BY MS. HASTINGS:

4 Q. Morning, Mr. Sievers, my name is Molly
5 Hastings and I'm representing U S WEST.

6 A. Good morning.

7 Q. I would like to refer you to page 3 of your
8 direct testimony, and at line 8 you indicate that
9 substantial public benefits will be realized by U S
10 WEST moving its access charges closer to competitive
11 cost based levels. Is it your position in this docket
12 on behalf of Sprint that you are advocating pricing at
13 TS LRIC or at something close that approximates TS
14 LRIC?

15 A. I think that the practical recommendations
16 that we're making in this docket are summarized on
17 page 5, and also in section 3 of my testimony where we
18 talk about the recommended access policies. And what
19 Sprint is specifically recommending in this case are
20 four things that will move U S WEST's access charges
21 closer to a cost based competitive level, and that's
22 parity with the interstate access rates. There's no
23 reason that the same facilities, the same services
24 ought not to have the same price.

25 The second is eliminating the differential

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1 between terminating and originating access charges.
2 Again, the same kind of rationale applies that the
3 same services, the same facilities ought to have the
4 same price.

5 The third is to eliminate the carrier
6 common line charges. As U S WEST witnesses have
7 testified in this case, the interchange carriers are
8 not the cost causers for this particular rate element
9 and therefore it wouldn't be a rate element that one
10 would expect to persist in a competitive environment.

11 The fourth recommendation is to eliminate
12 the RIC. Again as your witnesses have testified
13 there's no cost basis for the residual interconnection
14 charge, therefore one wouldn't expect it to persist in
15 a competitive marketplace and it ought to be
16 eliminated. In my testimony I've offered TS LRIC as
17 the theoretical economic objective for setting
18 competitive access rates because I believe that TS
19 LRIC is where access charges would equilibrate in a
20 competitive marketplace.

21 Q. But I think my question was are you
22 recommending to this Commission that they set access
23 charges for U S WEST at TS LRIC?

24 A. I think that would be desirable, yes.

25 Q. Rather than moving them closer to TS LRIC,

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1 as your testimony seems to imply?

2 A. I think if you could set it there that
3 would be great, but as an interim step towards moving
4 towards those cost based competitive rates you could
5 take the four steps that I've identified and
6 unambiguously move U S WEST's access charges closer to
7 a competitive cost based rate, and I think that TS
8 LRIC would be that competitive cost based rate. If
9 you want to go there by directly by setting rates at
10 TS LRIC that's great but if the Commission wishes to
11 take steps to move toward that competitive rate those
12 are the four steps I would recommend.

13 Q. Is Sprint recommending to the
14 Commission that it set access charges at TS LRIC?

15 A. Yes.

16 Q. Mr. Sievers, can you tell me how Sprint
17 prices its interstate interLATA MTS type services? Is
18 it at TS LRIC?

19 A. We don't do cost studies in the same sense
20 that U S WEST does cost studies. When you say how
21 does Sprint set its long distance rates, understand
22 that in a competitive environment a firm like Sprint
23 or AT&T or MCI manages several thousand rates. I
24 think the estimate for Sprint is that we have roughly
25 20,000 long distance rates that we set, so it's

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1 economically and it's infeasible to do cost studies for
2 all of those rates in the competitive environment.

3 Q. How many rate elements do you think U S
4 WEST has? Do you have an opinion?

5 A. I think it's far less than 20,000.

6 Q. And so I'm not sure if I got an answer to
7 my question. Sprint does not use TS LRIC cost
8 studies; is that correct?

9 A. No. We function in a competitive
10 environment and so the primary driver for setting our
11 prices is the marketplace.

12 Q. And so --

13 A. Certainly we will look at what our costs
14 are but in a very crude kind of sense. We will look
15 at what our access expenses are and make sure that the
16 prices we're charging are going to at least recover
17 our access charges but because we function in a
18 competitive environment it were Sprint has to look at
19 what our competitors are charging for the service and
20 use that as a guide.

21 Q. And in that competitive environment it's
22 correct, isn't it, that Sprint prices its services to
23 cover those costs that you just described plus some
24 margin that's sustainable in that competitive
25 environment; isn't that correct?

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1 A. Yes, if there is a margin to be had. I
2 mean there may be instances where we're forced to
3 match our competitors' prices even though there might
4 be not be a margin for that particular rate element.

5 Q. Are you familiar with the Sprint's
6 responses to U S WEST's data requests regarding how it
7 prices its services?

8 A. Yes.

9 Q. And isn't it correct that Sprint did
10 respond to a question regarding how -- what its
11 economic price floors that Sprint prices its
12 intrastate intraLATA services in Washington based on
13 the underlying access cost plus the marginal
14 sustainable in the competitive long distance market?

15 A. Yes, and I think that's consistent with how
16 I've answered today.

17 Q. I would like to refer you now to page --
18 also page 3 of your testimony and let's look at one of
19 your exhibits. You indicate that by reducing the
20 access charges -- this is at the bottom of page 3 on 19
21 to 21 -- that by reducing the access charges to
22 competitive levels in Washington that would be worth
23 approximately \$606 million annually to the ratepayers
24 in Washington; is that correct or end users customers
25 in Washington. Do I understand correctly?

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1 A. That is correct. And that 600 million is
2 composed of two separate types of benefits, if you
3 will. One is that when long distance charges come
4 down or the price of any service is reduced consumers
5 benefit because they pay less for the services and the
6 volumes they currently consume. The second economic
7 benefit is that a lower price stimulates usage of a
8 service and consumers realize a benefit on the new
9 volumes that they consume, and basically the 600
10 million is about 353 million in benefits for the
11 reductions on existing services, and 253 million for
12 the value of new or stimulated services.

13 Q. If I understand your \$606 million correctly,
14 looking at your Exhibit MPS-3 which has been marked
15 here as Exhibit 477, you arrived at that 606 million
16 benefit by assuming, if I'm correct, the most
17 optimistic assumption which is that there would be a
18 flow through of 100 percent of access reductions to
19 toll prices; is that correct?

20 A. That is correct.

21 Q. And if you assumed that, for instance,
22 Sprint would only pass through 65 percent of the
23 access reductions what would that dollar amount be,
24 that \$606 million become?

25 A. I think I've included those in the exhibit.

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1 Let me look it up. But I think a 100 percent flow
2 through is not an unreasonable assumption given that
3 nationally access charges have dropped by about five
4 cents a minute since 1988 but long distance prices
5 have fallen by seven cents so there's been at least a
6 100 percent flow through of access charges nationally,
7 so I don't think that 100 percent is completely out of
8 line, but to answer your question, the number for
9 Washington is \$502 million assuming a 65 percent flow
10 through and assuming the pessimistic -- the other
11 pessimistic assumptions that go into that.

12 Q. Now, the 100 percent, the 606 million, by
13 that testimony is Sprint committing to this Commission
14 that it will flow through the access reductions 100
15 percent?

16 A. I think that the competitive marketplace
17 will force us to do so.

18 Q. I'm asking are you making that commitment
19 to this Commission in your testimony?

20 A. No, I'm not.

21 Q. On page 4 of your testimony you sort of
22 have -- I think your theory is correct that all things
23 being equal that if our rivals are equally efficient
24 that their profits should be equal. Have you provided
25 any evidence in this docket that U S WEST rivals --

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1 and you're referring to them in lines 15 and 16 -- are
2 as equally efficient as U S WEST?

3 A. No, and that's not the point I'm making by
4 making that statement.

5 Q. Thank you. But you produced no evidence
6 that they're equally efficient?

7 A. No.

8 Q. That's fine, thank you. And then I would
9 like to refer you to your Exhibit MPS-5 which has been
10 marked as Exhibit 479. Now, on the bottom of page 4
11 there on your testimony you indicate that this
12 particular document is a good example. It shows that
13 the traditional imputation test like the one proposed
14 by U S WEST are inadequate to prevent an anti-
15 competitive potential from occurring in the
16 marketplace. Could you help me find where in this
17 document you've analyzed U S WEST or any U S WEST
18 specific data in Washington?

19 A. In MPS-5?

20 Q. Yes.

21 A. There is no Washington specific data in
22 MPS-5. It's offered strictly as a numerical
23 illustration to illustrate the mechanics of how a
24 price squeeze could occur if subsidies or substantial
25 contribution are maintained in access services which

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1 are an essential input to long distance competitors.

2 So MPS-5 has no Washington specific data, did I

3 understand that correctly?

4 A. That's correct. It is strictly a numerical
5 example to illustrate how the phenomenon works.

6 Q. Does it have any U S WEST specific data in
7 it, be it Washington or any other state?

8 A. No, it doesn't but I don't believe that
9 detracts from its value as a numerical illustration to
10 illustrate the mechanics of the phenomenon.

11 Q. Let me direct you to page 2 of that
12 exhibit. Now, you've run your calculations, as I
13 understand it, based on Southwestern Bell. Do you
14 know, for instance, what U S WEST's toll revenues are
15 that would equate to the 22.54 cents you have for
16 Southwestern Bell in your example here?

17 A. No, I do not.

18 Q. Do you know what U S WEST's costs are that
19 equate to the 7.56?

20 A. No.

21 Q. So have you taken a look at U S WEST
22 revenues and costs and determined whether or not in
23 fact a price squeeze might exist as it relates to U S
24 WEST in Washington?

25 A. No. The point of the exhibit is to

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1 illustrate that if access charges, which are an
2 essential input for long distance competitors are
3 maintained in a competitive marketplace the providers
4 of that essential service can use that contribution to
5 obtain a competitive advantage and drive equally
6 efficient rivals out of the marketplace.

7 Q. But you've looked at no U S WEST specific
8 data and no U S WEST Washington specific data to
9 conclude or put any evidence on the record that in
10 fact that occurs in Washington; isn't that correct.

11 MS. LEHTONEN: Objection, asked and
12 answered.

13 JUDGE WALLIS: I do believe that that has
14 been asked and answered several times.

15 Q. Referring you to page 5 of your testimony,
16 you indicate at about line 6 that there are other
17 benefits of reduced access charges, that reduced
18 charges will lead to the need to develop better
19 information highways and the development of a super
20 highway. Have you provided or produced any evidence
21 in this record to support that statement?

22 A. Yes.

23 Q. And that is?

24 A. I think that we answered some data requests
25 as to how consumers access the information super

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1 highway, how they access the Internet, and that's
2 largely through dial up services or long distance
3 services directly. Dial up services of course go
4 through a packet data network that's typically
5 provided by a long distance carrier, and so to the
6 extent that access charges and access costs are
7 reduced, the costs of providing access to remote
8 databases is reduced for consumers, and consumers then
9 -- their usage of the information super highway would
10 be stimulated.

11 Q. Yes, and I understand you to say you have
12 responded to some data requests. Have you provided
13 any evidence for the record?

14 A. I just did through my testimony. Is that
15 not data and evidence for the record?

16 Q. Facts, any specific facts that would
17 support your statements?

18 A. Sprint, for example, is a provider of a
19 packet data network, public packet data network. When
20 people subscribe to America On Line for example
21 typically they access America On Line and the remote
22 databases that are contained in that by dialing the
23 Sprint packet data network.

24 Q. But you've conducted no studies or provided
25 them in this record; is that correct?

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1 A. No.

2 Q. And then referring you on page 7 of your
3 testimony at lines 4 and 5 you indicate that even
4 though its witnesses -- referring to U S WEST --
5 explicitly acknowledge that U S WEST access charges in
6 Washington contain substantial levels of embedded
7 contribution or subsidies, could you direct me to
8 where in the testimony of U S WEST witnesses that U S
9 WEST has explicitly acknowledged that U S WEST access
10 charges contain substantial levels of subsidies?

11 A. I think throughout her testimony Barbara
12 Wilcox indicated that access charges are priced
13 substantially above costs and I think she's labeled it
14 as contribution. Whether you label it as contribution
15 or subsidies I think is a matter of semantics.

16 Q. So you're using the word contribution and
17 subsidy interchangeably?

18 A. Yes.

19 Q. So that -- I don't want to be redundant but
20 for the purposes of the record where you indicate that
21 contribution or subsidy, I can insert the word where I
22 see subsidy contribution in each instance.

23 MS. LEHTONEN: I believe that is redundant.
24 Objection.

25 Q. Let me refer you then to your study, which

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1 is marked -- it's your MPS-4 which would be Exhibit
2 478, and I would like to refer you to page 2 of that
3 where you answer the question what is a subsidy, and
4 you indicate both at the bottom of page 2 and the top
5 of page 3 there that in a sense a subsidy is an above
6 cost charge that would not otherwise be included in a
7 competitive market. And I guess my question is, does
8 your use of the word subsidy here and how you've
9 defined it conform with the way other witnesses in
10 this proceeding are using the word contribution?

11 A. I don't know how other witnesses are using
12 the phrase contribution.

13 Q. At page 9 of your testimony at about lines
14 12 or so you indicate that said another way a firm
15 would willingly produce a new product as long as its
16 revenues were greater than any additional costs where
17 you were talking about incremental costs. Would your
18 opinion change if a company didn't have the option to
19 choose to provide a particular product or service but
20 was obligated by law to do that?

21 A. The example in my testimony talks about a
22 firm entering the market, a competitor making a
23 decision to enter a market only if its anticipated
24 revenues exceed the incremental costs of entering that
25 particular market. So your question, as I understood

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1 it, was would that analogy be correct if the firm were
2 ordered to provide the service, and I think that if
3 the firm were ordered to provide the service it
4 wouldn't be making this economic choice so I don't
5 think it makes sense to talk about this.

6 Q. My question was would your opinion change
7 if the company didn't choose to enter the market but
8 was obligated to do it, and I think you said your
9 answer is yes you would not have the same opinion?

10 A. That's correct, because the analogy would
11 not apply.

12 Q. Thank you. On page 11 of your testimony at
13 the bottom of the page you indicate because of the
14 structure the CCL does not match the structure of the
15 costs that U S WEST reaps a competitively unearned
16 economic windfall when its CCL revenues exceed its NTS
17 loop costs. Have you produced any evidence on this
18 record that U S WEST has reaped a completely unearned
19 economic windfall as a result of the pricing of its
20 services?

21 A. I think that because carrier common line
22 revenues are minute driven and NTS costs are line
23 driven, in other words, as people subscribe to service
24 NTS costs increase but as people's volumes for long
25 distance increase carrier common line revenues

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1 increase, to the extent that those two revenue streams
2 have been mismatched over time that's an uneconomic
3 windfall that U S WEST has earned since the
4 establishment of carrier common line charges. In other
5 words, NTS costs that carrier common line charges are
6 theoretically declined to recover because those have
7 grown by say 3 percent a year as people subscribe to
8 telephone service, to the extent that those are
9 mismatched with how long distance traffic and access
10 traffic has grown, which is 17 percent a year, that
11 differential is a windfall that U S WEST has earned,
12 and I think that it's true nationally that access
13 traffic has grown faster than the rate of growth of
14 subscriber lines. Now, I don't know what the figure is
15 for Washington specifically, but I would be very
16 surprised if the growth in access lines was not
17 substantially smaller than the growth in access
18 traffic.

19 Q. But you don't have any actual knowledge of
20 that, is that correct, and you've provided no evidence
21 of that fact; is that correct?

22 A. I have for the nation as a whole but not
23 for Washington.

24 Q. And actually to get back to my question, my
25 question was have you provided any evidence in this

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1 proceeding to indicate that U S WEST has reaped a
2 competitively -- a completely unearned economic
3 windfall because of the way it prices its services?

4 A. I guess I'm confused as to what you mean by
5 evidence, because the question that this is responding
6 to asks why are cost-based rates and rate structures
7 important for access structures or access services.

8 Q. U S WEST is operating under a rate of
9 return regulation, an alternative form of regulation
10 plan, actually not even any longer in this state, so
11 it's regulated by rate of return regulation?

12 A. I will accept that, yes.

13 Q. And have you looked at what U S WEST has
14 earned in the last six months, the last year?

15 A. No, I have not.

16 Q. So you don't know for a fact whether or not
17 the way U S WEST is pricing its products and services
18 provides U S WEST a completely unearned economic
19 windfall; is that correct?

20 A. No, that's not correct because I believe as
21 long as there's a mismatch between the way NTS costs
22 are incurred and the way carrier common line revenues
23 are earned that that differential will be unearned
24 windfall because the revenue stream doesn't match the
25 cost stream.

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1 Q. And you have produced evidence in this
2 proceeding to show that U S WEST has earned -- has
3 completely earned -- earned an uneconomic windfall; is
4 that correct?

5 MS. LEHTONEN: Objection, asked and
6 answered.

7 MS. HASTINGS: I don't think he's answered
8 my question.

9 JUDGE WALLIS: The witness may respond.

10 A. I'm really not sure how to answer your
11 question other than the response I've given.

12 Q. Well, I think a yes or no would work. Have
13 you produced any evidence to substantiate your
14 statement is my question.

15 A. Yes.

16 Q. Thank you. On page 15 of your testimony
17 you indicate based on your analysis of the market that
18 an additional 21,000 households would be ascended to
19 subscribe to the telephone network. What percent of
20 those households would be U S WEST customers?

21 A. I don't know.

22 Q. And then on page 17 of your testimony at
23 about lines 13 to 15 you talk about in fact -- and am
24 I correct in assuming that these are national numbers
25 and none of these numbers are specific to the state of

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1 Washington or specific to U S WEST alone?

2 A. That's correct.

3 Q. So the \$20 billion annually is not a U S
4 WEST number or --

5 A. It is a national number.

6 Q. And during that time period it says there
7 that in fact long distance reductions have reduced
8 long distance expenditures in excess of 20 billion
9 annually, and looking at your footnote down there
10 actually the footnote is at the bottom of the next
11 page, you talk about how that figure is the figure --
12 is the difference between what consumers actually paid
13 in 1994, et cetera versus what they would have paid
14 in '88, et cetera. Do you see your footnote?

15 A. Yes, I do.

16 Q. Now, my question is during the same time
17 period and using the same assumptions that you used,
18 what was the total reduction in access charges?

19 A. I don't know off the top of my head but the
20 way I would have calculated it in the paper is five
21 cents a minute times an estimate of the total number
22 of minutes, and that would be the change in access
23 over that period. But in the paper itself I actually
24 produced an estimate of the change in prices that were
25 due to access reductions, and depending on the

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1 methodology one uses it's somewhere between 24 and 33
2 percent of the change in long distance prices is due
3 to access reductions.

4 Q. And do all --

5 A. And again, in the previous footnote, when I
6 talk about access reductions it's total access
7 expenses of long distance carriers, and access
8 expenses, the change in access expenses is driven by
9 three things. One is the change in access rates which
10 are controlled by local telephone companies. The
11 second is a change in long distance products so if a
12 company starts to provide more special access products
13 their access expenses could be reduced.

14 The third is the configuration of a long
15 distance carrier's network. If Sprint location its
16 facilities closer to the facilities of U S WEST it can
17 reduce its transport expenses. The latter two items
18 are things that are driven by the competitive
19 marketplace and are controlled by long distance
20 carriers. It's only first item, the change in access
21 rates, that's controlled by local carriers, and that's
22 a small portion of the total change in access expenses
23 over this time period.

24 Q. I'm not sure you answered my question. My
25 question was whether or not during the same time

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1 period and using the same assumptions that you have in
2 your footnote whether the total reduction access
3 charges was greater or larger, that number, and I
4 think you said you didn't know?

5 A. No. I said it was smaller. I said that
6 the change in price over this time period due to
7 access reductions was at most between 24 and 33
8 percent.

9 Q. And then on page 19 of your testimony at
10 lines about 14 or 15, is it your testimony that U S
11 WEST residence exchange services in Washington are
12 below cost?

13 A. I don't know whether they're below cost.

14 Q. Then can you help me understand your
15 testimony there on page 14 where you say Washington
16 college students calling long distance in Washington
17 are paying inflated long distance rates to support the
18 below cost local phone service for Bill Gates. Is it
19 your testimony that Mr. Gates is paying below cost for
20 his telephone service?

21 A. I think that the standard assumption that's
22 often made in the telecommunications industry is that
23 local residential telephone service is a service
24 that's subsidized by the contributions or subsidies,
25 whatever adjective that you want to use, that are

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1 provided by other services like access services or
2 toll services and that if one reduces access charges
3 the inevitable result is that local residential
4 telephone service will have to be increased and
5 therefore universal service will be threatened.

6 Now, I don't know whether U S WEST's local
7 telephone service is actually provided below cost but
8 that's the story, that's the rationale that's
9 typically offered for not reducing access charges is
10 that if we reduce access charges we're going to have
11 to raise local rates to make up the difference. Now,
12 I think that there's several reasons why that may not
13 be the case. In a competitive environment I think
14 that competition doesn't necessarily threaten
15 universal service especially if you were to introduce
16 competition to local markets. Competition would
17 provide an incentive for firms to reduce local
18 telephone rates not to raise local rates.

19 Secondly I think that competition in the
20 long distance industry has shown that the incumbents
21 aren't necessarily harmed by competition. AT&T, for
22 example, has reduced its long distance prices
23 somewhere between 40 and 60 percent since divestiture
24 but yet today its revenues and earnings are higher
25 than they were prior to divestiture and that's because

02566

1 AT&T is fundamentally a different company. It's
2 reduced its expenses. It's become more efficient.
3 It's learned to compete. I would expect the same
4 thing would be true of U S WEST in a competitive
5 environment.

6 Q. I'm not sure I got an answer to my
7 question. My question was whether or not it was your
8 testimony that U S WEST residential exchange service
9 is below cost and I think that you said that you don't
10 know; is that correct?

11 A. That's correct.

12 Q. So the example that you've given here is
13 just speculation on your part; is that correct?

14 A. I think it responds to a common perception
15 in the telecommunications industry.

16 Q. But you don't have any actual fact to
17 support this example?

18 A. I don't know whether U S WEST local
19 telephone service is currently provided below cost nor
20 do I know what U S WEST costs would be in a
21 competitive environment.

22 Q. On bottom of page 26 and top of page 27 you
23 talk a little bit Sprint's affiliation with its local
24 exchange companies. Does Sprint buy access from the
25 local exchange access with whom it's affiliated?

02567

1 A. Yes.

2 Q. And are those rates for access services, do
3 they include a significant contribution?

4 A. It varies by the company. Certainly the
5 access charges are high in some of the rural
6 exchanges, the rural companies that are served by
7 Sprint's local telephone companies but in other areas
8 like Las Vegas for example, access charges are about a
9 penny a minute so they're very low there.

10 Q. If you know isn't it true that the access
11 rates for Sprint's local exchange companies are
12 generally much higher than U S WEST's access rates?

13 A. It depends on the company. If we were to
14 look at the Las Vegas operation it would be
15 substantially lower than U S WEST's.

16 Q. But I guess that's not really helpful for
17 me to know what's going on in Las Vegas. Do you know
18 in Washington whether that's true?

19 A. I don't know in Washington.

20 Q. You don't have that information.

21 A. But I think our exchanges in Washington are
22 predominantly rural isolated exchanges whereas the Las
23 Vegas exchange is a metropolitan exchange. It's
24 probably more comparable to, say, Seattle or the
25 metropolitan areas that are served by U S WEST here.

02568

1 Q. Do you know whether or not competition
2 exists for those access rates in those rural areas
3 that you just described?

4 A. No, it does not.

5 Q. I would like to ask you a couple of
6 questions about your exhibit, it's MPS-2 and I think
7 it is marked as Exhibit 476, and I would like to refer
8 you to -- it's not your resume. It's the next one,
9 the MPS-3, I'm sorry, and that's marked as 477. Like
10 to refer you to page 2 of that. Down there under the
11 bold headline "Impacts of Access Charge Changes on
12 Toll Prices," you make a statement there that
13 interexchange carriers' interLATA and intraLATA
14 pricing volumes are affected by access competition
15 according to how it affected the access charges paid
16 by XCs, and then in contrast the local exchange
17 carrier's toll prices which are predominantly short
18 haul intraLATA services are not directly affected by
19 access charges and you parenthetically note that that
20 the LECs do not pay access charges to another carrier.
21 Are you making this statement about the way U S WEST
22 operates in the state of Washington?

23 A. I assume that if U S WEST originates and
24 terminates an intraLATA long distance call within its
25 on network, if it originates in a U S WEST exchange

02569

1 and terminates in a U S WEST exchange it's not writing
2 a check for access charges for the origination or
3 termination of that call. Similarly, in a call
4 originates in a U S WEST exchange but terminates in a
5 GTE exchange and it's intraLATA in nature, U S WEST
6 does not write a check for the origination for the
7 originating access charges. It might pay access
8 charges to GTE but I don't know what arrangements it
9 has made in the state of Washington.

10 Q. So your answer to my question is you do not
11 know whether the statement here, the assumptions you
12 laid out are specific to the state of Washington and
13 how U S WEST operates in the state of Washington?

14 A. Well, unless you're representing to me that
15 U S WEST actually writes a check for access charges
16 for toll services that originate in its exchanges or
17 originate and terminate in exchanges, I think it is
18 accurate for Washington.

19 Q. So I testify I'm not going to represent
20 anything to you. I'm asking do you know whether or
21 not this statement --

22 MS. LEHTONEN: Objection, it's asked and
23 answered.

24 MS. HASTINGS: I don't think he's answered
25 my question.

02570

1 MS. LEHTONEN: I think it's been answered
2 quite completely.

3 MS. HASTINGS: I don't think he's answered
4 my question. I think I asked him if this statement
5 reflects the way U S WEST operates in the state of
6 Washington and I think he answered by saying if that's
7 what I'm representing to him that's how it is he would
8 agree with me.

9 JUDGE WALLIS: I believe he answered that
10 he does not know; is that correct?

11 THE WITNESS: That's correct.

12 Q. And it seems that this statement also sort
13 of ignores the fact that this Commission has some
14 imputation tests. Are you familiar with the
15 Commission's imputation orders in this state, this
16 jurisdiction?

17 A. No, I'm not.

18 Q. So you have not, for instance, read the
19 Commission's order in docket U-87-1083-T?

20 A. No.

21 Q. You have not read the Commission's order in
22 docket U-88-2052-T?

23 A. No, I have not.

24 Q. Do you support -- does Sprint support a
25 flat-rated CCL?

02571

1 A. We have not really seen one so it's hard
2 for me to unequivocally say that we do support or not
3 support a flat rate CCL because I don't know what the
4 rate would be. For example, if the CCL were
5 established at a rate of 200 million a year I would
6 say that we're probably not going to support that.

7 Q. Do you know whether Sprint supports the FCC
8 filing on sent us block groups?

9 A. I don't think there has been an FCC notice,
10 a proceeded rulemaking, a census blocks. Sprint was a
11 participant with U S WEST in filing the sent us block
12 model in response to the universal service docket, so
13 in that sense we did support the use of census block
14 groups as a way of calculating the costs of providing
15 local service or the local loop on a census block
16 basis.

17 Q. And I just have one last question, Mr.
18 Sievers. Would Sprint support a CCL that is tied to
19 growth in access lines rather than growth in minutes
20 of use?

21 A. Yes. We have in other states.

22 MS. HASTINGS: Thank you.

23 JUDGE WALLIS: Public counsel?

24

25

CROSS-EXAMINATION

02572

1 BY MR. MANIFOLD:

2 Q. Good morning, Mr. Sievers, my name is Rob
3 Manifold. I'm an assistant attorney general. I'm
4 representing the public counsel which represents the
5 people of the state in this proceeding.

6 A. Good morning.

7 Q. In response to some of your questions to
8 Ms. Hastings, I want to ask you some follow-up. Do I
9 take it that in your opinion any charge above
10 incremental cost or L S -- total service LRIC would be
11 a subsidy in your view?

12 A. Yes, because I believe that in a
13 competitive environment prices would equilibrate at
14 the TS LRIC level. That's the cost level that a new
15 competitor, somebody who is entering the market, who
16 use in determining whether or not it makes sense to
17 enter that market, and to the extent that prices are
18 maintained above that competitive level then yes it
19 provides a subsidy or contribution.

20 Q. Do you recognize the existence of joint
21 costs in the provision of telephone service?

22 A. Certainly.

23 Q. And would you as an economist exclude joint
24 costs from the calculation of incremental costs?

25 A. Yes.

02573

1 Q. For a firm that's regulated you recognize
2 that the firm would nevertheless assert that it has a
3 right to recover its joint costs someplace?

4 A. That's correct.

5 Q. And you're not recommending that those
6 joint costs be entirely written off and borne by the
7 shareholders of the company?

8 A. No, but I think the question you're getting
9 at, and it's --

10 Q. Well, let me ask the questions if you
11 would, please. And I promise not to give the answers.
12 Do I understand that Sprint is in alliance with
13 several cable television companies and may be
14 providing direct access to customers at some point?

15 A. Yes. We're very interested in
16 participating in the local telecommunications market
17 and being a competitive provider of local telephone
18 service.

19 Q. Do you anticipate that Sprint would be
20 constructing facilities to end users' residences in
21 areas around the United States?

22 A. Yes.

23 Q. Let us assume then that it has done so in
24 Indiana, and U S WEST doesn't currently provide any
25 service in Indiana, does it?

02574

1 A. That is correct.

2 Q. There are proposals afoot that would allow
3 U S WEST to provide long distance service to my cousin
4 in Indiana, aren't there?

5 A. Yes. There's legislation pending before
6 the U.S. Congress that would create a mechanism that
7 would allow U S WEST to provide interLATA and
8 interstate long distance service.

9 Q. If Sprint built a local facility to get to
10 my cousin in Indiana and paid for that, maintained the
11 wires, and U S WEST became eligible to provide
12 interstate long distance service and came to Sprint
13 and said we would like to complete a call over your
14 local network that reaches my cousin in Indiana and
15 you've already paid for that network and we're just
16 going to use it and we're not going to impose any
17 additional costs on you for using it so will you let
18 us use it for your marginal costs, which is in this
19 instance zero, do you expect Sprint will accede to
20 that proposal?

21 A. I don't think it's accurate. I think that
22 there are some costs that will be imposed by virtue of
23 U S WEST interconnecting with Sprint's local network
24 in Indiana and Sprint would expect to recover those
25 costs from U S WEST.

02575

1 Q. And would those be only the incremental
2 costs caused by Sprint interconnecting?

3 A. I think if the access market were a
4 competitive market chilled expect it to be, given in
5 this hypothetical future world where Sprint enters the
6 local telephone market that that would be the rate at
7 which that market would equilibrate.

8 Q. And so your representation would be that
9 Sprint would then provide that service to U S WEST at
10 Sprint's incremental cost which would exclude any
11 joint costs?

12 A. Yes.

13 Q. And would exclude any common costs?

14 A. Yes.

15 Q. My cousin would be very happy, by the way
16 assuming the prices were reflected in the charges to
17 my cousin.

18 A. I thought you weren't going to testify.

19 Q. Fair comment. Well, isn't it true that my
20 cousin would be very happy?

21 In your direct testimony at pages 3 and 4
22 you present some calculations on the claimed savings
23 to Washington consumers from reductions in access
24 charges, and that would be flowed through
25 theoretically and reductions in toll rates; is that

02576

1 correct?

2 A. That's correct.

3 Q. In those calculations did you assume that
4 all other charges to consumers -- telephone charges
5 would remain the same?

6 A. Yes. I didn't perform a calculation that
7 talked about the impact on local telephone rates
8 because I don't know what that linkage is between
9 access charges and local telephone rates.

10 Q. And you understand that the proposal made
11 by U S WEST in this proceeding does make a linkage
12 there?

13 A. Yes, and it's not particularly, in my mind,
14 as I've testified in my prefiled testimony, the
15 linkage is a little bit strange because they're asking
16 for, as I understand it, a \$200 million local rate
17 increase to offset an access charge change that's in
18 the neighborhood of 15 or 20 million.

19 Q. Thank you.

20 MR. MANIFOLD: No other questions.

21 JUDGE WALLIS: Are there other questions
22 from counsel? Questions from the commissioners.

23 CHAIRMAN NELSON: No.

24 COMMISSIONER HEMSTAD: No.

25 JUDGE WALLIS: Commissioner Gillis.

1

2

EXAMINATION

3 BY COMMISSIONER GILLIS:

4 Q. As it still happens I also have a cousin in
5 Indiana. Just a follow-up to Mr. Manifold's
6 questions. Where would you suggest then recovering
7 your joint costs if not in access fees?

8 A. I guess I'm not convinced that the recovery
9 of joint and common costs is as pressing an economic
10 problem as it has been made out to be. Sprint long
11 distance and AT&T and MCI and all of the competitors in
12 the long distance business have joint and common costs
13 and we recover them in the competitive marketplace in
14 the natural course of things, so I'm not convinced that
15 if access charges were set at or near competitive
16 levels that there would necessarily be a huge shortfall
17 in common costs that would need to be recovered,
18 because I don't know what U S WEST's cost structure
19 would look like in a competitive environment.

20 Certainly AT&T, for example, their cost
21 structure has changed dramatically since divestiture.
22 They're a much more efficient competitive company, and
23 I would expect the same phenomenon to occur with U S
24 WEST, so it's not clear to me that there would be a
25 huge shortfall to be made up in a competitive

02578

1 environment for U S WEST.

2 Q. Let me say, are you saying that all
3 services can be priced at the -- tend towards TS LRIC?

4 A. I think that's an economic if he nonnonthat
5 would occur in a competitive environment. I think
6 that new entrants, if you open the door to competition
7 new entrants are going to be evaluating the
8 marketplace based on whether or not they can recover
9 their incremental cost. They're going to be looking
10 at the market, if you're a cable company, for example,
11 in deciding whether or not to provide local service
12 based on whether or not you think that the market rate
13 would be sufficient to cover your incremental costs.
14 So I think that as a natural consequence competitive
15 markets prices will equilibrate at some sort of
16 long-run incremental cost level.

17 Q. Can a firm survive in the long run if all
18 services were to go to equilibrate at TS LRIC?

19 A. I think they can.

20 COMMISSIONER GILLIS: Thank you.

21 JUDGE WALLIS: Ms. Lehtonen.

22 MS. LEHTONEN: Couple of questions.

23

24 REDIRECT EXAMINATION

25 BY MS. LEHTONEN:

02579

1 Q. Mr. Sievers, are you aware in general of
2 whether access has grown or declined on a national
3 basis over the past five years?

4 A. Access charges, the rate?

5 Q. Access lines.

6 A. Access lines have grown nationally.

7 Q. And would you expect that to be true in the
8 next five years?

9 A. Yes, certainly.

10 Q. What do you base that expectation on?

11 A. People have babies and the population
12 grows. It's also a function of the marketplace. As
13 new services are offered that stimulates demand. As
14 competition is introduced into the marketplace and
15 firms start advertising their services and talking
16 about the new services they offer that also stimulates
17 demand so I think that access lines or local telephone
18 service is going to be stimulated by population growth
19 and by competition.

20 Q. Do you have any information on the growth
21 in access minutes?

22 A. The growth in access minutes has been
23 substantially larger than the growth in access lines
24 nationally.

25 Q. And would you expect that to be any

02580

1 different for the state of Washington?

2 A. No, it would not.

3 MS. LEHTONEN: That's all I have.

4 JUDGE WALLIS: Any follow-up questions?

5 MS. HASTINGS: Follow-up question from a
6 question from Commissioner Gillis.

7

8 RE CROSS-EXAMINATION

9 BY MS. HASTINGS:

10 Q. Mr. Sievers, is U S WEST in Washington
11 classified as an effectively competitive company?

12 A. I don't know how you're classified in the
13 state of Washington.

14 MS. HASTINGS: Thank you.

15 JUDGE WALLIS: Is there anything further?

16 It appears that there's not. Mr. Sievers, thank you
17 for being with us today. You're excused from the
18 stand at this time. Let's be off the record while the
19 next witness takes the stand.

20 (Recess.)

21 JUDGE WALLIS: Let's be back on the record,
22 please. AT&T has called Robert E. Kargoll to the
23 stand.

24 Whereupon,

25 ROBERT KARGOLL, PhD,

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1 having been first duly sworn, was called as a witness
2 herein and was examined and testified as follows:

3 JUDGE WALLIS: In conjunction with Mr.
4 Kargoll's appearance some documents have been
5 distributed. These include his direct testimony which
6 is marked as 480T for identification, his rebuttal
7 testimony which is marked as 481T for identification,
8 and document distributed today by public counsel
9 include the response to data requests 43 consisting of
10 one page marked as 482C for identification, and the
11 response to data request 11 consisting of two pages
12 marked as 483 for identification.

13 (Marked Exhibits 480T, 481T, 482C, 483.)

14

15 DIRECT EXAMINATION

16 BY MS. PROCTOR:

17 Q. Would you please state your name and
18 address for the record.

19 A. My name is Robert Kargoll, K A R G O L L.
20 Business address is 795 Folsom Street, San Francisco,
21 California 94107.

22 Q. And did you prepare and cause to be filed
23 in this proceeding the direct testimony that has been
24 marked as Exhibit 480T and the rebuttal testimony
25 marked as 481T?

02582

1 A. Yes, I did.

2 MS. PROCTOR: Your Honor, I have to
3 apologize. Mr. Kargoll is going to answer yes to the
4 question do you have any corrections to that testimony,
5 and there's just one change.

6 Q. If you could please give that for us.

7 A. Yes, certainly. It occurs in both my
8 direct testimony marked as 480 as well as my rebuttal
9 marked 481. In my direct testimony it occurs on page
10 24, line 9. The margin between wholesale and retail
11 rates that AT&T is advocating should be 33 percent and
12 not the 35 percent listed there twice on line 9. This
13 correction should also be made to page 9 of my
14 rebuttal testimony. I believe that's on line 13.

15 Q. Is that the extent of your corrections?

16 A. Yes, it is.

17 Q. And with that correction, is this
18 testimony, Exhibits 480T and 481T true and correct
19 to the best of your knowledge?

20 A. Yes, it is.

21 MS. PROCTOR: Your Honor, we would move the
22 admission of Exhibits 480T and 481T and make Mr.
23 Kargoll available for cross-examination.

24 JUDGE WALLIS: Is there objection? Let the
25 record show that there is no objection and Exhibits

02583

1 480T and 481T are received.

2 (Admitted Exhibits 480T, 481T.)

3

4 CROSS-EXAMINATION

5 BY MS. HASTINGS:

6 Q. Morning, Mr. Kargoll.

7 A. Good morning.

8 Q. In your direct testimony, I don't think the
9 page is actually numbered, it's the first page -- you
10 indicate that your responsibilities include developing
11 and implementing of AT&T's regulatory policies
12 regarding local exchange competition; is that correct?

13 A. That's correct.

14 Q. Can you elaborate for me exactly what that
15 involves?

16 A. It involves a variety of things including,
17 for example, what I'm doing today, appearing as AT&T's
18 policy witness in regulatory proceedings where local
19 competition and intraLATA competition issues have come
20 up and need to be addressed. It includes working on
21 developing policies that AT&T goes forward and
22 advocates before regulatory bodies on those issues.
23 Partnerships in workshops, meeting with commissioners,
24 their staff, meeting with company representatives and
25 the like.

02584

1 Q. So would you say you have a fairly good
2 sense of the local exchange marketplace, the
3 competitive environment in the local exchange market
4 at this time?

5 A. Yes.

6 Q. Mr. Kargoll, are you aware of the article
7 that appeared in the Wall Street Journal in December
8 of this past year that reported the circulation within
9 AT&T of a document that describes the company's plans
10 to develop five regions within AT&T to provide local
11 phone service in those regions?

12 A. I'm familiar with the article, yes.

13 Q. And are you familiar with the plan that the
14 article references?

15 A. No, I'm not familiar specifically with the
16 plan that's referenced in the article.

17 Q. So in connection with your responsibility
18 for developing and implementing regulatory policies
19 regarding local exchange service you don't have
20 familiarity with AT&T's plans in that regard? Is that
21 my understanding of what you just said?

22 A. That's correct.

23 Q. That particular memo names there will be
24 five vice-presidents or executives that will head
25 AT&T's local phone business on a regional basis. Do

02585

1 you have any reason to believe that's not a correct
2 identification of what AT&T's plans are in that
3 regard?

4 A. I believe that is correct.

5 Q. And for instance, the article indicated
6 that a Ms. Lois Hedg-peth will be named to head up the
7 AT&T division in the Pacific area?

8 A. She has been, yes.

9 Q. Do you know how large her work organization
10 is at this time?

11 A. No, I do not.

12 Q. And do you have any reason to believe that
13 the reorganization that's announced that there's any
14 inaccuracy in the Wall Street Journal article that
15 said the reorganization is part of a 10 year strategic
16 plan which the memo dubbed target growth 2000 strategy
17 which is AT&T's plan to enter the local exchange
18 market at a fairly intense level? Do you have any
19 reason to believe that?

20 MS. PROCTOR: Excuse me, Your Honor. I'm
21 sorry, I didn't mean to interrupt, but I think that
22 since Ms. Hastings has the article in front of her it
23 would be easier and more fair to the witness if he also
24 had the article in front of him.

25 MS. HASTINGS: Be happy to accommodate him.

02586

1 Q. Do you have any reason to believe that what
2 the article reported in that regard is not correct,
3 that AT&T plans a 10 year strategy to infiltrate the
4 local exchange market?

5 A. I don't know if I would characterize it as
6 infiltrate. I think the article correctly captures
7 our desire to enter into the local phone business in
8 order to meet the needs that have been expressed by
9 our customers so to that extent I think the article is
10 entirely accurate.

11 Q. Thank you. Mr. Kargoll, you weren't here
12 the other day when Mr. Mayo testified?

13 A. I was eavesdropping.

14 Q. So was I. I believe Mr. Shaw asked Dr.
15 Mayo whether or not he could identify any services
16 which could be provided at TS LRIC on a sustained
17 basis, and if I recall the testimony correctly he was
18 unable to do that. Can you identify any service that
19 a company can provide on a sustained basis at a TS
20 LRIC?

21 A. Well, as I recall Dr. Mayo's response was
22 that he didn't have the cost information available to
23 him to be able to make that determination, nor do I
24 have before me any cost information specifically for
25 telecommunications or other services that would lead

02587

1 me to believe that the services either had or hadn't
2 been over the long-term been priced at TS LRIC.

3 Q. So your answer is you can't identify any
4 service in any market in any industry in the United
5 States that over a sustained basis has been priced at
6 TS LRIC?

7 MS. PROCTOR: Objection, asked and answered.

8 MS. HASTINGS: I'm not sure that I
9 understood that he had answered my question. I think
10 he said that he hadn't looked at any studies but I was
11 asking him if he could identify any product, and I
12 don't think he's answered that he cannot identify a
13 product.

14 JUDGE WALLIS: The witness may respond.

15 A. No, I do not. I don't have the cost
16 studies available that would allow me to make that
17 determination.

18 Q. If U S WEST is able to get into the
19 interLATA market and it needs interstate interLATA
20 facilities from AT&T, is AT&T in a position or is it
21 AT&T's position that they would provide those
22 interstate interLATA facilities to U S WEST at their
23 TS LRIC costs?

24 A. AT&T would be willing to provide U S WEST
25 on a resale basis with the facilities it needed to

02588

1 provide long distance toll at market rates, and as Dr.
2 Mayo had pointed out on Monday those rates at any point
3 in time can be above or below or at TS LRIC, but
4 they're the market pressures that drive those rates to
5 TS LRIC and they would be the rates that the market
6 dictates.

7 Q. But you're not testifying that you would in
8 fact offer those services to U S WEST at TS LRIC in
9 all instances; is that correct?

10 A. That's correct.

11 Q. I wanted to ask you a few questions about
12 your resell proposal. AT&T seems to be about the only
13 party in this proceeding that has a position on
14 resell; is that correct?

15 A. That's correct.

16 Q. And would it be a fair characterization
17 that your position is directly related to AT&T's
18 desire as exhibited in the Wall Street Journal article
19 to enter the local exchange market that resell would
20 be a quick and easy way for AT&T to do that?

21 A. It would be -- resell certainly would be
22 one of the vehicles that we would use to enter the
23 long distance market. As expressed in the Wall Street
24 Journal article there are a variety of options that
25 would be available but resell we would like to see as

02589

1 being one of them.

2 Q. You indicated I think you just changed your
3 testimony, corrected it on the stand, that you believe
4 based on your analysis that the margin between
5 wholesale and retail for local exchange rate services
6 should be set at least at 33 percent now I think is
7 your corrected number; is that correct?

8 A. That's right.

9 Q. And what exact studies have you done that
10 allowed you to arrive at that 33 percent?

11 A. This comes from an internal study developed
12 in the controller organization in New Jersey, an
13 economic analysis group that had initially set out, I
14 believe, to try to quantify what benchmark retailing
15 costs we could expect to incur as we go into a resell
16 environment. At that point I think middle of this
17 last year we had begun operating in Rochester, New
18 York reselling local service, and I think there was a
19 desire to see if the costs we were incurring were
20 efficient or not, and there was a study undertaken to
21 look at the benchmark costs, the costs that local
22 exchange carriers incur for those types of retailing
23 functions.

24 That study also pointed to, as I indicate
25 here, the retail avoided costs that the LECs would

02590

1 experience in selling to a wholesale as opposed to a
2 retail channel so this comes from an internal AT&T
3 study.

4 Q. Did you participate in the preparation of
5 that study?

6 A. No, I did not.

7 Q. Did you prepare any of the materials in any
8 way that related or produced this percent that you're
9 reflecting in your testimony?

10 A. No, I did not.

11 Q. Did anyone under your direct supervision or
12 control prepare or develop any of the materials that
13 lead to the percents that you're identifying in your
14 testimony?

15 A. Not in my supervision. There was a witness
16 who had filed testimony previously in this proceeding
17 Diane Toomey, from what I understand directed the
18 completion of the study.

19 Q. I believe her testimony is no longer part
20 of this docket; is that correct?

21 A. That's my understanding.

22 Q. Do you know whether AT&T paid to have the
23 study produced?

24 A. The study was produced, my understanding,
25 by AT&T employees who worked for the company. They

02591

1 were paid for that work.

2 Q. Do you know whether or not the study is a TS
3 LRIC study?

4 A. No, the study is not a TS LRIC study.

5 Q. So, to follow up on that, you haven't
6 studied the TS LRIC models and the cost methodologies
7 of U S WEST to determine the retail costs that a LEC
8 would avoid; is that correct?

9 A. That's right. My understanding is those
10 results are not available to us. In fact I think in
11 my testimony I point out my preference would be to do
12 exactly that, look at TS LRIC studies in order to
13 determine what the avoided retailing costs are but
14 those are not available to us.

15 Q. So in fact you don't -- and I don't want to
16 ask you a question you think you've already answered
17 but to make sure it's clear on the record, you have
18 not looked at U S WEST TS LRIC cost studies to
19 determine whether or not in fact 33 percent of its
20 costs are avoidable in a retail market; is that
21 correct?

22 A. That's correct.

23 Q. Now, is it your understanding -- and
24 actually I should ask you, have you read Dr. Wilcox's
25 testimony?

02592

1 A. Yes, I believe so a few months back.

2 Q. Thank you. Would you agree, and I would be
3 happy to give you the chance to look at it, that in
4 her testimony Dr. Wilcox indicates that the access
5 service U S WEST provides is a wholesale service?

6 A. That's my recollection that reference to
7 that was made, yes.

8 Q. And U S WEST access service is available
9 for resale; is that correct?

10 A. I don't know if I would agree entirely with
11 the characterization of access as a wholesale service
12 that was available for resale. In other words, the
13 resale environment I'm talking about is taking a
14 service that U S WEST currently sells to an end user
15 customer, say flat rate service, and allowing AT&T to
16 buy that flat rate service from U S WEST to resell to
17 perhaps the same customer. Access services are not
18 sold by U S WEST to end users. They're sold to
19 interexchange carriers that turn around and provide
20 other inputs of their own and then package that as toll
21 service that is ultimately sold to the customer, so I
22 think it's somewhat of a gray area but I wouldn't
23 necessarily characterize access as a wholesale service
24 in the same vein as I would what we're attempting to do
25 for your end users services.

02593

1 Q. If you know, do you know whether the
2 processing of service orders is necessary for the
3 company to provide access service?

4 A. Yes. I believe we do have a service
5 ordering process when we make a request for certain
6 types of services you would process that order and
7 implement the service.

8 Q. And is there accounting and record
9 maintenance work that needs to be done in order to
10 provide that access service to interexchange carriers,
11 if you know?

12 A. Oh, certainly, yes, there would be.

13 Q. Is there billing and collection services
14 associated with providing access service to
15 interexchange carriers?

16 A. That's right. In fact if you look at many
17 of the functions to sell both in a wholesale and
18 retail channel certainly those functions exist in both
19 channels, but as I demonstrate in my testimony that
20 the costs you incur for providing the service in a
21 retail channel are markedly less.

22 Q. I thought you indicated earlier that you
23 hadn't looked at U S WEST costs and so you're not
24 really sure?

25 A. The study that I referred to, the 33

02594

1 percent, does examine U S WEST costs for the state of
2 Washington.

3 Q. It looks at U S WEST TS LRIC costs in the
4 state of Washington?

5 A. No, embedded cost.

6 Q. And is receiving trouble reports and
7 arranging for ongoing repair a function that the
8 company performs in providing access services?

9 A. Yes, it does.

10 Q. And it's dealing with overdue accounts,
11 risk among collectibles, sales and marketing, product
12 development functions in providing its access
13 services?

14 A. I would hope we wouldn't have a problem
15 with you with overdue accounts but certainly product
16 development and the other sales functions you
17 mentioned are associated with the access service you
18 provide.

19 Q. Have you investigated what costs -- well,
20 let me back you up here. You indicate in your
21 testimony on page 24 that in connection with resell
22 there ought to be some automated interfaces that
23 should be established between U S WEST and the
24 resellers. Have you investigated what it would cost U
25 S WEST to provide those automated interfaces?

02595

1 A. No, I have not. My expectation is that
2 there will be costs for interfaces for both resellers
3 and for U S WEST. My expectation would be that the
4 costs by and large would be borne by the resellers.
5 We're not advocating that U S WEST change in any way
6 it does service order processing, it handles trouble
7 reports, it does any of the other functions that it
8 does in providing, for example, residential service.
9 What we're asking that carriers like AT&T understand
10 and get from U S WEST the specifications for their
11 systems, and we are allowed to build toward the system
12 so we're not looking for U S WEST to change in any way
13 the systems to provide for these interfaces but to
14 allow us electronic access to these systems.

15 Q. And so if there are costs I think I heard
16 you say, correct me if I'm wrong, that if there are
17 costs incurred by the LECs to develop these specific
18 interfaces for resellers those costs should be borne
19 directly by the resellers; is that correct?

20 A. That's right.

21 Q. And so would that be in your mind like a
22 direct charge to them or would you expect that that
23 would somehow be embedded somehow in the cost of the
24 retail product?

25 A. Again, the costs I'm envisioning would be

02596

1 primarily the costs that the resellers would expend in
2 order to develop their own systems to interface with
3 the systems that you have available. To the extent
4 that U S WEST incurs any costs at all -- and the only
5 one that frankly comes to mind would be costs for
6 security systems which would prevent, say, a reseller
7 from getting access to information about your
8 customers. I think the option would be to examine
9 two methods of recovery; one, the method that you had
10 suggested, pricing the wholesale service in a way that
11 recovers the costs, for example, of implementing
12 security procedures. The other alternative would be
13 whether that cost should be spread out among all
14 carriers and recovered over a two or three or four year
15 period in order to minimize the barrier to entry that
16 that could cause by having it included in the price
17 directly.

18 Q. And so you're assuming in your answer that
19 these systems somehow exist at this point and just
20 simply need to have some security attached to them; is
21 that correct?

22 A. Yes. For example, customers now in U S
23 WEST territory can call up a commerce service
24 representative that works for U S WEST and order local
25 exchange service and order custom calling features and

02597

1 tell U S WEST who they want their toll provider to be,
2 and U S WEST will go forward and take that order and
3 process it. From what I understand those systems are
4 in fact in place and customers do this every day.
5 We're looking for the ability to be able to
6 electronically interact with your systems in order to
7 perform the same function for customers when we resell
8 your service.

9 Q. But you don't know for a fact that those
10 systems with automated interfaces would in fact meet
11 the needs of resellers, do you?

12 A. Resellers' needs would be met if we were
13 able to provide service to our customers on the same
14 basis as you provide service to your customers. If,
15 for example, you didn't have an automated system
16 available then we're not proposing that you make one
17 available specifically for resellers. In other words,
18 if you deal with your end users on a manual basis for,
19 say, trouble reporting, then we would expect a similar
20 type of system to be set up for resellers.

21 Q. Does AT&T resell services today?

22 A. On a local basis?

23 Q. On any basis.

24 A. We are currently reselling local exchange
25 service in only one jurisdiction, and that would be in

02598

1 Rochester, New York. Rochester Telephone Company
2 offers a wholesale flat rate local service offering
3 that we resell to end users.

4 Q. But my question is does AT&T resell its own
5 services?

6 A. Oh, yes. For our long distance services
7 yes, we do.

8 Q. Do you provide mechanized interfaces to the
9 resellers in the provisioning of those resold
10 services?

11 A. My understanding is we do not. We provide
12 the interfaces to resellers here again that are
13 necessary in order for them to provide their customers
14 with the same service quality that we provide to our
15 own users.

16 Q. Would AT&T agree with the U S WEST tariff
17 on resell that would make resell subject to the
18 availability of facilities?

19 A. Let me make sure I understand your
20 question. If, for example, there was unserved
21 territory in U S WEST's area would we be looking to
22 ask U S WEST to provide us resold services currently
23 on unserved territory.

24 Q. Or there was a lack of facilities in
25 downtown Seattle.

02599

1 A. Again, let me see if I can answer it this
2 way. On a resell basis we would just be utilizing
3 your underlying facilities to provide our service,
4 local intraLATA toll, custom calling features. To the
5 extent you didn't have facilities we wouldn't be able
6 to and couldn't provide that service. So in other
7 words, AT&T would not be asking U S WEST to build out
8 in any areas in order to allow us to provide resold
9 service. We would be looking to resell your existing
10 network.

11 Q. So in answer to my question you would then
12 agree with the U S WEST provision that it would place
13 in a tariff that would make the resale of its services
14 subject to the availability of facilities?

15 A. I guess I'm having problem with the subject
16 to availability of facilities. If it's limited to the
17 fact that the facilities are not in place to that
18 customer location, then, yes, we would be satisfied
19 with that. We wouldn't be satisfied with any tariff
20 provision that would limit, say, our ability to
21 provide resold service to customers that you are
22 already serving. That we would certainly find
23 problematic. I don't know if that clears it up.

24 Q. So you would find it if you came to U S
25 WEST and you had a requirement for a service so that

02600

1 you could resell it to a service and U S WEST did not
2 have the right pair in downtown Seattle you would
3 expect that U S WEST would take a held order on that?

4 A. Again, I'm not sure based on the question.
5 Let me try this one more time. If you have an
6 existing customer and that customer decides it want to
7 take its office from AT&T on a resell basis we
8 wouldn't want to see any tariffed provision that would
9 prevent us from doing that or, alternatively, if a new
10 customer moved into the area, say in an apartment
11 building, that you as U S WEST were already serving we
12 would find it problematic to have any tariff provision
13 prevent us from reselling service on a resell basis to
14 delivering service to a customer in that apartment
15 building you are already serving. But we're not
16 asking that you install new facilities or build out to
17 new locations in order to allow us to provide resale.

18 Q. So let me see if I can ask the question
19 again. You would expect, then, under the scenario
20 that I've described that U S WEST would take a held
21 order, say in downtown Seattle if it did not have
22 facilities to meet a particular need for AT&T on a
23 particular day?

24 A. Yes, if what you mean by facilities you
25 didn't have facilities in place to mean that you

02601

1 currently weren't serving that location, the answer
2 would be yes.

3 Q. You indicate on page 15 of your testimony
4 at about lines 8 through about 11 that U S WEST can
5 price its intraLATA toll services to customers at its
6 toll price and still earn a substantial return on
7 switched access and you go on to say that this is not
8 because U S WEST is any more efficient than an IXC but
9 rather because U S WEST retains substantial market
10 power in the provision of services. Have you provided
11 any evidence for this record that U S WEST is not more
12 efficient than an IXC?

13 A. No, I have not, and I don't mean to imply
14 that U S WEST is any more less or equipment to IXCs in
15 terms of efficiency. The statement there just got to
16 the fact that this didn't matter whether they were
17 more, less or equally efficient that they would always
18 have the ability to compete profitably where IXCs
19 might not.

20 Q. Isn't that in theory only? You're not
21 producing any evidence on this record that AT&T is
22 just as efficient as U S WEST, are you?

23 A. No, that's right. I have no knowledge of
24 whether they're more, less or equally efficient.

25 Q. So in theory if they're both equally

02602

1 efficient then you would have equal profits, is that
2 your point?

3 A. No, that's not. The point is we could be
4 equally -- let's assume we're equally efficient in how
5 we provision toll service. The problem comes up where
6 U S WEST is able to extract all of its profitably from
7 the monopoly access service it sells to us that we buy
8 natural and it becomes immediately our cost. U S WEST
9 in doing that is available to limit our profitably in
10 providing toll service yet it continues to remain
11 profitable in that market because of the contribution
12 it earns on access.

13 Q. But my question to you was whether or not
14 you have produced any evidence in this proceeding that
15 AT&T is as efficient as U S WEST in the provision of
16 its services.

17 MS. PROCTOR: Objection, Your Honor. He has
18 been asked and answered this question several times.

19 MS. HASTINGS: I don't know that he has.
20 My questions are fairly simple, has he produced any
21 evidence and I don't know that I've heard him say he
22 has or has not.

23 A. I have not.

24 Q. Thank you. On page 14 of your testimony,
25 Mr. Kargoll, you indicate or you seem to imply that a

02603

1 disproportionate reduction in toll in carrier access
2 will put AT&T in a classic price squeeze. Have you
3 produced any evidence in this docket that would
4 demonstrate that that in fact has occurred?

5 A. AT&T witness Ms. Parker has looked into
6 this and determined that that may actually be the
7 case. Evidently you have on the board some fairly
8 substantial reductions planned for toll and based on
9 my discussions with Ms. Parker it looks like at least
10 in the fares phase there's going to be little if any
11 toll reductions that take place because access doesn't
12 look like it's going to come down at all for toll
13 customers.

14 Q. So is your answer that Ms. Parker has put
15 evidence on the record that would indicate that there
16 is a price squeeze caused by the disproportionate
17 reduction in toll in carrier access?

18 MS. PROCTOR: Objection, Your Honor. I
19 don't see how any witness can determine anything
20 because as late as yesterday U S WEST was providing us
21 a new proposal for access charges which frankly at this
22 point in time AT&T has not been able to analyze.

23 MS. HASTINGS: Well, that's fine. If the
24 answer is that there's no evidence on the record,
25 that's fine. Is that the answer?

02604

1 MS. PROCTOR: No, that's not the objection.
2 I'm saying that it would not be possible for anyone at
3 this point in time to have made a determination and the
4 form of your question says there is no evidence
5 anywhere in the record at any time and that's not
6 correct.

7 MS. HASTINGS: Well, I think my question
8 was have you produced any evidence.

9 JUDGE WALLIS: I'm going to allow the
10 witness to respond.

11 A. I would suggest that you hold that question
12 until Ms. Parker takes the stand because I believe she
13 can address that more thoroughly.

14 Q. And I will ask her, but I'm also asking
15 you, have you produced any evidence if you can answer
16 whether you have and then I can ask her when she comes
17 on next week?

18 A. I have not.

19 Q. I wanted to ask you, you talk earlier in
20 your testimony -- is the interLATA toll market
21 effectively market?

22 A. The interLATA market?

23 Q. Yes.

24 A. Yes, it is.

25 Q. At what point did the interLATA toll market

02605

1 become effectively competitive?

2 A. I have not done a study to document exactly
3 when that occurred. Generally speaking I think it was
4 the combination of a couple of things that occurred
5 about the same time in the early to the mid '80s that
6 broke up the former Bell system and provided for
7 interLATA equal access that allowed the ability of
8 competing facilities-based carriers to enter the
9 market and begin to effectively compete against AT&T,
10 so early to mid '80s is my general understanding of
11 when the market became effectively competitive.

12 Q. What percent of the market did AT&T have at
13 that time that you're referring to for interLATA long
14 distance services?

15 A. My understanding is that the onset of the
16 divestiture we had approximately 90 or 10 percent of
17 that market and throughout the '80s as equal access
18 cutovers were made, I guess excluding more or less in
19 '87, that that market share declined rapidly.

20 Q. And to what percent?

21 A. Today I know it stands.

22 Q. I don't want to know today. I would like
23 to know in '87 time frame you're referring to in terms
24 of equal access subscription?

25 A. My recollection is that it was brought down

02606

1 to about the 70s, somewhere in the 70 percent or so
2 market share area.

3 Q. Do you know for a fact that that was the
4 percent?

5 A. It's been quite a while since I've looked
6 at the numbers. I really can't recall the exact
7 number.

8 Q. Thank you. And so you don't know for a
9 fact that 70 percent is accurate?

10 MS. PROCTOR: Objection, asked and answered.

11 MS. HASTINGS: I think he said he couldn't
12 recall. I just wanted to clarify that he knew for a
13 fact.

14 JUDGE WALLIS: I believe the question has
15 been answered.

16 Q. On page 14 of your testimony you indicate
17 that U S WEST has continued to control the -- can
18 continue to control the intraLATA market. Are you
19 saying by that testimony that U S WEST controls the
20 intraLATA toll market today in Washington?

21 A. Can you point out the line?

22 Q. On page 14 at about lines 12 and 13.

23 A. Yes, that's right both through the
24 exorbitant contribution U S WEST earns on access as
25 well as the absence of intraLATA presubscription.

02607

1 Q. Do you know what percent of the market
2 share of the intraLATA toll market U S WEST has today?

3 A. Not specifically for the dial one MTS dial
4 services, although in most states that I have looked
5 at those numbers are in excess of 90 percent.

6 Q. Thank you. But have you looked at any U S
7 WEST data in that regard?

8 A. Not specifically, although I do know that
9 U S WEST can come in and petition for effectively
10 competitive treatment of its services, and my
11 understanding is that it's not done that for its MTS
12 service.

13 Q. Do you know whether or not -- let me ask
14 you this. Does AT&T invest and do advertising in
15 markets where it doesn't think it will succeed?

16 A. Generally, no.

17 Q. So if it does marketing or advertising in a
18 particular area it is because it believes it will
19 succeed in that area; is that correct?

20 A. Yes. We try to make our advertising as
21 effective as possible and we wouldn't expend those
22 resources if we didn't think we would be successful.

23 Q. Do you have any evidence that demonstrate
24 that the company's zone density proposals are harmful
25 to the market?

02608

1 A. Yes. I think Dr. Mayo was pretty clear in
2 his testimony regarding the harm that will come about
3 if U S WEST is allowed to adopt zone density pricing
4 for access.

5 Q. I'm asking you if you have any evidence of
6 your own.

7 A. Not specifically, no.

8 Q. And then you indicate on page 21 of your
9 testimony that you advocate commercially feasible
10 resell and then you indicate that the Justice
11 Department has included commercially feasible resales
12 as one of the conditions which must be met before
13 Ameritech can be offering interexchange services. Do
14 you know whether or not your use of the words
15 commercially feasible resell and the Justice
16 Department reference that you've made there that
17 they're using the words in the exact same way?

18 A. I cannot state that we used the term in
19 exactly the same way. The Justice Department I don't
20 believe really gave any more detailed explanation
21 whereas you can see I go into quite a bit of detail of
22 what's required.

23 Q. So it would be a fair characterization of
24 your testimony to conclude that when you refer to the
25 Justice Department including commercially feasible

02609

1 resale that that is not meaning necessarily the same
2 thing you mean when you say commercially feasible
3 resale?

4 A. Specific point by point basis, no. I think
5 generally the understanding is consistent between AT&T
6 and the Justice Department and that is resale
7 opportunities need to be made available that actually
8 allow resellers to come in and compete.

9 Q. But your specific recommendations on what
10 you mean by commercially feasible resale are not the
11 same as what has been testified here to as what the
12 Justice Department has included as commercially
13 feasible; is that correct?

14 MS. PROCTOR: Objection, asked and answered.

15 MS. HASTINGS: Well, I don't think he did.

16 JUDGE WALLIS: I believe he has.

17 MS. HASTINGS: Thank you.

18 Q. In the Ameritech region does Ameritech
19 price or provides its residential services below its
20 cost if you know?

21 A. I don't know.

22 Q. And do you know whether or not they provide
23 flat-rated local exchange service or measured local
24 exchange service?

25 A. I don't know what their service

02610

1 alternatives are.

2 Q. And it's your testimony that AT&T believes
3 resale is a good thing; is that correct?

4 A. That's certainly correct. We believe all
5 types of local exchange competition are good, but
6 certainly resale hold the promise of getting
7 competition out there sooner.

8 Q. And resale is also a good thing in the
9 interexchange market; is that correct?

10 A. That's correct.

11 Q. Did AT&T offer resale at divestiture of its
12 long distance services?

13 A. We were required to by the FCC. The FCC
14 prohibits AT&T from including resale prohibitions.

15 Q. At divestiture?

16 A. In fact I believe it predates divestiture.
17 As I recall, the order that forced us to remove all
18 our resale prohibitions I believe was issued by the
19 FCC in '82.

20 Q. Isn't it true that AT&T was found by the
21 FCC to have violated the Communications Act by its
22 unlawful refusal to provide services for resale in the
23 Public Services Enterprises of Pennsylvania situation?

24 MS. PROCTOR: Do you have a date on that,
25 please?

02611

1 MS. HASTINGS: 1995.

2 Q. If you know.

3 A. I'm somewhat familiar with that case. It
4 includes an issue that had been simmering for a while
5 between AT&T and the reseller community, and that had
6 to do with resellers not meeting the terms in volume
7 commitments that had been initially established in the
8 tariff toll offering.

9 Q. My question to you was whether or not it
10 was true they were found by the FCC to have violated
11 the Communications Act and so I think a yes or no
12 answer would be sufficient.

13 A. On a technical condition they had
14 determined we violated. We had not violated in terms
15 of refusing to resell service to that particular
16 company.

17 Q. So in that particular instance AT&T was not
18 in accord with the views you espouse today that resell
19 is a good thing?

20 A. No, I think we were entirely in accord.
21 Again, the case you're referring to had to do with
22 network design information we were looking for the
23 company to provide us in order to make us feel
24 comfortable that they could meet the minimum in volume
25 commitments.

02612

1 Q. What kind of wholesale rates did AT&T offer
2 to long distance providers at divestiture?

3 A. I'm not exactly sure of the rate back at
4 divestiture. At that point there was a WATS tower
5 available where resellers large users could come in
6 and buy toll service at bulk prices. Resellers used
7 WATS initially as a vehicle to enter the long distance
8 business and resell to residential customers and I'm
9 unaware of what that margin exactly was.

10 Q. So your testimony is that AT&T at
11 divestiture did provide wholesale rates to resellers?

12 A. Yes.

13 Q. And on page 21 you talk about line 18 that
14 resellers can succeed in the marketplace by passing
15 along some of the price breaks that they receive.
16 Would you agree with me that inherent in the idea of
17 wholesale is the thought that a party would purchase
18 something in bulk and get a discount for purchasing
19 some entity in bulk and then breaking out the bulk and
20 charging a greater amount or charging amount for each
21 part that they've broken out to reach a greater amount
22 than they would have paid for the wholesale price?

23 Would you agree that's sort of inherent in wholesale?

24 A. Right. I mean, that's where the profit
25 opportunity exists, ability to buy at a bulk price and

02613

1 repackage to end users and offering the end users a
2 price break but garnering for yourself some level of
3 profitability.

4 JUDGE WALLIS: Let me interject just a
5 moment here and ask Ms. Hastings how you're doing on
6 your cross.

7 MS. HASTINGS: Very, very close.

8 Q. Mr. Kargoll, how would you break up an
9 access line?

10 A. Well, AT&T isn't looking to resell -- in
11 terms of services resale, resale an access line, what
12 we're looking to sell is the line, the local usage,
13 the toll usage, the custom calling features. In other
14 words, all the services that you provide today is an
15 integrated package to your end user we would be
16 looking to resell, so we wouldn't be looking to say
17 resell the line without local usage on a resell basis.
18 That might be a vehicle eventually for us if we
19 decided to put a switch in and purchase the unbundle
20 loops that you are about to tariff, but on a resell
21 basis it would be the line, the usage for toll and
22 local as well as the vertical features.

23 Q. And then on page 23 of your testimony you
24 indicate that there would be some costs. The costs
25 included associated end year billing --

02614

1 MS. PROCTOR: Do you have a line?

2 MS. HASTINGS: Lines 1 through 5.

3 Q. Do you know what the cost to provide call
4 forwarding is for U S WEST?

5 A. No, I do not.

6 Q. Do you know how much -- if you don't know
7 the costs then you don't know how much of that cost is
8 attributed to marketing and advertising then, do you?

9 A. No. My understanding is generally speaking
10 the costs of vertical features or custom calling
11 features are significantly less than their current
12 retail price but I don't know specifically what that
13 relationship is for U S WEST.

14 Q. And then just finally, Mr. Kargoll, on page
15 26 of your testimony, you indicate on line 5 to the
16 extent U S WEST has been able to offer any subsidized
17 local exchange rates resellers should have the same
18 ability. Is it your testimony that U S WEST has a
19 choice as to whether or not to offer customers
20 subsidized local exchange rates that U S WEST has an
21 option to serve the residence customers in its
22 territory?

23 A. Yes. I believe you certainly have that
24 option. My understanding is U S WEST has embarked on
25 a fairly aggressive campaign to sell its local

02615

1 exchange. That indicates to me that you've got the
2 ability to determine what exchanges you provide
3 service to and what exchanges you don't.

4 Q. In the exchanges where it's offering
5 service do you believe U S WEST has a choice whether
6 to serve a particular customer?

7 A. As long as U S WEST decides it wants to
8 serve that exchange, but once it decides it wants to
9 sell it it no longer has that obligation.

10 Q. But where it has exchange and is serving
11 the exchange do you understand that it has or is it
12 your testimony that it has a choice to serve a
13 customer within the exchange?

14 A. On an intraexchange basis, no. It has to
15 hold itself out.

16 Q. Mr. Kargoll, do you know whether any
17 interexchange carriers bid for any of the exchanges
18 that U S WEST put up for sale in the state of
19 Washington?

20 A. I don't know.

21 MS. HASTINGS: Thank you.

22 JUDGE WALLIS: Let's take a 15-minute
23 break, please.

24 (Recess.)

25 JUDGE WALLIS: Let's be back on the record,

02616

1 please, following our morning recess. We'll take up
2 now with examination of witness Kargoll by Mr.
3 Manifold of public counsel.

4

5 CROSS-EXAMINATION

6 BY MR. MANIFOLD:

7 Q. Good morning.

8 A. Good morning.

9 Q. You were just answering some questions
10 regarding resale. Does AT&T have a position on
11 whether or not there should be restrictions on the
12 resell of wholesale -- of residential services to
13 business? If you were to purchase residential
14 flat-rated service from U S WEST on a wholesale basis
15 would you agree or not agree or have an opinion on
16 restrictions from selling that to business customers?

17 A. Well, I know from reading the testimony of
18 various parties in this proceeding that there's some
19 contention over where flat rate service is priced with
20 respect to underlying costs, and there have been
21 various studies that U S WEST and AT&T and staff have
22 offered up in that regard. To the extent that remains
23 an open issue and a concern with the Commission that
24 potentially, for example, flat rate service may indeed
25 be priced below cost it would be our recommendation

02617

1 that a resale restriction as you have described
2 prohibiting the selling of flat rate services to
3 business customers would be appropriate.

4 Q. What if there was a finding that both were
5 above cost, would that change your answer?

6 A. Yes, it would. I wouldn't see frankly the
7 need to maintain that specific prohibition provided
8 that it was determined that flat rate service indeed
9 recovered its costs.

10 Q. And costs here we're talking about
11 incremental cost?

12 A. That's right.

13 Q. Does AT&T have something called a true, I
14 think in quotes, or capitalized, discount plan?

15 A. Yes. I believe that's what we call one of
16 the toll discount plans that we offer.

17 Q. Can you tell me generally who is eligible
18 for that, what the terms of that are?

19 A. Hopefully I'm current. I know that there
20 have been some changes made recently, but my
21 understanding is that customers get discounts on their
22 toll usage at various break points, the first being \$10
23 which works out to about 33 cents a day. At that point
24 my understanding is customers get a 10 percent discount
25 on their calling. 25 percent -- I'm sorry. At \$25 a

02618

1 month calling there's another discount break point and
2 I believe that is 20 or 25 percent. I'm not exactly
3 sure, and then I believe it's \$75 or above there's a 30
4 percent discount that kicks in.

5 Q. So and does a customer have to sign up for
6 the program or do they get it automatically if their
7 bill is above that amount?

8 A. My understanding is they need to call an
9 AT&T customer service representative and enroll in the
10 program proactively.

11 Q. Or have received a call from AT&T marketing?

12 A. That's right, from a response to any direct
13 marketing we might do.

14 Q. So if a customer had AT&T as their
15 interexchange carrier and had a toll bill over the \$25
16 break point but had not enrolled in the program they
17 would not receive that discount?

18 A. That's right.

19 Q. And if a customer had less than -- even if
20 they wanted to enroll in the program if they had less
21 than \$10 of usage they wouldn't be receiving any
22 discounts per month?

23 A. For that particular program. Now, for both
24 the customer as you describe as calling with amounts
25 over \$25 or a customer with calling amounts less than

02619

1 10 there are other discount programs that AT&T offers
2 that the customer may in fact qualify for. For the
3 customer, for example, under \$10 there may be a reach out
4 program if that customer qualifies for where they buy
5 an hour's worth of usage, and depending on the state
6 and the location that would vary, but that would
7 provide, say, customers with under \$10 of usage a
8 different rate or a lower rate off of the MTS schedule,
9 so what I'm basically saying is the true program is not
10 the only discount package we have out there. There are
11 other programs that we offer customers as well.

12 Q. At page 12 of your testimony, and I think
13 this was touched on earlier with U S WEST's
14 cross-examination, you testified that AT&T has had
15 greater price reductions than its access reductions.
16 Is that basically your testimony?

17 A. That's right.

18 Q. And you base this on some data that was
19 over a particular five-year period?

20 A. That's right.

21 Q. 1990 to 1995?

22 A. Right.

23 Q. Do you know if your conclusion is sensitive
24 to the particular number of years you picked to
25 perform your calculation?

02620

1 A. Well, certainly ultimately the number I
2 referred to in my testimony certainly depends on what
3 point in time you start and in the analysis, yes. My
4 understanding is the data was not available prior to
5 1990 in this form and we had -- at the time this was
6 filed up until the first quarter of 1995 data
7 available, so we looked at this over the entire range
8 of data availability, but certainly if you were to look
9 at this at any particular point in time the results
10 could vary, yes.

11 Q. Did you perform any sensitivity analysis to
12 determine the relationship between different choices
13 of time and the results of your analysis?

14 A. No, I did not.

15 Q. Do you have what's been marked for
16 identification as Exhibit 482, and that's your response
17 to our data request No. 43?

18 A. Yes, I do.

19 MS. PROCTOR: I would just note for the
20 record, Mr. Manifold, that that's Exhibit 482C.

21 MR. MANIFOLD: Thank you.

22 Q. And this is a confidential exhibit or piece
23 of paper?

24 A. Yes, it is.

25 Q. And is this the response that was given by

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1 the company to that question?

2 A. Yes, it is.

3 MR. MANIFOLD: Your Honor, I would move for
4 the admission of what's been marked as 482C.

5 MS. PROCTOR: No objection.

6 JUDGE WALLIS: The exhibit is received.

7 (Admitted Exhibit 482C.)

8 Q. Now, I would like to ask you a couple of
9 questions about this and I think I can do it without
10 mentioning the specific numbers and I will appreciate
11 your assistance in making sure we don't violate any
12 asserted confidentiality. At the bottom of the page
13 there's a couple of lines, one of which is -- I assume
14 the label at the left is not confidential?

15 A. That's right.

16 Q. One of the labels is the average revenue
17 per minute in various years and the other line is the
18 access unit to cost in various years?

19 A. That's right.

20 Q. And your conclusion was based upon a
21 comparison of the revenue and the unit cost in 1990 to
22 1995?

23 A. That's right, the difference in those two
24 numbers, yes.

25 Q. Looking at this it appears that both lines

02622

1 go up and down over the period between '90 and '95; is
2 that correct?

3 A. Right.

4 Q. Do I understand that the way that you made
5 your calculation was that you took the 1990 number,
6 for instance, for revenue, subtracted the 1995 number,
7 and got an absolute number, made the same calculation
8 for unit cost, got an absolute number and then divided
9 those two by each other?

10 A. That's right. I think actually what I did
11 was compare those two absolute numbers to each other
12 and show that in absolute terms a decline in the
13 average revenue per minute exceeded the access cost
14 per minute.

15 Q. And that was a decline in absolute terms,
16 not percentage or anything like that?

17 A. That's right. That's my recollection.

18 Q. I guess you've said you did not do that
19 then, for instance, from 1991 to 1995?

20 A. No, I did not.

21 Q. Would you accept subject to your check that
22 if you had done that for 1991 to 1995 you would have
23 shown that the average revenue AT&T receives increased
24 while the average access charge decreased?

25 A. Could you just give me a moment?

02623

1 Q. Yes.

2 A. Yes. That appears to be the case.

3 Q. So we could conclude that the conclusion
4 you reached from this is highly sensitive to the
5 choice of beginning year, since the conclusion turns
6 around which year you start with?

7 A. I would agree it's certainly sensitive to
8 using either 1990 or 1991.

9 Q. And would you accept subject to your check
10 that one can get various answers depending upon which
11 combination of years was used limited only by how late
12 I was willing to stay up last night?

13 A. I would.

14 Q. Is it also true that the data that was used
15 to produce the numbers on this exhibit was taken only
16 from customers in the True savings program?

17 A. That's not true. My understanding is this
18 information came from all customers, both business and
19 residence.

20 Q. Do you have available to you the company's
21 response to our data request No. 42?

22 A. Hold on one minute.

23 Q. I have a copy if you don't have it.

24 A. Sorry, I don't have a copy.

25 Q. Give you a minute to look at that.

02624

1 A. Okay.

2 Q. Is what this response shows that this
3 information was based upon business, residential and
4 operator handled and credit card calls Washington
5 intrastate for those who had the true discount plans?

6 A. That's one interpretation. I'm sorry, it
7 does appear to be somewhat ambiguous in this regard.
8 My understanding is that this utilized data across the
9 board from all of our customers in terms of arriving at
10 the average revenue per minute. For example, business
11 customers to the best of my knowledge do not qualify
12 for the True program, that it's a residential customer
13 service offering, so certainly none of the business
14 customers would be included as True, but I do recognize
15 that an interpretation of this could be in fact that
16 this only looks at the True Discount plan. This is
17 something certainly we can check but my understanding
18 is it does consider all of our customers and all of
19 their usage, so in other words if a residential
20 customer were not on our True plan but rather bought
21 toll service out of the standard MTS plan that that
22 would be reflected in the price as well.

23 Q. On the response to data request 42, the
24 references to the two numbers there, I guess it's
25 nine-tenths of a cent and four-tenths of a cent.

02625

1 MR. MANIFOLD: Can we go off the record for
2 a moment?

3 JUDGE WALLIS: Yes.

4 (Discussion off the record.)

5 JUDGE WALLIS: Back on the record.

6 Q. Those are the same numbers -- those are the
7 numbers calculated from Exhibit 482C?

8 A. Right. In response to the question 42 we
9 are in fact referring to the numbers presented in
10 Exhibit 482C.

11 Q. And the company's response to 42 does say
12 that AT&T does not have -- we asked for some
13 historical data. Says, "AT&T does not have this
14 historical data. However, AT&T has done a comparison
15 of average revenue per minute ('ARPM') for 1990
16 through one quarter 1995 for Washington intrastate
17 business, residence, operator handled and credit card
18 calls with True Discount plans." I can read the rest
19 of the response but that's the operative part for
20 this?

21 A. Yes, that's correct.

22 Q. What is there about that that you find
23 confusing or misleading? It seems fairly
24 straightforward that it says that this was for True
25 Discount plans?

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1 A. Unfortunately, you're absolutely right.
2 What I find unsettling about that is my discussion
3 with the person that pulled these numbers together,
4 Diane Toomey who had gathered this data for me, my
5 understanding from her was that this included not only
6 True but customers that purchased data, the MTS tariff
7 and our business customers as well, and again my
8 understanding is that the True program is only
9 available to residential customers. So I see
10 certainly that inconsistency within the answer itself
11 as well as the knowledge that I was given to
12 understand in preparing for this case that indeed this
13 included usage from all of our customers.

14 MS. PROCTOR: Mr. Manifold, we will be glad
15 to look into that. It's my understanding that the
16 witness's understanding is correct, that this is just
17 -- and that's certainly not a clear statement, is it,
18 but that we could have put a period after credit card
19 calls, and the concern was to reflect the inclusion of
20 discount plans, and the True plans it's my
21 understanding were the only plans in effect in
22 Washington state on a state basis, but we can check for
23 you on that.

24 Q. New subject. Page 4 of your testimony you
25 say that if a customer makes one or a hundred or

02627

1 a thousand calls per month, the MTS costs remain the
2 same as toll calls you're talking about?

3 A. Correct. In fact I think I referred to
4 Mark Sievers's testimony in that regard. I think
5 that's where it was included in there initially.

6 Q. I assume you're adopting that for purposes
7 of your testimony?

8 A. Yes, I am.

9 Q. Would you also agree that if a customer
10 makes a thousand local calls per month, the MTS costs
11 remain the same as well?

12 A. Yes, I would.

13 Q. Is it your understanding that when a
14 subdivision is put in the developer or the phone
15 company would normally put in telephone plant to serve
16 that subdivision?

17 A. I'm not a network engineer. That would be
18 my layman's expectation.

19 Q. Yes, I will agree with you then. I'm not
20 either. When a customer -- when a person purchases
21 one of those homes and moves in they then have a
22 choice of whether to order telephone service or not?

23 A. That's right.

24 Q. If they choose not to order telephone
25 service, does that change the investment that the

02628

1 phone company has made in the plant extended to that
2 house?

3 A. Well, certainly the facilities up and until
4 the service drop or where the inside wire begins, I
5 imagine that would not need to be provided so
6 certainly I would imagine there would be some portion
7 of investment that it would in fact shed as a result
8 of not providing that service.

9 Q. Would you expect that there would be a
10 significant portion of nontraffic sensitive costs that
11 would not be affected by whether or not that customer
12 decided to order phone service?

13 A. I don't know frankly what proportion of
14 nontraffic sensitive costs would be impacted, but I
15 would expect that there would be some impact.

16 Q. And some that would not be impacted?

17 A. That's right.

18 Q. And would you agree that when that customer
19 or when that individual then becomes a customer and
20 calls up and orders service from the local phone
21 company that they are in effect ordering local and toll
22 service?

23 A. I don't know if we can speak to exactly
24 what they're ordering beyond access to the network. I
25 think we can safely presume that they want to use the

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1 access for some purpose, but on that it's certainly
2 unclear as to what purpose or what type of usage they
3 want to supply, but generally if what you're asking is
4 do customers order for both access and usage, I could
5 agree with that.

6 Q. And that would be access to the local
7 network and access to the long distance network and
8 international network for that matter?

9 A. That's right.

10 Q. End usage of those?

11 A. That's right.

12 Q. Do you know if that person can order
13 service in Washington that excludes the ability to
14 receive toll calls? In other words, when I call and
15 order telephone service can I tell them I don't want
16 to get any marketing calls from outside my local area
17 or any other toll calls?

18 A. I'm not aware of that type of function
19 being available, no.

20 Q. So people can reach out and touch me no
21 matter what I want to do if I have a phone?

22 A. Unfortunately, as the case might be, yes.

23 Q. You have answered some questions earlier
24 regarding the 33 percent margin in your testimony,
25 which is your understanding of a study that your

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1 company did on the I take it appropriate markup or
2 minimum appropriate markup from wholesale to retail for
3 local exchange. Is that a fair characterization?

4 A. Yes.

5 Q. Do you know what services or functions or
6 things are included in that 33 percent markup?

7 A. Generally, yes. Let me list a few of them
8 perhaps to give you a feel for what was considered.
9 The retailing costs, for example, of end user billing,
10 the collection, bill collection process,
11 uncollectibles, customer service representatives' time
12 spent talking to an end user, advertising to the
13 customer what the company may do for its customers,
14 product development, sales, those are the types of
15 avoided expenses that we're examining.

16 Q. Are there any joint costs included in that?

17 A. The analysis was done, as I had mentioned
18 to counsel for U S WEST before, not on a TS LRIC basis
19 but rather on an embedded cost basis. It made use of
20 some embedded numbers that were filed with the FCC, so
21 there were in fact what would be considered in a TS
22 LRIC analysis perhaps to be joint common costs
23 included in that.

24 Q. Do you have what's been marked as Exhibit
25 483 for identification purposes which is the company's

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1 response to -- AT&T's response to our data request

2 No. 11?

3 A. Yes, I do.

4 Q. And is this a true and correct copy of that
5 response?

6 A. Yes, it would appear so.

7 MR. MANIFOLD: Your Honor, I would move for
8 the admission of what's been marked as Exhibit 483.

9 MS. PROCTOR: No objection.

10 JUDGE WALLIS: The exhibit is received.

11 (Admitted Exhibit 483.)

12 Q. In this data request we asked whether AT&T
13 would guarantee that any reduction in access charges
14 in Washington would be passed through to Washington
15 customers; is that correct?

16 A. That's right.

17 Q. And do I understand your answer to be no,
18 AT&T would not guarantee it but we think that the
19 market would deliver it?

20 A. I think that's the legitimate paraphrasing
21 of the response, yes.

22 Q. Would that still be your answer today?

23 A. Yes, it would.

24 Q. So AT&T will not itself guarantee that any
25 particular percentage would be passed through?

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1 A. Our expectation would be that we're there
2 on access reduction as part of this proceeding.
3 Certainly we have grave doubts if the company's
4 proposal is adopted there will be, but assuming that
5 the Commission responds to our proposal and
6 significantly drops the price of access there would be
7 declines in AT&T's toll prices.

8 Q. If AT&T lowered its toll prices in
9 Washington would you expect to have an increase in
10 traffic as a result of that?

11 A. Typically that's what we find happens.
12 It's called stimulation and it's a fairly common
13 observation that occurs when you drop the price of a
14 good or service the demand for that good or service
15 increases, so we would expect upon price decline in
16 toll service the demand for toll service to increase.

17 Q. So if your access charges are paid to U S
18 WEST on a per minute basis and your number of minutes
19 of use go up, you would expect to be paying more --
20 for more minutes of use even if it were at a lower
21 rate per minute?

22 A. That's right.

23 MR. MANIFOLD: I have no further questions.

24 JUDGE WALLIS: Mr. Harlow.

25 MR. HARLOW: Thank you, Your Honor.

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2

CROSS-EXAMINATION

3 BY MR. HARLOW:

4 Q. Morning, Mr. Kargoll. My name is Brooks
5 Harlow. I represent intervenor Metronet Services
6 Corporation.

7 A. Good morning.

8 Q. You were asked a number of questions on
9 direct and also on cross this morning about resale.
10 One of the questions that Ms. Hastings asked you was
11 whether or not AT&T was the only party in this docket
12 with a position on resale. Have you ever heard of
13 Metronet Services Corporation before?

14 A. Sorry, no, I have not.

15 Q. Have you ever heard of another intervenor
16 in this proceeding, Enhanced Telemanagement Inc.

17 A. I believe so. I believe they were involved
18 in a proceeding in Oregon that I was involved in as
19 well.

20 Q. Do you know what type of firm they are,
21 what type of services they offered?

22 A. My recollection was that they either
23 through a resell arrangement or an agency arrangement
24 sold Centrex services to end user customers.

25 Q. In response to another question by Ms.

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1 Hastings, actually a line of questioning about AT&T
2 believing that resale is good, one of the things you
3 indicated was that it would promote competition in the
4 local exchange market. Do you recall that question
5 and answer?

6 MS. HASTINGS: Your Honor, I am going to
7 object. I think we have some friendly cross going on
8 here.

9 MR. HARLOW: Ms. Hastings opened the door
10 on this. I'm trying to clarify Mr. Kargoll's position
11 both in his direct and on the cross by Ms. Hastings.

12 MS. HASTINGS: With respect to AT&T or with
13 respect to other resellers who have put in no evidence
14 in this docket on resale?

15 MR. HARLOW: I'm trying to clarify AT&T's
16 position.

17 JUDGE WALLIS: I'm going to allow the
18 question, but ask counsel to assure that there's no
19 duplication of material on the record.

20 MR. HARLOW: I don't intend to duplicate
21 the material other than to focus the witness's
22 attention on the subject matter in my cross.

23 Q. Do you recall that question and answer?

24 A. I'm sorry, could you repeat it.

25 Q. It was regarding the benefit of resale to

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1 development of competition?

2 A. Yes, I recall those questions.

3 Q. Are there any other benefits of resale
4 other than developing competition?

5 A. Well, certainly for local exchange services
6 it would provide for the more rapid introduction of
7 competition in areas that might normally receive local
8 competition through facilities-based entrants or
9 either not received those benefits on an expedited
10 basis, and we see that certainly for Washington as
11 being one of the major benefits allowing customers who
12 might not normally have alternatives who live in rural
13 areas or residential customers getting the benefits of
14 choices.

15 Q. Is there any effect on the ability of the
16 incumbent monopoly LEC to engage in discriminatory
17 pricing?

18 MS. HASTINGS: Objection. This is friendly
19 cross.

20 MR. HARLOW: Your Honor, this clearly flows
21 out of Ms. Hastings' cross. Whether or not friendly or
22 not we don't know, I guess, until we get the witness's
23 answer but the Commission considered and declined to
24 adopt a rule prohibiting friendly cross. Instead
25 Commission's rule provides that evidence shall not be

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1 duplicative. This is a new line of inquiry arising
2 from the cross and the direct but it does not duplicate
3 the existing testimony in the record.

4 JUDGE WALLIS: The witness may respond.

5 Q. Do you have the question in mind?

6 A. Could you please repeat it.

7 Q. I will try to. Does allowing unrestricted
8 resale have any effect on the incumbent monopoly LEC's
9 ability to engage in discriminatory pricing?

10 A. Yes. Certainly to the extent that if resale
11 prohibitions were removed for LEC services, for
12 example, the LEC would not be able to price its
13 services differently or like services differently among
14 users or among potential competitors and end users
15 unless there were cost justifications for doing so. In
16 other words, the LEC would not be able to price
17 discriminate if resale prohibitions were removed from
18 their tariffs.

19 Q. Is this one of the reasons that the FCC
20 ordered AT&T to eliminate resale restrictions?

21 A. That's my recollection, yes.

22 Q. Are you familiar with U S WEST Centrex per
23 location pricing scheme that offers discounts to large
24 volume users but only based on the number of lines in
25 a particular location?

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1 MS. HASTINGS: I'm going to object. That's
2 clearly friendly cross and well beyond the scope of
3 any cross I had for Mr. Kargoll and well beyond the
4 scope of his testimony.

5 MR. HARLOW: Well, perhaps I can back up
6 and it would be more clear how it relates to the
7 direct testimony.

8 Q. Dr. Kargoll, in your direct testimony, you
9 testify that a number of locations that you advocate
10 development of commercially feasible resale and the
11 eliminations of restrictions on resale. In offering
12 that direct testimony were you intending only to refer
13 to expressed tariff provisions the LEC might have in
14 place prohibiting resale or were you also intending to
15 encompass pricing structures that might hinder resale?

16 A. I think you interpret my testimony more
17 broadly to include the latter. Indeed it's not
18 specifically or not just the presence of a resale
19 prohibition that could eliminate the ability to
20 resellers to come into the market. There could be
21 tariff structures, discriminatory tariff structure put
22 in place in the market that would not make it feasible
23 or not likely that resellers would come in.

24 Q. Would a tariff structure that bases the
25 discounts to large volume users based solely on their

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1 geographic location be an example of that type of a
2 structure that you're talking about?

3 MS. HASTINGS: I'm going to object again.
4 I don't believe this is even closely relevant to Mr.
5 Kargoll's testimony and again is friendly cross.

6 MR. MANIFOLD: Your Honor, I would like to
7 join in that objection.

8 MR. HARLOW: I don't think it's
9 duplicative. I think it flows directly out of his
10 direct testimony, and it expands on it somewhat but
11 it's clearly not duplicative. It addresses a specific
12 example that is not in the record so it's not
13 duplicative. Friendly or not, it's not prohibited
14 unless it's unduly duplicative.

15 JUDGE WALLIS: I will allow the question.

16 Q. Do you need to have the question read back?

17 A. I believe I understand the question. I
18 think any tariff structure that looked to limit the
19 ability of a reseller to aggregate for purposes of,
20 say, obtaining a volume discount, aggregate either
21 over customers or customer minutes or lines or what
22 have you would clearly be discriminatory and have a
23 dampening effect on the development of resale.
24 Resellers, whether they're reselling toll, flat rate
25 service, Centrex, what have you, should be allowed the

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1 opportunity to qualify for certainly existing volume
2 discounts by aggregating their traffic, and again that
3 could either be lines, customers or minutes of use.

4 Q. Are you aware that U S WEST in Washington
5 charges resellers such as ETI a \$2.50 charge that's
6 referred to as a joint user fee?

7 A. I am not aware of that, no.

8 Q. Is this something that AT&T would be
9 permitted to charge resellers, a specific charge
10 targeted at resellers under the FCC order you refer
11 to?

12 A. Perhaps if you could explain what the joint
13 user fee is. I'm not sure I understand.

14 Q. Joint user fee is a charge that U S WEST
15 imposes on the reseller on a per customer basis,
16 that's the end user customer and the reseller.

17 MS. HASTINGS: I'm going to object. I
18 don't believe that's a proper characterization of what
19 the joint user fee is. Perhaps if Mr. Harlow would
20 like to testify we could have him go on the stand.

21 MR. HARLOW: I do have a copy of the joint
22 user tariff. This is from WNU 31 section 2 revised
23 sheet 31.1, section 2.2.5 A.2.T, joint user services in
24 paragraph 5.6 shall apply to the Centrex plus customer
25 of record. In other words, each end user customer in

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1 order to obtain a directory listing in the Yellow Pages
2 must pay a joint user fee, a JUF tariff charge of
3 \$2.50, and if Ms. Hastings thinks I'm
4 mischaracterizing it I would be happy to have her
5 clarify.

6 MS. HASTINGS: Now he's testifying. I will
7 object on that basis.

8 JUDGE WALLIS: If counsel wishes to phrase
9 a hypothetical question perhaps that would be the way
10 to go.

11 MR. HARLOW: I think I could do it that
12 way.

13 Q. Assume hypothetically that U S WEST poses,
14 in addition to the tariff charges that the high volume
15 nonreseller business customer pays, it charges an
16 additional fee of let's assume hypothetically \$2.50
17 per reseller customer. Is that something that AT&T
18 would be permitted to do under its FCC requirement
19 that it remove restrictions on resale, if you know?

20 A. So what you're saying --

21 MS. HASTINGS: Excuse me, but one more time
22 I would like to object. There's no basis that AT&T in
23 this record that I am aware of that AT&T provides any
24 Centrex services and so I'm not sure the hypothetical
25 is correct.

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1 MR. HARLOW: I'm simply referring to that
2 type of charge, not referring to Centrex services
3 obviously.

4 JUDGE WALLIS: Question is allowed.

5 A. Let me make sure I understand the question.
6 The 2.50 charge would be, for example, charged to your
7 end users because they elect to take service from you
8 as a reseller but would not be charged by U S WEST to
9 their own end users?

10 Q. Yes.

11 A. Yes. That would be discriminatory in terms
12 of -- my guess would be presumed to be discriminatory
13 in the eyes of the FCC if we attempted to do that in
14 terms of our toll service as we sold it to resellers.

15 Q. Assuming hypothetically that U S WEST
16 proposes to increase that charge in a transition basis
17 from \$2.50 to \$5 by the year 1997, would that be
18 consistent with your recommendations in your direct
19 testimony regarding resale?

20 MS. HASTINGS: That's sort of vague. What
21 recommendations regarding resale? Do you have anything
22 more specific?

23 MR. HARLOW: Recommendations against
24 restrictions and prohibitions on resale.

25 A. I don't believe that would be consistent at

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1 all with what I am recommending.

2 Q. In your direct testimony you also discuss a
3 need to unbundle basic network functions. Do you
4 recall that testimony?

5 A. Yes, I do.

6 Q. Assume hypothetically that U S WEST Centrex
7 service is broken down into component parts consisting
8 of the NAC network access connection, which is
9 basically the local loop; features, such as speed
10 calling, conference calling, call holding as another
11 element; and then finally network access. Assume
12 hypothetically that U S WEST's Centrex tariff and
13 price lists require, for example, that a customer, a
14 Centrex customer, purchase both a NAC and features
15 although separate prices are stated for those two
16 elements. Do you have that hypothetical in mind?

17 A. Yes, I do.

18 Q. Would that kind of a tariff requirement be
19 consistent with your direct testimony urging
20 unbundling of basic network functions?

21 A. Well, it certainly wouldn't be unbundling.
22 The purpose of unbundling would be in order to allow
23 for the separate purchase of for example, the NAC, and
24 allow potentially an independent provider to offer the
25 vertical features or the usage or whatever else, so as

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1 long as those functions, that is network access
2 channel and vertical features, remain bundled together,
3 no, that would not conform to what I'm proposing to be
4 done.

5 MR. HARLOW: Thank you, Dr. Kargoll. All I
6 have this morning.

7 JUDGE WALLIS: Any other questions from
8 counsel? From the commissioners.

9 CHAIRMAN NELSON: Yes.

10

11 EXAMINATION

12 BY CHAIRMAN NELSON:

13 Q. Morning, Dr. Kargoll.

14 A. Good morning.

15 Q. Has AT&T filed a tariff to offer local
16 exchange service in Washington?

17 A. No, we have not.

18 Q. Does it intend to?

19 A. I don't have any specific knowledge about
20 our intentions in terms of local entry into this
21 market. I do know that the recent reconsideration in
22 the interconnection order and some of the proposals
23 that we have put on the table here in the U S WEST
24 rate case, depending on the outcome of these
25 proceedings, that will certainly have a big influence

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1 on whether or not we are and other providers come into
2 this market.

3 Q. Are you reasonably conversant with the
4 federal legislation?

5 A. I kind of felt I was a couple of months
6 ago. I don't know where that stands now to be honest
7 with you in terms of what is in and what isn't. It
8 seems to change every day.

9 Q. I understand your dilemma. Let me ask you
10 if AT&T, since you're the policy witness, has an
11 opinion on the legislation, as you understand it,
12 provisions applicable to resale as well as intraLATA
13 toll dialing parity issues. Two questions really.

14 A. I guess in terms of the resale we had in my
15 last examination of the bills real concerns that
16 although both the house and the Senate versions of the
17 legislation endorsed or spoke to the need for resale
18 that there was no real specificity in how resale ought
19 to be accomplished on a local level, so that in terms
20 of resale that was our chief concern, that it didn't
21 embody the specifics that I've proposed here in terms
22 of intraLATA dialing parity. As you may be aware, the
23 concern we have there is my recollection was it linked
24 the availability or the implementation of dialing
25 parity to the RBOC and GTE entry into the long

02645

1 distance business, and certainly, as you know from, I
2 guess advocacy that we've done here and in other
3 states, we don't believe that is the legitimate
4 linkage.

5 Q. Thank you. At page 20 of your direct
6 testimony you discuss the universal service goal and
7 recommend refashioning the mechanism for achieving the
8 goal. Have you heard of the case here in Washington
9 where Thurston County Superior Court held that the
10 Commission lacked the authority to divert funds from
11 one company's ratepayers to another?

12 A. I am afraid I'm not familiar with that.

13 Q. Well, at the top line you recommend the
14 Commission establish a competitively neutral
15 distribution mechanism. I guess you would agree that
16 if we don't have authority that the legislature would
17 be the next candidate to establish such a mechanism?

18 A. That would be right.

19 Q. Have you heard of any other state that has
20 fashioned a distribution mechanism which AT&T would
21 approve of which would fit all of these criteria?

22 A. Let me give you an example. In California
23 we have what's called the universal Life Line
24 telephone service fund, and what that does is it's a
25 fund that provides support to low income households.

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1 It's a state fund that will reimburse the LEC for
2 providing flat rate or measured rate service at half
3 price and installation charges at half price, and
4 that's collected as a surcharge on end user billings
5 of both interexchange carriers and local exchange
6 providers as well. Usually the surcharge historically
7 has been in the 3 to 6 percent area. I don't know
8 what it is today, but that would be an example.

9 Q. Well, that's a targeted subsidy which I
10 think most everyone agrees Life Line, Link Up programs
11 in the various states fit the desire of targeted
12 subsidies going to consumers. I guess -- and perhaps
13 I'm just assuming something in this question, but for
14 the truly high cost rural places has any state met the
15 goal of finding something that's more neutral,
16 competitively neutral for supporting universal service
17 in high cost areas?

18 A. I'm not aware of any state in particular.
19 I don't see any reason, though, you couldn't, say,
20 utilize the same approach that's been done in
21 California and elsewhere for the more targeted low
22 income type programs. Include in that a low income
23 high cost area type of surcharge, but in answer to your
24 question I don't know of any state in particular that's
25 tackled that.

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1 Q. Then with respect to your recommended
2 margin between wholesale and retail rates which you
3 discuss at page 24 of your testimony, am I to
4 understand that you're using the ARMIS cost data just
5 because it is available?

6 A. Basically you're absolutely right. Had we
7 had at our disposable TS LRIC studies, for example, I
8 think those for a variety of reasons would be the
9 studies you want to look at.

10 Q. And then finally page 11 of your rebuttal
11 testimony you address a bit the quality of service
12 issue. My question to you is has AT&T any complaints
13 with respect to the quality of access services it
14 receives from U S WEST in this state?

15 A. Unfortunately, we do. Ms. Parker, an AT&T
16 witness who I think will appear next week has detailed
17 the concerns in two areas, held orders and circuit
18 failures, but, yes, we do have a problem.

19 Q. Thank you.

20 CHAIRMAN NELSON: That's all I have for
21 now.

22 COMMISSIONER HEMSTAD: I don't have any
23 questions.

24 COMMISSIONER GILLIS: I don't have any
25 questions.

02648

1

2

REDIRECT EXAMINATION

3 BY MS. PROCTOR:

4 Q. Just one clarifying question, Dr. Kargoll.

5 In your conversation earlier with Ms. Hastings you
6 were talking about held orders, and again of course
7 you used the term in response to the chairman's
8 questions. What is your understanding of that term
9 held order?

10 A. My understanding is -- and this would apply,
11 I guess, to both interexchange carriers and end users
12 customers -- is that a held order occurs when the
13 company misses a commitment date for installing service
14 or installing a line, that after a certain amount of
15 days beyond the agreed to installation date the order
16 becomes a held order.

17 Q. And in an environment where AT&T were able
18 to resell U S WEST local service, would you expect if
19 AT&T placed an order for local service that just as it
20 places orders today for access services that it could
21 in certain circumstances give rise to a, quote, held
22 order?

23 A. That can certainly occur. Again, the
24 underlying facility will be provided by U S WEST, but
25 if U S WEST were delayed in its installation that

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1 could potentially occur.

2 Q. Thank you.

3 MS. PROCTOR: No further questions.

4 JUDGE WALLIS: Follow-up questions.

5 MS. HASTINGS: I have a couple of follow-up
6 questions if I might.

7

8 RE-CROSS-EXAMINATION

9 BY MS. HASTINGS:

10 Q. Mr. Kargoll, assuming in the resale
11 environment that there remains a difference between
12 the 1FR and 1FB rates, if there were unrestricted
13 resale of the residence service to business customers,
14 as you I think discussed with Mr. Harlow, isn't it true
15 that U S WEST would have no business customers for its
16 business tariff rates?

17 MS. PROCTOR: Excuse me, but that's well
18 beyond the scope of my redirect.

19 JUDGE WALLIS: The question is allowed.

20 A. That would depend on where your business
21 rates stood.

22 Q. I asked you to assume that they would be
23 disparate today like they are now from the 1FR rate.
24 Isn't it true that if they were in fact different, the
25 residence and the business rate, and there were

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1 unrestricted resale to residence customers that U S
2 WEST would have no business customers for its business
3 tariff rates?

4 A. As long as the difference was not cost
5 based and the company was in a sense able to continue
6 to price discriminate against business say, vis-a-vis
7 residential customers or vice versa that type of
8 activity arbitrage for example would indeed occur.

9 Q. Also, I think you asked a question or
10 answered a question in regard to a conversation with
11 Mr. Harlow. Just a clarifying question -- actually,
12 I'm sorry, I believe this was from Mr. Manifold. Might
13 the introduction of competition stimulate advertising
14 for services and thus lead to an increase in
15 advertising expenses?

16 A. I don't doubt that at all. I'm sure that
17 would occur, but it's important to recognize that
18 advertising expenses that the company incurs in order
19 to garner customers or have customers maintain on their
20 network should not be charged or allocated to the
21 wholesale service as you might sell a competitor. In
22 other words, you wouldn't want to see a competitor
23 having to pay U S WEST part of U S WEST's advertising.

24 Q. Thank you.

25 JUDGE WALLIS: Ms. Hastings, before we

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1 leave the company, would it like to reoffer Exhibit
2 368?

3 MS. HASTINGS: Not at this time. Thank
4 you.

5 JUDGE WALLIS: Other follow-up questions?
6 Is there anything further of the witness? It appears
7 that there's not. Mr. Kargoll, thank you for
8 appearing. You're excused from the stand at this
9 time. Let's be off the record while we change
10 witnesses.

11 (Recess.)

12 JUDGE WALLIS: Let's be back on the record,
13 please, following a brief recess. The company has
14 recalled witness Farrow to the stand. Mr. Farrow, I'm
15 going to merely remind you that you have previously
16 been sworn in this proceeding and you remain under
17 oath. Four documents have been distributed in
18 conjunction with Mr. Farrow. One is a multi-page
19 document first page of which is designated revenue
20 analysis, ASIC costs portrayed, that's marked as
21 Exhibit 485 for identification. And Mr. Harlow has
22 distributed three documents the first described as
23 NWP-01-068 is marked as 486 for identification. The
24 second entitled executive overview is 487 for
25 identification, and the third NWP 01-008 is marked

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1 as 488 for identification.

2 (Marked Exhibits 485C, 486, 487 and 488C.)

3 JUDGE WALLIS: I've been reminded that
4 Exhibit 485 contains confidential information and
5 should be designated 485C.

6 MR. OWENS: I think 488 also is
7 confidential.

8 JUDGE WALLIS: And 488 is also designated
9 as confidential.

10 (Discussion off the record.)

11 JUDGE WALLIS: Let's be back on the record.

12 MR. OWENS: Thank you, Your Honor.

13 Whereupon,

14 BRIAN FARROW,
15 having been previously duly sworn, was recalled as a
16 witness herein and was examined and testified
17 further as follows:

18

19 DIRECT EXAMINATION

20 BY MR. OWENS:

21 Q. Good morning, Mr. Farrow. Do you have
22 before you what's been marked as Exhibit 485C?

23 A. Yes, I do.

24 Q. Can you explain what this is, please?

25 A. This document is a comparison of the

02653

1 revenues and total service incremental costs of U S
2 WEST. It shows not only revenues and total service
3 incremental cost, but it also shows the contribution
4 based upon the revenues in total service incremental
5 cost.

6 Q. Under the column entitled cost basis,
7 what's the designation there, staff and USWC and
8 wherever something else appears, what are those
9 intended to convey?

10 A. That column represents the basis for which
11 the total service incremental costs were calculated.
12 Staff would indicate that we use the prescribed
13 depreciation lives as well as the 10.53 percent cost
14 of money that the staff asked us to use in calculating
15 costs. U S WEST C would indicate that we use the
16 economic depreciation lives and the 11.3 percent cost
17 of money that we have proposed in this case. Just a
18 little bit further, the source column indicates the
19 source of the data used in the analysis, and I think
20 most cases here the data has already been filed in
21 this case in some way.

22 Q. Now, on the last two pages of the exhibit,
23 the column headings are a little bit different from
24 the first two pages. Could you explain what those
25 column headings mean, where they are different?

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1 A. On the last two pages we calculated cost
2 based upon the staff ADSRC, in other words, using the
3 proposed assumptions that the staff gave us, the
4 prescribed depreciation lives and the 10.53 percent
5 cost of money. And we also calculated based upon what
6 U S WEST is calculating as ADSRC, and that is using
7 11.3 percent cost of money and economic depreciation
8 lives, so these are totals based upon those costs.

9 Q. Now, I'm sorry, had you finished?

10 A. Yes.

11 Q. There actually aren't any column headings
12 as such on the last page. Should we interpret this as
13 the column headings on the next to the last page
14 carrying over to the columns on the last page?

15 A. That's correct.

16 Q. Why was it that the company prepared this
17 exhibit?

18 A. Well, this was a request from the
19 Commission and from the staff that we provide a basis
20 to show whether or not a product is being subsidized,
21 so we provided this information to show that
22 information.

23 Q. Now, all services are included on Exhibit
24 485C; is that correct?

25 A. No, they are not.

02655

1 Q. Can you state approximately what percent of
2 U S WEST intrastate test year operating revenues are
3 represented by the services that have been included in
4 this exhibit?

5 A. They represent 83 percent of U S WEST's
6 test year revenues.

7 Q. Are Centrex revenues included in the
8 revenue numbers?

9 A. No. Centrex is not included in this.

10 Q. Can you identify the services in addition
11 to Centrex that are not included, at least the major
12 services?

13 A. Well, I can't identify all of them, but some
14 of them are 911, public telephone, 976. Also there's
15 some revenues from -- a big component of it would be
16 the independent to Bell revenues for toll, and that
17 would be about 10 percent of our total revenues so
18 that is not included as well.

19 Q. So to understand what proportion of the
20 company's test year operating revenues would be
21 encompassed by the services in Exhibit 485C and
22 independent toll combined, would we just add those two
23 figures, the 83 and the 10 percent?

24 A. Yeah. If you just add those together you
25 would come up with 93 percent.

02656

1 Q. Do you have any understanding one way or
2 another on the amount, if any, of contribution as
3 you've defined it on Exhibit 485C that's generated by
4 the independent toll product?

5 A. I understand that it's pretty much -- that
6 it doesn't provide any contribution at all, and I
7 think you're probably be better to talk to Mr. Purkey
8 about that since he's more familiar with the revenues
9 for independent to Bell, but I understand it does not
10 provide any contribution.

11 Q. Thank you, Mr. Farrow.

12 MR. OWENS: That completes the oral direct.
13 U S WEST offers Exhibit 485C and I understand that
14 after the noon recess Mr. Farrow will be available for
15 cross on this exhibit plus the cross on the oral
16 surrebuttal of Northwest Payphone Association witness
17 Murray that was delivered on the 15th.

18 JUDGE WALLIS: Is there objection to 485C.

19 MR. BUTLER: Yes. At this point I would
20 ask that at least Your Honor reserve ruling until
21 we've had a chance to ask some questions about what's
22 in this document and what the basis for the numbers
23 are.

24 MS. PROCTOR: I would join in that motion.

25 MR. OWENS: I believe the witness testified

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1 as to what the meaning of the source was. Do I
2 understand you want to go into more detail than that?

3 MS. PROCTOR: Well, for example, Mr. Owens,
4 on switched access the source is listed as "an
5 attached," and I believe Mr. Farrow just testified that
6 there were some materials that had not been previously
7 filed in the docket.

8 MR. TROTTER: Maybe it will be simpler to
9 withhold ruling on this and let the parties examine on
10 this?

11 JUDGE WALLIS: Yes. I will suggest that we
12 will reserve ruling right at this moment and also
13 suggest that during the noon recess the parties may
14 have an opportunity to discuss with the company any
15 questions they might have as a preparation for this
16 afternoon's session. Because we are getting out of
17 here in a relatively timely manner let's set 1:15 as
18 our return time.

19 (Lunch recess taken at 11:48 p.m.)

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AFTERNOON SESSION

2

1:15 p.m

3

JUDGE WALLIS: Let's be back on the record, please, following our noon recess. At the conclusion of this morning's session the Exhibit 485C was offered and questions were posed about it so we reserved a ruling. I understand that there have been some discussions among the matters and that we're ready to proceed. Mr. Shaw.

10

MR. SHAW: Give it to Mr. Owens.

11

MR. OWENS: As I understand it, the concern had to do with a mathematical error in the backup that Mr. Farrow made a correction on the bench's copies and we can supply a revised page tomorrow, and as I understand it other parties wish to have the backup introduced as an exhibit in the record, and U S WEST does not oppose it. We won't sponsor it but we will stipulate its admission without a sponsoring witness, if that accommodates the interest.

20

JUDGE WALLIS: Does that satisfy the other parties? I see some nods and hear no contrary expressions, so consequently 485 thus will include both the exhibit itself as described and also the backup materials and it does contain the correction as noted by the witness and the corrected pages.

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1 MR. NICHOLS: May I just ask a follow-up
2 question on that topic?

3 JUDGE WALLIS: Mr. Nichols.

4 MR. NICHOLS: Perhaps this is directed to
5 U S WEST, actually. Does the fact that the backup
6 material is not going to be sponsored by this witness
7 mean that as far as U S WEST is concerned this witness
8 is not prepared to respond to any examination on the
9 backup material?

10 MR. OWENS: No. That's not what I intended
11 to convey. The backup material is obviously backup
12 for the exhibit that the witness is sponsoring, and so
13 we would not object to cross on the backup as being
14 beyond the scope of his limited supplemental
15 testimony.

16 JUDGE WALLIS: Very well. Are we ready to
17 proceed? The purpose for Mr. Farrow's return is to
18 allow cross-examination by Mr. Harlow, and I am going
19 to suggest that we begin with that and then broaden it
20 to include the material in the recent direct. Would
21 that be acceptable? Please proceed.

22 MR. HARLOW: I do have one procedural
23 question. Did you designate Exhibit 488 as a
24 confidential exhibit?

25 JUDGE WALLIS: Yes.

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1 MR. HARLOW: I wanted to make sure of
2 that.

3

4 CROSS-EXAMINATION

5 BY MR. HARLOW:

6 Q. Good afternoon, Mr. Farrow. My name is
7 Brooks Harlow, and I represent the Northwest Payphone
8 Association in this proceeding.

9 A. Good afternoon.

10 Q. Mr. Farrow, are you an economist?

11 A. No, I'm not an economist by education-wise.

12 Q. At page 1831 of the transcript, which was
13 your oral surrebuttal last week, you referred to nine
14 costing principles. Do you recall that?

15 A. Yes, I do.

16 Q. And do you know that Dr. Emmerson was a
17 party to writing those costing principles?

18 A. Yes.

19 Q. Was that done in connection with a
20 California PUC proceeding?

21 A. Yes, it was.

22 Q. Do you know if Dr. Emmerson worked with Ms.
23 Murray on those costing principles?

24 A. Yes, I do.

25 Q. And she did in fact?

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1 A. She did, yes.

2 Q. Did you prepare the public telephone
3 service cost study of U S WEST that was provided in
4 response to data request by Northwest Payphone
5 Association?

6 A. It was provided in that request. It was
7 prepared by U S WEST.

8 Q. But did you prepare it yourself?

9 A. Not personally I did not prepare it.

10 Q. Are you familiar with the cost study?

11 A. Yes, I am.

12 Q. Also at page 1831 in the transcript you
13 were asked that there's an allegation at page 6 of Ms.
14 Murray's testimony that U S WEST omitted certain costs
15 of the refurbished pay phone terminal in its cost
16 study and you indicated that it was your testimony at
17 that time that that was not a true statement?

18 A. That's correct.

19 Q. Is that question basically the same
20 question that the pay phone association asked U S WEST
21 in data request No. 68 which has been marked as
22 Exhibit 486?

23 A. No. The question there was, is there a
24 market for using unrefurbished standard set that U S
25 WEST removes periodically from various locations.

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1 Q. Do you see the third subpart? Is this
2 value included in the cost summarized in Lanksbury
3 confidential exhibit LDL-2?

4 A. Yes.

5 Q. Is that basically the same question that
6 you were asked on oral surrebuttal?

7 A. No, that's not the same question.

8 Q. How do the questions differ?

9 A. The question I was asked refers to whether
10 or not we included the refurbished pay phone terminal
11 equipment in our cost study and this question refers
12 to the value of the -- is the value included in the
13 cost summarized by Lanksbury confidential exhibit.

14 Q. Do you happen to have Ms. Murray's
15 testimony in front of you that you were referring to
16 in your oral surrebuttal?

17 A. No, I don't.

18 MR. HARLOW: Counsel, can you provide the
19 witness with a copy of Ms. Murray's testimony that was
20 referred to. Appreciate that. Thank you.

21 Q. Now in the transcript you refer to page 6
22 in supplemental testimony of Terry Murray?

23 A. Yes.

24 Q. Do you have page 6 in front of you?

25 A. Yes, I do have it.

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1 Q. Specifically what line number or line
2 numbers were you referring to in your oral
3 surrebuttal?

4 A. Lines 24 and 25.

5 Q. And so the bench can understand what we're
6 talking about, U S WEST's pay phone cost study for the
7 so-called standard pay phones, essentially the costs
8 were the costs shown for the set shelf, the box, if
9 you will, with the key pad and coin slot and
10 everything, essentially the costs, and U S WEST
11 is calculating that by calculating the costs to
12 refurbish an old set; isn't that correct?

13 A. That's correct.

14 Q. And is it not correct that in the pay phone
15 cost study that forms the basis for Mr. Lanksbury's
16 LDL-2 exhibit that it was assumed that the cost of
17 obtaining an old set to be refurbished was zero? Is
18 that not correct?

19 A. We assumed in the cost study the costs to
20 refurbish the set. We did not assign zero to the --
21 as the costs of the set. In other words, the cost to
22 refurbish is the cost of the set.

23 Q. Right, but let's assume in a hypothetical
24 that you're starting a pay phone company. You're not
25 U S WEST, you haven't been in the pay phone business

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1 for 80 years or so. You're starting a company. If
2 you want to install standard refurbished set you would
3 have to go out and buy -- if you want to refurbish them
4 yourself you would have to go out and buy some old
5 sets to refurbish, wouldn't you?

6 A. If you're not purchasing new?

7 Q. If you want to buy surplus sets from any
8 LEC and you want to refurbish sets and install
9 refurbished sets, you would have to go out and purchase
10 them in the open market, would you not?

11 A. Yes, you would.

12 Q. And there would be some costs associated
13 with that for this hypothetical new pay phone company;
14 isn't that correct?

15 A. Yes.

16 Q. But in U S WEST's cost study U S WEST
17 showed a zero element for that particular type of
18 cost; isn't that correct?

19 A. You're talking about the cost of purchasing
20 the pay phones?

21 Q. U S WEST assumed there would be no cost to
22 acquire the old unrefurbished sets; isn't that
23 correct?

24 A. Yes, because we already owned them.

25 Q. And that's essentially the question that

02665

1 was asked in Exhibit 486; is that correct?

2 A. Yes.

3 Q. And the response to that is consistent with
4 the testimony you have just given, that is, that U S
5 WEST did not assign a cost to that acquisition of the
6 old set?

7 A. Not to the acquisition, no. But my
8 testimony refers to lines 24 and 25 which is we
9 assigned a zero cost, and we did not do that to the
10 old style sets. We did assign a cost to the old style
11 sets.

12 Q. Right, but just not to acquire them
13 initially?

14 A. That's correct.

15 Q. Thank you for that clarification.

16 JUDGE WALLIS: Mr. Farrow, could you manage
17 to get that microphone up closer to you.

18 Q. You refer to Ms. Murray's testimony oral
19 surrebuttal beginning at page 7, line 23 and if you
20 could turn to that through page 8, line 4. And it
21 refers to the defects in U S WEST's ASIC cost study.
22 Do you have that testimony in mind?

23 A. Could you give me the numbers? You said
24 Ms. Murray as line 4.

25 Q. It's the question and answer that started

02666

1 at the bottom of page 7 and the answer continues at
2 the top of page 8. Particularly look at the top of
3 page 8 where it refers to the fact that the cost
4 elements are not properly associated with the most
5 important drivers of incremental costs. Do you see
6 that testimony?

7 A. Yes.

8 Q. Are you familiar with Mr. Lanksbury's
9 Exhibit LDL-2 which is an imputation analysis of U S
10 WEST pay phones?

11 A. I am not familiar with the details of it,
12 no, I am not.

13 Q. Have you seen it?

14 A. I have seen it, yes.

15 Q. Might be helpful, I do have an extra copy
16 which I will give you to have in front of you. Do you
17 see how Mr. Lanksbury has three columns of costs in
18 call volume data?

19 A. Yes.

20 Q. And the first two columns break down costs
21 in call volumes according to the type of pay phone set
22 whether it's a standard set or a millenium set?

23 A. Yes.

24 Q. And you see that on line 16 it shows the
25 compensation costs, that the compensation figures are

02667

1 different for a standard set -- I guess it's called
2 public set in this particular set -- versus a
3 millenium set, that the costs shown are different?

4 A. Yes.

5 Q. Is the type of set, pay phone set, that
6 happens to be at a location a cost driver for
7 compensation costs?

8 A. I don't know that answer specifically. I
9 will defer to Mr. Lanksbury on that.

10 Q. Would you be willing to agree that the main
11 driver of compensation costs is the traffic on the
12 phone?

13 A. No, I would not be willing to agree with
14 that because I don't know.

15 Q. We'll save these questions for Mr.
16 Lanksbury then. Do you have any awareness as to
17 whether or not the pay phone market is becoming more
18 or less competitive in Washington?

19 A. That's another question that should go to
20 Mr. Lanksbury.

21 Q. Do you recall your testimony on oral
22 surrebuttal regarding the amortization period --

23 A. Yes, I do.

24 Q. I hadn't finished my question.

25 -- the amortization period for the

02668

1 nonrecurring costs for the installation of the access
2 line?

3 A. Yes.

4 Q. Are you aware that in the 1991 cost study
5 that was used in this Commission's docket No. UT-920174
6 the amortization period was five years?

7 A. No, I am not aware of that.

8 Q. Are you aware of any factor that has
9 changed regarding average station life between 1991
10 and the 1994 cost study that would support U S WEST
11 changing its amortization period from five years to
12 ten years?

13 MR. OWENS: Objection. Assumes a fact not
14 in evidence. The witness stated he wasn't aware that
15 there had been a change.

16 MR. HARLOW: Well, I think the Commission
17 can take official notice of that from its footnote in
18 the fourth supplemental order in UT-920174. The order
19 referred to the cost study or if necessary I guess we
20 can submit it in this docket.

21 JUDGE WALLIS: Perhaps the form of the
22 question.

23 MR. HARLOW: Let me ask it as a
24 hypothetical.

25 Q. Assuming hypothetically that U S WEST has

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1 changed its amortization period from 1991 from five
2 years to ten years in the 1994 cost study, are you
3 aware of any factors that would cause -- that would
4 support changing assumptions in the average station
5 life so as to change that amortization period?

6 A. I am not familiar with the factors that
7 cause that change.

8 Q. Are you personally knowledgeable of what
9 the average station life is for U S WEST pay phones?

10 A. No, I don't have that information
11 available.

12 Q. So in giving your oral surrebuttal you have
13 no knowledge of any fact that would support the use of
14 a ten year amortization period rather than a five year
15 period?

16 A. The ten year period was used because it is
17 aligned with the life of the set.

18 Q. I asked you if you had any facts that you
19 know of to support that ten year assumed life.

20 MR. OWENS: That was asked and answered.
21 The witness just stated what the facts that he was
22 aware of were.

23 JUDGE WALLIS: I believe that the answer
24 was responsive.

25 Q. You have in front of you Exhibit 487?

02670

1 A. Yes.

2 Q. And can you identify this as the executive
3 overview of the public telephone service cost study?

4 A. Yes.

5 Q. And if you turn to page No. 0-5, the
6 definition of -- wait a second. 0-4. Description of
7 long-run incremental costs?

8 A. Yes.

9 Q. Do you see where it says toward the end of
10 the first paragraph LRIC is forward looking in nature,
11 i.e., LRIC uses the latest technologies costs or
12 replacement costs?

13 A. Yes.

14 Q. Further it says, "since LRIC is forward
15 looking it does not measure historical investment
16 decisions of the corporation"?

17 A. Yes.

18 Q. Is that how you would define LRIC cost
19 study methodology?

20 A. Yeah, but this is a rather short
21 definition. A more complete would be to look at the
22 nine cost principles.

23 Q. Okay, but you would agree with this
24 statement?

25 A. Uh-huh.

02671

1 Q. It's your understanding that U S WEST in
2 studying the millenium and standard costs used the
3 then existing and forecasted numbers of millenium and
4 standard pay phones at the time they did the cost
5 study?

6 A. Yes.

7 Q. And so when U S WEST installed more
8 millenium sets than they had forecasted in the cost
9 study, basically installing them at lower traffic
10 locations, the compensation costs, average
11 compensation costs in the study, would have been too
12 high; is that correct?

13 A. Your question is if we installed millennium
14 sets in locations that have low traffic that the
15 compensation costs would be incorrect?

16 Q. Let me try to rephrase it. As I understand
17 Mr. Lanksbury's rebuttal testimony what he is saying
18 is he needed to redo the cost study because US WEST
19 ended up installing more millenium sets than was
20 forecast for purposes of the 1994 cost study. Am I
21 understanding that correctly?

22 A. Yes.

23 Q. And basically what he's saying is just
24 because you install a millenium set that doesn't
25 necessarily increase the compensation costs for that

02672

1 particular location; is that correct?

2 A. If he said that, yes.

3 Q. And looked at in the aggregate, in other
4 words, if you have 50 percent millenniums or 25
5 percent millenniums the aggregate compensation costs
6 for the company as a whole is going to be roughly the
7 same; is that correct?

8 A. I don't know that. Really I have to defer
9 to Mr. Lanksbury as far as how compensation is paid on
10 millenium versus our standard sets.

11 Q. Well, in your surrebuttal you were
12 attacking Ms. Murray's criticism of the linking of the
13 set costs to the compensation -- linking the type of
14 set to the compensation costs. Are you not able to
15 explain that?

16 A. I'm sorry, I didn't believe I attacked her
17 on linking the type of set to the compensation. I
18 said that the number of sets had something to do with
19 the amount of compensation.

20 Q. The number of what type of sets?

21 A. Both types.

22 Q. The overall number?

23 A. It could be individual. See, the
24 information was provided by Mr. Lanksbury.

25 Q. We'll reserve some of these questions for

02673

1 Mr. Lanksbury. Let me ask you, keeping in mind the
2 definition of long run in Exhibit 487, how do you
3 believe a long-run incremental cost study should
4 determine the forward looking cost of pay phone
5 compensation costs?

6 A. Pay phone compensation is a direct cost of
7 providing the service, so those costs should be
8 assigned to the service on a direct basis.

9 Q. But how should you go about determining
10 those costs on a forward looking basis?

11 A. It should be based upon the contractual
12 basis that that exists with our customers.

13 Q. In your opinion should any forward looking
14 adjustment be paid to take into account any
15 expectation by U S WEST that it will have to increase
16 compensation payments in order to obtain and retain
17 pay phone sites?

18 A. If we do have information that is going to
19 cost us more in the long run then we should reflect
20 that in our cost studies.

21 Q. And if you've done a careful and thorough
22 job of preparing your long-run incremental cost
23 studies you wouldn't necessarily expect, but I would
24 assume you would hope that your actual compensation
25 costs would be somewhat close to your long-run

02674

1 incremental cost studies forecasts of those costs.

2 MR. OWENS: Is that a question?

3 MR. HARLOW: What did you say, Mr. Owens.

4 MR. OWENS: I wondered if it was a
5 question.

6 Q. Isn't that correct?

7 A. Are you asking me if our costs today will
8 be equal to our costs tomorrow for compensation?

9 Q. I'm asking you would it be your goal in
10 preparing a long-run incremental cost study, would it
11 be your goal to have your forecasted forward looking
12 compensation costs be borne out by actual experience?

13 A. Experience does -- in many of our long-run
14 cost studies experience does play a role in
15 determining the future costs of the corporation.

16 Q. I'm not asking you now your methodology for
17 determining the costs in the cost study. What I'm
18 asking you is, is one of your goals in doing a cost
19 study to be accurate in forecasting those forward
20 looking costs?

21 A. Yes.

22 MR HARLOW: I apologize in advance for
23 the cumbersomeness of this, but I'm going to ask the
24 witness to work with some confidential numbers and so
25 to avoid getting those on record it would be a little

02675

1 more cumbersome than I would like.

2 Q. Do you have Exhibit 488C in front of you?

3 A. Yes, I do.

4 Q. Do you have a calculator there available to
5 you? If not I have one.

6 A. No, I don't have one.

7 Q. Can you identify Exhibit 488C as the
8 Northwest Payphone Association's data request
9 requesting the total amount paid in commissions to
10 premise owners including signup bonuses or premiums for
11 the placement of U S WEST owned pay phones in
12 Washington by month for 1990 to present and U S WEST
13 responded by providing data for 1994 aggregated and for
14 part of a year 1995?

15 A. Yes.

16 Q. Do you still have in front of you that copy
17 of Exhibit LDL-2 that I provided you?

18 A. Yes.

19 Q. The compensation figure is on line 16, and
20 I've circled it to make it easier for you to see it.
21 There's a compensation figure for public and for
22 millenium and there's not a compensation for
23 semipublic. Do you see that?

24 A. Yes.

25 Q. And the reason for that is that no

02676

1 compensation was paid to semipublic site owners. In
2 fact, they pay U S WEST for the pay phone?

3 A. I don't know that.

4 Q. Would you please multiply the compensation
5 figure for public shown on line 16 times the total
6 number of stations shown on line 27 to come up with
7 the aggregate monthly compensation figure for the
8 public phones?

9 A. Yes, I've done that.

10 Q. Do you have someplace to jot that down so
11 we can add that later?

12 A. (Complying).

13 Q. Now, would you please multiply the
14 compensation figure on line 16 for millenium phones
15 times the total number of millenium stations on line
16 27.

17 Would you please add those two figures?

18 A. (Complying.)

19 Q. Would you please add those two figures that
20 you've written down?

21 A. (Complying).

22 Q. Do you have the sum there now?

23 A. Yes, I do.

24 Q. And that should reflect the total monthly
25 compensation for U S WEST public and millenium phones

02677

1 in the state of Washington?

2 A. I don't know that to be true.

3 Q. Well, is it your understanding --

4 A. I think you really should talk to Mr.
5 Lanksbury about this exhibit.

6 Q. Well, Mr. Lanksbury did not prepare the cost
7 study, did he?

8 A. There's a note here that says less 30
9 percent per Commission order.

10 Q. Excuse me, you're correct about that. That
11 should represent 70 percent on the total commissions,
12 then, shouldn't it?

13 A. I don't know, okay. I don't know what this
14 compensation, if this is compensation to the owner --
15 I should say to the people that replaced the set. I
16 don't know what the compensation is referring to and
17 what's included in it.

18 Q. Well, let me ask you --

19 A. I really would like you to ask Mr.
20 Lanksbury about this exhibit.

21 Q. All right. We'll come back to that with
22 Mr. Lanksbury. Did Mr. Lanksbury ask you to help him
23 in preparing LDL-2?

24 A. No, he did not.

25 Q. Did he have any assistance of U S WEST

02678

1 economists that you're aware of?

2 A. I do not know.

3 MR. HARLOW: Your Honor, at this time I
4 would like to offer exhibits 487 and 486 and 487 and
5 we'll reserve 488C for Mr. Lanksbury.

6 JUDGE WALLIS: Is there objection?

7 MR. OWENS: No objection.

8 JUDGE WALLIS: 486 and 487 are received.

9 (Admitted Exhibits 486 and 487.)

10 MR. HARLOW: That's all the questions I
11 have.

12 JUDGE WALLIS: Let's shift over to cross of
13 the additional testimony and ask if staff has any
14 questions.

15 MR. SMITH: Yes, I do, Your Honor.

16

17 CROSS-EXAMINATION

18 BY MR. SMITH:

19 Q. Good afternoon, Mr. Farrow.

20 A. Hi.

21 Q. I have a few questions about Exhibit 485C.
22 You stated that on page 1, the column entitled cost
23 basis that where staff has indicated the study
24 assumptions are at 10.53 percent cost of money and the
25 Commission's prescribed depreciation rates; is that

02679

1 correct?

2 A. Yes. There are some circumstances where
3 there's 9.23 percent cost of money and I have so
4 indicated that on there as well.

5 Q. 9.23?

6 A. Yeah, for a DS1 and DS3.

7 Q. And where under the column cost basis USWC
8 has indicated the assumptions were for 10.53 rate of
9 return --

10 A. 11.3.

11 Q. I'm sorry, 11.3 rate of return and what you
12 refer to as economic depreciation lives?

13 A. 11.3 cost of money and economic
14 depreciation lives.

15 Q. Are there any other differences between the
16 staff cost basis and the U S WEST cost basis?

17 A. There may be some differences in the 9.23 I
18 believe associated with interest during construction
19 but they're very small.

20 Q. And you indicated also before lunch I think
21 that -- well, these represent total revenues on page
22 2. That figure represents, I believe you said, 83
23 percent of the test year operating revenues; is that
24 right?

25 A. That's correct.

02680

1 Q. And you indicate that your revenues from
2 independent toll would constitute another 10 percent,
3 as I recall?

4 A. That's correct.

5 Q. Is there some document in this record that
6 shows that 10 percent that you're aware of?

7 A. I am not aware of the specific document, but
8 I think we did file this as part of our revenue
9 requirement filing a breakdown of our revenues, and I
10 believe that Mr. Purkey deals with it in one of his
11 analyses.

12 Q. On page 2 of Exhibit 485C at the bottom
13 there's some revenues shown for Centrex at no cost?

14 A. We haven't included Centrex in this
15 analysis. That part of it is not complete yet.

16 Q. Right, and when it's completed will that be
17 available?

18 A. Yes. In fact, we plan on doing this
19 analysis as I mentioned the other day that it will be
20 done on a USOC basis and it takes several months to
21 complete it that way so you will see much more detail
22 later.

23 Q. In that analysis you just described will
24 the studies be conducted on a Commission basis?

25 A. As far as I know the plan is only to do the

02681

1 ones that we were specifically asked to do on a
2 Commission basis.

3 Q. On page 3 of the exhibit you have a column
4 that's labeled staff ADSRC, and from your explanation
5 this morning I understand that that uses the
6 Commission basis assumptions we've just discussed, am
7 I correct about that?

8 A. Yes. You have to be aware that in some
9 cases in looking at this particular column there are
10 some costs that we did not have on a Commission basis,
11 so some of the costs may not be using the prescribed
12 depreciation lives in the 10.53 percent so we would
13 have used the U S WEST ADSRC in that column instead.
14 There are a few instances in there where we had to do
15 that.

16 JUDGE WALLIS: Mr. Smith, I wonder if you
17 could identify the page which you're working from.

18 MR. SMITH: I'm working from page 3 of
19 Exhibit 485C.

20 Q. Just to be clear, Mr. Farrow, it's not your
21 testimony that staff has used the ADSRC cost method in
22 its testimony or exhibits?

23 A. No, it's not.

24 Q. And now there's also some --

25 JUDGE WALLIS: Can we be off the record for

02682

1 just a minute.

2 (Discussion off the record.)

3 Q. Mr. Farrow, you also provided some
4 supporting documentation that's now a part of the
5 exhibit; is that correct?

6 A. Yes.

7 Q. And do you know whether any check was made
8 to insure that the test year quantities used in the
9 calculation of direct costs were accurate?

10 A. I assumed they were but if there was an
11 additional check made other than copying the numbers
12 down you mean?

13 Q. Yes.

14 A. I don't know that.

15 Q. In the case of residential service, am I
16 correct that all of the costs of the loop are assigned
17 to that service?

18 A. The loop costs are shown separately.

19 Q. On page 1 of the exhibit for residence 1FR
20 you show a contribution level there?

21 A. Yes.

22 Q. And is that there because you've assigned
23 all the loop costs to the residential service?

24 A. Yes.

25 Q. If I could, working from the back of the

02683

1 larger exhibit now, and I hope we all have the same
2 pages but mine is the eleventh from the back. It's
3 headed custom calling res USWC?

4 A. Yes, I have it.

5 MS. PROCTOR: Could we go off the record for
6 just a minute.

7 JUDGE WALLIS: Yes.

8 (Discussion off the record.)

9 Q. Mr. Farrow, do you have the page to which I
10 referred?

11 A. Yes, I do.

12 Q. Now, looking at column J of that sheet, it
13 indicates that in some cases ADSRC cost is used and in
14 other cases ASIC is used; is that correct?

15 A. Yes, that's correct.

16 Q. And would the asterisks in column D
17 indicate those cases in which an ASIC estimate was
18 used?

19 A. That's correct.

20 Q. Have cost summaries been included that show
21 the ASIC and ADSRC costs for the custom calling
22 services?

23 A. Not for all of them. Some of the services
24 were not filed in this case and we have not completed
25 updating cost studies for those, so what you're

02684

1 looking at is some older costs that were older studies
2 that we provided and since we did not have in those
3 older studies a breakdown between the ASIC and the
4 ADSRC we provided that was available and that was the
5 ADSRC.

6 Q. And is that what you would have called LRIC
7 in the past?

8 A. That's what we used to call LRIC in the
9 past.

10 MR. SMITH: Thank you. That's all I have.

11 JUDGE WALLIS: Mr. Trotter.

12

13 CROSS-EXAMINATION

14 BY MR. TROTTER:

15 Q. Just staying with the first page of Exhibit
16 485C, the general format of this exhibit or the key
17 format here is revenue in the first column of numbers
18 and then TSIC in the second?

19 A. Yes, that's correct.

20 Q. And turning to the second page down near
21 the bottom you show the total of those two columns of
22 figures; is that right?

23 A. Yes. The total is total for each
24 individual section. In other words, there are some
25 subtotals in there.

02685

1 Q. But I'm just looking at the line called
2 total five up from the bottom on page 2?

3 A. Yes.

4 Q. And in the figure in the first column of
5 figures that ends in \$504, that figure, to the best of
6 your knowledge, test year units times test year rates?

7 A. To the best of my knowledge, yes.

8 Q. And the second, the column next to that
9 which ends in the figure \$120, that is the sum total
10 of what you have characterized as TSIC?

11 A. Yes.

12 Q. And because the revenues exceed that
13 figure, you conclude that if you priced at TSIC you
14 would not cover your test year revenues. Is that the
15 conclusion you intend to draw from this exhibit, this
16 page?

17 A. That is a true statement.

18 Q. Now, if the Commission concluded that some
19 of the costs that you included in TSIC should not be
20 included in TSIC that would make your case even more,
21 would it not? It would show a higher difference
22 between revenues and TSIC?

23 A. If the TSIC was lower, yes, it would show a
24 larger difference.

25 Q. And turning to the fourth page of the

02686

1 exhibit you show the same total revenues as on page 2;
2 is that right?

3 A. Yes.

4 Q. And this time you're comparing that total
5 to the fourth column of figures the amount that ends
6 in 00 pennies; is that right?

7 A. Yes.

8 Q. And because that number that ends in 00
9 pennies is less than the revenue set then you conclude
10 that if you priced at ADSRC you would not obtain your
11 test year revenue level?

12 A. Yes.

13 Q. Did you assume -- I take it from your last
14 couple of responses, since you're comparing it to test
15 year revenue levels, you did not assume any particular
16 level of efficiencies that might be gained had the
17 company priced at TS LRIC or TSIC or ADSRC; is that
18 correct?

19 A. Are you saying that we adjust the numbers
20 in any way for any -- assuming inefficiencies? We
21 didn't make any adjustments in numbers.

22 MR. TROTTER: Those are all my questions.

23 Thank you.

24 JUDGE WALLIS: Ms. Proctor.

25

1 CROSS-EXAMINATION

2 BY MS. PROCTOR:

3 Q. Good afternoon, Mr. Farrow. I'm Susan
4 Proctor from AT&T. On page 1 of Exhibit 485C you
5 entered revenues from the residence CALC, it has no
6 cost under TSIC and there's also a blank under
7 contribution. Was there a reason that the revenue
8 numbers wouldn't appear over in the contribution
9 column?

10 A. They should have.

11 Q. And would the same be true on page 2 where
12 we show revenues of -- excuse me.

13 MS. PROCTOR: Mr. Shaw and Mr. Owens, my
14 understanding the revenues under access are not
15 confidential numbers; is that correct?

16 MR. SHAW: Could we go off the record.

17 JUDGE WALLIS: Yes.

18 (Discussion off the record.)

19 Q. So that the same would be true for the
20 equal access charge, the CCLC and the RIC, those
21 numbers should also appear under contribution?

22 A. Yes.

23 Q. The total that you were just discussing
24 with Mr. Trotter, did it include the numbers you and I
25 were just noting should be included in the

02688

1 contribution column?

2 A. Yes.

3 Q. This morning when you were identifying this
4 exhibit -- and I'm sorry, I don't remember from this
5 morning, Mr. Farrow, did you testify that you prepared
6 this exhibit?

7 A. I worked very closely with the people that
8 worked on this exhibit. It was prepared with my
9 input.

10 Q. And are those people who work for you or
11 with you?

12 A. They work with me, yes.

13 Q. On page 2 under the source, unlike all of
14 the others that either refer to testimony or data
15 requests --

16 A. I didn't quite understand that term. You
17 said source?

18 Q. Yes. I'm sorry, the last column on the
19 right-hand side is source?

20 A. Okay.

21 Q. And I assume that that's the same title for
22 the column on page 2; is that correct?

23 A. That's correct.

24 Q. And as I was saying, unlike for every other
25 service where you show either a data request or a

02689

1 testimony, for access you refer to "and attached."

2 Could you point me to which of these pages in the

3 exhibit you were referring to there?

4 A. It would be the page marked at the top,

5 says overall summary, Washington with prescribed lives

6 N 10.53 percent cost of money, switch access service

7 local transport restructure format. There's a date of

8 11-13-95 on it.

9 Q. Is that it (indicating)?

10 A. Yes, that's it.

11 Q. This is dated 11-13-95?

12 A. Yes.

13 Q. To your knowledge, is this part of a cost

14 study?

15 A. This was a part of the recalculation of the

16 costs that prescribed lives in 10.53 percent cost of

17 money.

18 Q. Does that mean it was part of a cost study?

19 A. Yes.

20 Q. And to your knowledge, was this cost study

21 produced to the interexchange carriers?

22 A. Was it given to them?

23 Q. Yes.

24 A. To my knowledge, no, this is the first

25 time.

02690

1 Q. And is there more documentation than simply
2 the single page that comprises the cost study?

3 A. Well, typically in some cases we don't do
4 full backup documentation when we run these scenarios
5 like this, so I'm not certain if there is full backup
6 for this one.

7 MS. PROCTOR: Your Honor, we would like to
8 make a record request for the new switched access
9 service cost study.

10 A. This is not the new cost study. This is
11 just a cost study that uses prescribed lives and 10.53
12 cost of money. It is not the new cost study.

13 Q. It is a new cost study, isn't it?

14 A. It is a new cost study, yes.

15 MS. PROCTOR: I would like to make a record
16 request for a new cost study or this new cost study in
17 particular.

18 MR. OWENS: Well, I believe the witness's
19 testimony is to the effect that this is simply an
20 output of the calculation that's mechanized the
21 underlying documentation of which has already been
22 produced. I suppose if there's any scintilla of
23 backup that we can find that hasn't been produced we
24 can come up with that, but I'm not sure there's
25 anything that the witness has stated that would

02691

1 support a record requisition at this point.

2 MS. PROCTOR: I think, Your Honor, I
3 understood the witness to say that this was part of a
4 new study that they had done, that it concerned
5 switched access, some cost that I think everyone knows
6 constitutes single largest component of an interchange
7 carrier's expenses. I would be a lot happier knowing
8 that we had all of this, but if there's nothing more
9 than this one page then they can just tell us that. If
10 there's more to this document than this one page I
11 think we're entitled to see it and actually it would
12 have been nice, since we have outstanding data requests
13 that were continuing requests for cost studies for
14 switched access had we received it in the November time
15 frame when it was produced.

16 MR. OWENS: The witness testified that this
17 was simply a rerun of the unchanged study with only
18 two modifications, that of the cost of money to
19 conform with the order the Commission issued and the
20 depreciation lives, again, in compliance. So to
21 characterize it as a new study, I mean, in some
22 angelic sense I suppose it is, but it's different
23 only, at least according to the witness's testimony,
24 in those particulars.

25 JUDGE WALLIS: Mr. Farrow, did Mr. Owens

02692

1 correctly characterize the document you're referring
2 to?

3 THE WITNESS: Yes, he did.

4 JUDGE WALLIS: Does that satisfy your
5 concerns, Ms. Proctor?

6 MS. PROCTOR: I'm not quite clear.

7 Q. Mr. Farrow, are there more pages to this
8 analysis than this single page? Do you know?

9 A. I think my response was I did not know
10 whether there were more pages to the analysis. I said
11 typically when we do this type of analysis we do not
12 prepare the additional pages. We just basically make
13 the runs and produce the output and we stop it there.
14 We don't go to a whole process of producing the full
15 cost study with full backup documentation. I don't
16 know whether it was done in this particular case or
17 not.

18 MS. PROCTOR:

19 And all I'm asking is that the witness check and
20 verify whether there is more to this than just the
21 single page and if there is just this single page then
22 that to me would satisfy the request.

23 JUDGE WALLIS: I don't think I hear the
24 company objecting to that.

25 MR. OWENS: That's fine.

02693

1 JUDGE WALLIS: Very well. The request is
2 noted.

3 Q. Mr. Farrow, directly in front of this page
4 that you were just referring to on switched access,
5 there's -- I don't think I've ever seen so many page
6 1's. There's a page 1, switched access price
7 worksheet phase 2 amended 5-18-95, and then in front
8 of that there's five more pages with yet another page
9 1 through 5 with the same title, and I was wondering,
10 is that the information that you were also referring
11 to in support of the numbers that you've shown on page
12 2?

13 A. Well, it's my understanding that most of
14 this information in the columns labeled quantity
15 revised proposed rates, proposed rates this filing,
16 annual revenue using those rates, which are some
17 calculated numbers here, but the inputs of these have
18 already been provided to you previously.

19 Q. Thank you, Mr. Farrow, but my question was
20 is this material also that which you were referring to
21 on page 2 as support and as source documentation for
22 the numbers on switched access?

23 A. Yes.

24 Q. Thank you. Now, the numbers that you show
25 here on switched access under the revenue columns,

02694

1 those are not consistent with the numbers that we got
2 from Ms. Wilcox yesterday in her supplemental
3 testimony. Are you aware of that?

4 A. Yeah. I understand she's revised them
5 since this was done, yes.

6 Q. I'm sorry, revised what?

7 A. I understand she has changed the revenue
8 numbers.

9 Q. From her testimony, her supplemental
10 testimony?

11 A. You said you just got something from her
12 yesterday?

13 Q. Yes. And you're now telling me that that's
14 not correct either?

15 A. I'm not telling you which is correct and
16 which is wrong. I'm just telling you she has revised
17 some of these numbers, as I understand it. She's
18 provided some supplemental testimony.

19 Q. Mr. Farrow, we're talking about \$60 million
20 here?

21 A. I don't think the difference is 60 million.

22 Q. I would like to know when we are going to
23 find out from the company what the real number is.

24 MR. OWENS: I'm going to object to the
25 question as being argumentative. If she has a

02695

1 question to put to the witness let her do it.

2 Q. Mr. Farrow, do you have an understanding of
3 what numbers are the correct numbers? Are your
4 correct numbers in column 1?

5 A. No. These numbers are dated 11-14-94, and
6 I am --

7 Q. I'm sorry, what page are you on of what
8 part of this exhibit?

9 A. I'm on page 1 of as a page marked amended
10 5-18-95 and it's the worksheets that you referred to
11 earlier when you asked me if these are the attached
12 sheets.

13 Q. Okay. I'm sorry. I'm on page 2, the page
14 2 that we labeled with Mr. Smith at the beginning of
15 this Exhibit 485?

16 A. Yes.

17 Q. And I was asking about the revenue numbers
18 that are shown on page 2 of your exhibit. Do you have
19 those in front of you now?

20 A. Yes, I do.

21 Q. And perhaps we should back up because maybe
22 you misunderstood my question because we were on
23 different pages.

24 A. I thought we were still back on page 2
25 here.

02696

1 Q. I'm sorry. On page 2 of your exhibit where
2 you show the revenues, are you aware of the fact that
3 the revenues that you show there are not the same as
4 those shown by Dr. Wilcox in the testimony with
5 exhibits that she gave us yesterday?

6 A. Yes.

7 Q. You're aware of that?

8 A. Well, I found out this morning.

9 Q. That they're different?

10 A. Uh-huh.

11 Q. And that her numbers are higher and
12 different?

13 A. I was not told whether they were higher or
14 lower.

15 Q. And were you told which numbers we are
16 supposed to believe?

17 A. I believe, as I said in the beginning, this
18 is a preliminary analysis that we put together here,
19 and we plan on revising this analysis with whatever
20 the latest data that is available. At the time this
21 was put together this was the latest information that
22 was available to us, and I'm pretty sure that it's
23 going to be revised and changed in the future as
24 there's more data available that's later than this
25 date.

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1 MS. PROCTOR: Thank you, Mr. Farrow.

2 JUDGE WALLIS: Ms. Lehtonen.

3 MS. LEHTONEN: No questions.

4 JUDGE WALLIS: Mr. Butler.

5

6 CROSS-EXAMINATION

7 BY MR. BUTLER:

8 Q. Mr. Farrow, you responded to a question
9 from Ms. Proctor to the effect that the revenues shown
10 on page 2 of the analysis for CCLC should have been
11 included under the contribution column. Do you recall
12 that?

13 A. Yes.

14 Q. Would it also be the case that the revenues
15 shown for the residence CALC and the business CALC
16 should also be included under the contribution column?

17 A. Yes.

18 MR. BUTLER: Thank you. No further
19 questions.

20 MR. NICHOLS: I do have a question.

21 JUDGE WALLIS: Mr. Nichols.

22

23 CROSS-EXAMINATION

24 Q. Mr. Farrow, on page 1 of Exhibit 485C,
25 just a followup on this contribution column questions.

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1 If I were to go back and add up all the contributions
2 that are actually listed there, would I come up to the
3 figure, the total figure which is on page 2?

4 A. No. You will not -- you should not come up
5 with that answer. What you should do is you should
6 take the line that says total and then take the
7 revenue minus the TSIC and then you would get the
8 contribution. So there are some numbers that should
9 be in the contribution column that are missing, but
10 they are in the total at the bottom.

11 MR. NICHOLS: Perhaps I could ask at this
12 point and it would end my further questioning on this,
13 since there are several changes like that to this
14 exhibit, at least the first four pages of this
15 exhibit, whether it would be possible for the company
16 to rerun those exhibits so at least those obvious
17 arithmetic problems would not be apparent.

18 MR. OWENS: May I ask perhaps a voir dire
19 question, see if the witness has knowledge of this?
20 It's simply a matter of characterization, I suppose.

21 Mr. Farrow, do you know whether there was
22 any particular intent on the part of the company in not
23 showing the carrier common line charge revenues and the
24 CALC revenues under the contribution column in terms of
25 drawing a conclusion one way or another as to the

02699

1 proper characterization of those revenues?

2 THE WITNESS: No, I don't.

3 MR. OWENS: I will represent to the
4 Commission that because this is an area of some
5 controversy as to what the proper characterization of
6 those items is, the company simply prepared this and
7 attempted to be as neutral as it could in the way it
8 portrayed them. If somebody wants to have those
9 figures inserted in the column so that the numbers
10 foot to the total, we can certainly do that or they
11 could do it.

12 JUDGE WALLIS: I understand that that is
13 requested, and the company has indicated that it would
14 do that.

15 MR. TROTTER: Your Honor, if I could
16 interpose here, there are a number of issues I would
17 take with this particular format of this exhibit. And
18 I've chosen not to because this is the company's
19 portrayal, and I would suggest if intervenors want to
20 produce their own portrayal they're free to do it. I
21 guess I'm making Mr. Owens's argument for the first
22 time, there was a time when we agreed on more things,
23 but I think staff has asked some questions regarding
24 inclusion of some costs, inclusion at 100 percent in
25 certain columns, and I am not going to object to this

02700

1 exhibit if it is understood that that is the company's
2 portrayal. I think from then on it's argument and at
3 this point our witnesses are gone. I can't put in
4 another exhibit and sponsor it. My witnesses are
5 hundreds of thousands of miles away. I think if it
6 goes in it should go in as the company's portrayal,
7 period.

8 JUDGE WALLIS: I'm feeling guilty that it
9 was my request that led to the production of the
10 information but the request did ask for the company's
11 portrayal of the information and I think Mr. Trotter's
12 suggestion is a valid one, that this is the company's
13 portrayal. The basis of the portrayal is clear
14 following the examination of Mr. Farrow, and parties
15 who wish to present additional information or present
16 it in a different manner may do so, in the course of
17 argument.

18 MR. BUTLER: Do I understand that the
19 request will be complied with? I didn't understand
20 that he was asking that the company's portrayal will
21 be changed, only numbers that are consistent with that
22 portrayal be included on this sheet.

23 MR. NICHOLS: I certainly didn't mean to
24 ask such a pregnant question, just that the numbers add
25 up on a piece of paper that we need to respond to that

02701

1 we need to use.

2 MR. TROTTER: It's my understanding that
3 Your Honor that they do add up, that the difference
4 between the revenues and the TSIC is the total
5 contribution.

6 MR. OWENS: The question is footing across
7 or footing down, I think, and I think the witness's
8 testimony is they foot across but not down at least in
9 that contribution column.

10 MR. NICHOLS: Well, I will withdraw my
11 question. If the company doesn't want to provide a
12 document that adds up in the ordinary course of the
13 way one adds up columns then that's fine. I will stop
14 questioning on that.

15 Q. I would like to ask a question that perhaps
16 goes to something of greater substance, at least that
17 I don't understand. On page 2 of Exhibit 485C there's
18 a total column near the bottom. Do you see that?

19 A. There's a line labeled --

20 Q. There's a line?

21 A. Labeled total, yes.

22 Q. And I believe Mr. Trotter asked you some
23 questions about what was represented there; is that
24 correct. Do you recall that?

25 A. Yes.

02702

1 Q. The numbers that I see here -- well, I
2 don't know whether I want to characterize that. Is
3 the contribution number that appears under the
4 contribution column that has as its last digit a 4?

5 A. Yes.

6 Q. That is the difference between the revenue
7 number which is in the first column and the TSIC
8 number which is in the second column; is that correct?

9 A. Yes.

10 MR. NICHOLS: I have no further questions.

11 MR. BUTLER: Can I ask one clarification.

12 JUDGE WALLIS: Mr. Butler.

13 MR. BUTLER: Mr. Farrow, if you were to add
14 the numbers listed under the contribution column would
15 you get the same figure that is listed in the
16 contribution column opposite total?

17 MR. OWENS: It's been asked and answered.

18 MR. BUTLER: Well, I'm confused with we've
19 got what I think is conflicting answers.

20 JUDGE WALLIS: Mr. Farrow?

21 THE WITNESS: No.

22 MR. BUTLER: In order to get that number
23 listed under the total you would have to include in
24 the contribution column those numbers for CCLC and the
25 CALC for residence and business and the equal access

02703

1 charge. Is that correct?

2 THE WITNESS: If you want to add down the
3 column.

4 MR. BUTLER: I renew this request to have
5 this page rerun to have the figures that total the
6 figures opposite total contribution included.

7 MR. TROTTER: Well, Your Honor, it's in the
8 record because he's identified what the amounts are.
9 I still think that this is the company's portrayal.

10 MR. BUTLER: It's not changing the
11 characterization. If we're going to be able to refer
12 to this in a brief it seems to me that it's going to be
13 much easier if we have a document that adds up and
14 doesn't change the company's characterization.
15 Otherwise we've got to include explanations that are
16 unnecessary to avoid confusion.

17 JUDGE WALLIS: Mr. Owens.

18 MR. OWENS: I think we've explored this now
19 for about half an hour or so and I think the
20 explanations are in the transcript, and I don't think
21 any party is going to have the slightest difficulty
22 referencing the discussion we've had to make sure that
23 the significance of these numbers is clear for
24 whatever argument they want to make.

25 JUDGE WALLIS: So the company is indicating

02704

1 that it does not wish to provide that portrayal and
2 because I think the information is readily available I
3 believe that's satisfactory. Is there any further
4 question from counsel to Mr. Farrow? Are there
5 questions for the commissioners.

6 Commissioner Gillis.

7 COMMISSIONER GILLIS: I have one, not to
8 belabor things.

9

10 EXAMINATION

11 BY COMMISSIONER GILLIS:

12 Q. I think it's page 5, that spreadsheet that
13 goes from columns A to P, resident one party flat rate
14 revenue cost analysis.

15 A. Yes. You're referring to the page that has
16 U S WEST Communications Inc. at the top?

17 Q. Right. A through P columns?

18 A. Yes.

19 Q. That column K, annual ASIC, should that be
20 annual TSIC?

21 A. Yes, it should be.

22 Q. Last time we talked to you you weren't able
23 to tell me what the difference of the rate groups are
24 in column C. Did you happen to find out since then?

25 A. Yeah. There are three rate groups. The

02705

1 first one is rural, second one, as I understand it, is
2 -- first one is the smaller in our smallest town and
3 the second is our medium sized towns and the third one
4 is in our large metropolitan areas where most of our
5 customers are.

6 Q. Looking at column J ASIC and the current
7 rates, it doesn't appear there's any particular
8 correlation between the current rates and ASIC and the
9 current structure; is that right? The ASIC is the
10 same all the way down?

11 A. The ASIC, these are using statewide average
12 ASIC costs, yes.

13 Q. So it's not the ASIC for rural, for
14 example, and mid size and city?

15 A. No, it is not, but the data for rural is
16 included in the calculation of the ASIC.

17 Q. And you told me last time that your
18 accounting doesn't allow you to calculate those
19 separate groups, I believe?

20 A. Our SCM model doesn't allow us to -- I
21 should say our switch usage model doesn't allow us to
22 build it calculated in that way, yes.

23 Q. I understand there's going to be more
24 information coming that you did say from your backup
25 materials at least you would be able to to provide

02706

1 cost specific information for zone one and zone two in
2 your proposing, right?

3 A. I hope so.

4 Q. You're working on that?

5 A. Yes.

6 COMMISSIONER GILLIS: That's all.

7 JUDGE WALLIS: Mr. Owens. Excuse me.

8 Commissioner Hemstad.

9

10 EXAMINATION

11 BY COMMISSIONER HEMSTAD:

12 Q. Maybe this is belaboring the point that has
13 already been pursued, but that triggers a question.
14 The company is proposing rates for zone one and zone
15 two of \$21 and \$26 or there approximately?

16 A. Yes, and we have provided cost support for
17 those.

18 Q. And you have cost support for that
19 difference?

20 A. That cost support what I was explaining in
21 those cost studies we use statewide average usage
22 costs in those cost studies but for the loop itself we
23 did do cost studies specific to zone one and zone two
24 in those studies. We have the ability in some of our
25 models to do it that way and others we don't.

02707

1 COMMISSIONER HEMSTAD: I will let that go
2 with that answer.

3 MR. OWENS: May I have just a moment, Your
4 Honor?

5 (Discussion off the record.)

6 MR. OWENS: Thank you, Your Honor. Ready
7 to proceed.

8

9 REDIRECT EXAMINATION

10 BY MR. OWENS:

11 Q. Counsel for the Commission staff asked you
12 with regard to Exhibit 485C, page 1, whether or not
13 the negative contribution shown in the contribution
14 column existed by virtue of the assignment of all of
15 the loop costs to residence service, and you answered
16 yes. Do you recall that?

17 A. Yes.

18 Q. In answering that question yes, did you
19 understand his question to refer only to loop costs
20 used to provide residence service as opposed to all
21 loop costs including business loop costs?

22 A. Yes. I assumed it meant only the loop cost
23 associated with providing service to residence.

24 Q. And public counsel asked you whether or not
25 in doing your study you assumed any efficiencies in

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1 terms of the amount of contribution that you came up.

2 Do you recall that?

3 A. Yes.

4 Q. Are your studies done as far as you are
5 able to on a true TS LRIC basis?

6 A. Yes.

7 Q. And does that basis assume anything
8 about --

9 A. Well, it does assume efficiency when you do
10 a least cost type of study so especially in the loop
11 we assume that least cost mix of facilities in the
12 loop.

13 Q. Finally, Commissioners Gillis and Hemstad
14 asked you some questions about the issue of costs
15 specific to the rate groups that appear on the
16 spreadsheet that you were discussing of rate groups 1
17 and 2 and 3. Are you aware of Exhibit 337C that's
18 attached to your rebuttal testimony? It's entitled
19 current residence rates versus costs?

20 A. Yes.

21 Q. Does that include any comparison of current
22 12 FR rates in those rate groups with ASIC and ADSRC
23 costs?

24 A. Yes, it does.

25 Q. Just to clarify, I believe you indicated

02709

1 that there were some costs that you were capable of
2 deaveraging and others that you weren't. Could you
3 explain how these different average costs, that is,
4 ASIC and ADSRC, were calculated for the three rate
5 groups describing which costs you could and which
6 costs you couldn't deaverage?

7 A. Yeah. If you could turn to my Exhibit in
8 my supplemental testimony, and I'm calling it BEF-3.
9 I don't have the specific number on it.

10 Q. Should be 336, I believe, C.

11 JUDGE WALLIS: What is the other
12 description in the document?

13 THE WITNESS: The document is labeled
14 results from a Washington residence access line 1995
15 long-run incremental costs revised, and it's page 1 of
16 17.

17 JUDGE WALLIS: Is that 341C?

18 MR. OWENS: 341C, I'm sorry. If you take a
19 look at this exhibit the costs that we are able to
20 calculate on a zone basis are the outside plant loop
21 and the drop wire. The NTS-COE B and C directory
22 listings and the set up and minute of use costs we were
23 unable to calculate those on a zone basis.

24 Q. Perhaps we could talk in addition to zones
25 about the rate groups. Do you recall that?

02710

1 A. Rate groups, yes.

2 Q. And in this comparison in Exhibit 337C,
3 it differentiates the rates and the costs by rate
4 group, were the elements that you used to come up with
5 the costs the same as you just described in your
6 testimony about the different zones or were they
7 different?

8 A. In the testimony that --

9 Q. That you just gave.

10 A. I didn't quite understand you.

11 Q. I'm sorry. Were you answering --

12 A. I pulled out this exhibit, the reason I
13 pulled this out was to show the different costs that
14 are included in residence access line costs and to
15 point out which ones that we can calculate on the zone
16 or on a rate group basis versus the ones that we could
17 not calculate on that basis. There are other examples
18 in here. Fact is, could probably go to my direct
19 testimony where I have actually -- let's see. Turn to
20 BEF-8 of my direct testimony.

21 Q. I believe that's Exhibit C90.

22 A. Turn to pages 10 and 11. BEF-8, this is
23 the exhibit that has at the top it says page 10, 1FR
24 residence line zone one. And page 11 shows zone two.

25 Q. Mr. Farrow, do you have BEF-4 from your

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1 rebuttal testimony?

2 A. Yes, I do.

3 Q. And that has the three rate groups as
4 opposed to the zones?

5 A. Yeah, but I don't have the detail on those
6 that I have here. I'm just using this as an example
7 to show what information we do have available on a
8 rate group or a zone basis and what information we
9 don't have available on that basis.

10 Q. So do I understand, then, that the type of
11 information that's available on a rate group basis in
12 terms of determining your costs is of the same
13 character as you've indicated available on the zone
14 basis?

15 A. That's correct.

16 Q. Thank you.

17 MR. OWENS: That's all.

18 JUDGE WALLIS: Is there anything further?

19 MS. PROCTOR: Your Honor, could I just ask a
20 clarification from the witness?

21 On page 2 of Exhibit 485C, in the source
22 there's no entry opposite DS1 and DS3. Do you know
23 what the source of those numbers was?

24 THE WITNESS: This was a part of an
25 information request. I would have to look it up and

02712

1 provide it.

2 MS. PROCTOR: If you could do that without
3 too much trouble I would appreciate it.

4 MR. SHAW: We can discuss that off the
5 record with counsel.

6 JUDGE WALLIS: Fine. Commissioner Gillis.

7 COMMISSIONER GILLIS: Just to be sure that
8 I understand. The exhibits that Mr. Owens took you
9 through that do make some comparison between zone one
10 and zone two, I only note ADSRC comparisons. I don't
11 see any ASIC comparisons.

12 THE WITNESS: I was using these to show
13 that we do have a breakdown by zone and, you're right,
14 these pages do not show ASIC.

15 COMMISSIONER GILLIS: In your backup
16 material do you think you might have it?

17 THE WITNESS: Oh, yes. This information is
18 in the backup materials.

19 COMMISSIONER GILLIS: And you already had
20 a bench request for those?

21 THE WITNESS: We did?

22 COMMISSIONER GILLIS: Last time.

23 THE WITNESS: Okay.

24 JUDGE WALLIS: Anything further of the
25 witness? It appears that there is not. Mr. Farrow, I

02713

1 think you can go home this time. Been delightful
2 having you here again and let's take a 10-minute
3 recess while the next witness steps forward.

4 (Recess.)

5 JUDGE WALLIS: Let's be back on record,
6 please, following a brief recess. The company has
7 called Dr. Richard Emmerson back to the stand.

8 Dr. Emmerson, I will merely acknowledge that
9 you've previously been sworn in this matter, and I will
10 note that Exhibits 360T and 361 have been received in
11 evidence, and ask if the company has anything further
12 of the witness.

13 Whereupon,

14 RICHARD EMMERSON, Phd,
15 having been previously duly sworn, was called as a
16 witness herein and was examined and testified
17 further as follows:

18 MR. SHAW: No, Your Honor. My recollection
19 is that AT&T had completed their cross and Dr.
20 Emmerson is available for examination from other
21 parties.

22 JUDGE WALLIS: Yes, Mr. Waggoner had
23 completed his cross.

24

25

CROSS-EXAMINATION

1

2 BY MR. SMITH:

3 Q. Good afternoon, Dr. Emmerson.

4 A. Good afternoon, Mr. Smith.

5 Q. You testified I guess Friday that you have
6 assisted U S WEST Communications in the area of costs
7 for about ten years now; is that correct?

8 A. Yes, in one form or another predominantly
9 through training.

10 Q. And one of the terms we heard in this case
11 last week was the term cost object. Can you explain
12 what a cost object is?

13 A. Yes. A cost object is any portion or
14 segment of a business to which one wishes to assign or
15 identify costs. That could be a geographical area.
16 It could be a product. It could be a basic network
17 function, for example.

18 Q. And for what purpose does the company
19 define and estimate costs for cost objects?

20 A. Well, for many purposes. For example,
21 revenue requirements are based on the cost object
22 which we would call the total company. Most often the
23 TS LRIC cost studies are performed for service or
24 groups of service in order to establish competitive
25 safeguards, namely, revenue floors in the form of

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1 satisfying imputation requirements and avoiding
2 subsidies, cross subsidies.

3 Q. From your definition, would I be correct to
4 say that the loop could be considered a cost object?

5 A. Yes.

6 Q. And do you consider the loop to be a cost
7 object?

8 A. Yes.

9 Q. As a general matter should the cost of
10 inputs used to recover multiple products be recovered
11 in prices of products to the extent markets would
12 permit it?

13 A. Yes.

14 Q. Is the local exchange loop an input used in
15 the production of several products such as local and
16 toll calls?

17 A. It's used for local and toll calls but it
18 would not be, by implication of your question, a
19 shared cost of local and toll calls. The cost of the
20 loop would be identified as such, and all other
21 questions would pertain to the recovery of that cost
22 and that is a pricing matter.

23 Q. So if I understood what you just said, the
24 issue of loop costs recovery is not a question of cost
25 assignment per se but a question of whether markets

02716

1 may or may not allow that cost to be recovered or
2 which markets will?

3 A. Certainly what you just said is correct.
4 There certainly is a very important issue as to how the
5 costs of the loop may be recovered, particularly in a
6 competitive environment. Competition puts many
7 restrictions on how one is able to recover costs, but
8 my point was that the cost of the loop is what it is,
9 and it's rather unambiguously unidentifiable, but
10 nevertheless it must be recovered. Historically as I
11 said in my testimony it has been recovered from a
12 variety of sources. In the future it will need to be
13 recovered through either end user charges or external
14 subsidies in order to be compatible with competition.

15 Q. Dr. Emmerson, are you familiar with the
16 Commission's sixth supplemental order in what we refer
17 to as the interconnection case that was recently
18 concluded?

19 A. No, I am not. I am aware there is an order
20 but I am not familiar with it.

21 Q. Do you consider the loop to be a service
22 specific fixed cost of local exchange service?

23 A. No. Depending on what one calls volume
24 determines what a volume sensitive cost is. For
25 example, volume could measure number of loops. In

02717

1 certain services that would be held a volume of
2 service measured. In that circumstance it would be a
3 volume sensitive cost. So I would not call it a
4 product specific fixed cost.

5 Q. In preparing your testimony in this case
6 did you conduct any study of telecommunications
7 markets in Washington for the company?

8 A. No, I did not.

9 Q. Did you examine the Washington statutes and
10 rules pertaining to the regulatory treatment of
11 competitive telecommunications services?

12 A. I reviewed the rules. I didn't study them
13 with that particular subject matter in mind.

14 Q. Do you have any knowledge of your own as to
15 why the company has not filed for competitive
16 classifications for services which it believes are
17 subject to effective competition?

18 A. No, I don't have any knowledge as to
19 whether or why the company has made such application.

20 Q. On page 5, beginning on page 5, line 16 of
21 your rebuttal testimony, you say that the forward
22 looking economic life should be used in incremental
23 cost studies. Do you see that testimony?

24 A. Yes, I do.

25 Q. Do you have any direct knowledge that the

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1 prescribed lives used in Washington today are not the
2 best estimates of economic lives for U S WEST's
3 Washington's plant?

4 A. I do not have any direct knowledge. I
5 certainly have knowledge of the fact that they are not
6 equal to the economic lives which were proposed by U S
7 WEST.

8 Q. If I were to tell you that the statewide
9 average embedded loop costs for Washington were
10 identified as being \$11.77 per month, excluding
11 overheads, would that figure surprise you?

12 A. I'm sorry, that figure is exclusive of
13 what?

14 Q. It's as defined in what will be Exhibit 3
15 Al titled loop dreams. Are you familiar with that?

16 A. No, but if I could review it I think I can
17 answer the question more directly, unless you can tell
18 me the component that are included in that cost. For
19 example, beyond the loop what might be included.

20 Q. It would include the outside plant loop,
21 the NTS-COE and the drop?

22 A. It would surprise me a little. That sounds
23 low but then I'm not as familiar with the state of
24 Washington and its population distribution as I would
25 need to be to say anything more than that.

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1 Q. Are there any circumstances where the
2 Commission might want to refer to embedded costs in
3 considering pricing for services?

4 A. Yes, but I think the circumstances are past
5 circumstances rather than present circumstances.
6 Certainly in the traditional setting of rates in a
7 monopoly environment and largely with the objective of
8 setting rates to satisfy public policy objectives as
9 opposed to being compatible with competition,
10 regulatory accounting and embedded or historical costs
11 were certainly relevant. I do not believe they're
12 relevant or even sustainable today, that is, prices
13 based on such costs would not be sustainable today in
14 a competitive environment. Certainly would not be
15 consistent with the competitive goals that are
16 evolving.

17 Q. Page 7 of your rebuttal testimony you talk
18 about the Smith versus Illinois case which led to the
19 practice of using regulatory accounting for
20 jurisdictional separations?

21 A. Yes.

22 Q. Is it correct the company has filed for
23 additional revenues in this case based on the embedded
24 costs recorded on the regulatory books of the company?

25 A. They may have, but I'm not familiar with

02720

1 that aspect of the case.

2 Q. And do you know whether the amount of
3 revenues and expenses being discussed in this case was
4 calculated by subjecting total Washington revenues and
5 expenses to the jurisdictional allocation process?

6 A. I am not familiar, as I said, with that
7 aspect of this case, I'm sorry.

8 Q. Same page, beginning on line 19 you
9 indicate that regulatory accounting is not the basis
10 for incremental cost analysis and does not substitute
11 for costs as they would be reflected in a competitive
12 environment. Has any witness in this case said that
13 regulatory accounting should be the basis for
14 incremental cost analysis?

15 A. Yes. Mr. Dunkel has at least taken
16 portions of what are regulatory accounting practices
17 and suggested that they be used in the development of
18 incremental costs.

19 Q. Has any witness for staff done so?

20 A. I don't recall that that's the case.

21 Q. On page 9 of your testimony you quote Dr.
22 Baumol as saying, "for a firm that is unregulated and
23 whose objective is maximization of profits this cross
24 subsidy story makes no sense." Are you familiar with
25 that portion of your testimony?

02721

1 A. Yes, I am.

2 Q. What is the cross-subsidization story
3 referred to in that sentence?

4 A. The fact that one would use revenues or
5 contributions from monopoly services to subsidize
6 competitive services.

7 Q. And are you suggesting by that quotation
8 from Dr. Baumol that he believes that residential
9 services is a service being cross subsidized?

10 A. No. This is a statement regarding economic
11 principles not pertaining directly to any specific
12 service.

13 Q. And Dr. Baumol's discussion is related to a
14 firm having monopoly -- having a monopoly service or
15 services where prices were already set at profit
16 maximizing levels; is that correct?

17 A. Well, the profits need not have been set at
18 profit maximizing levels in order for the statement to
19 be true, and I don't believe the statement was
20 directly related to that. Certainly when he made
21 reference to a profit maximizing firm he was making
22 reference to a firm whose prices were set equal to the
23 profit maximizing levels.

24 Q. Do you, Dr. Emmerson, have before you
25 what's been marked for identification as Exhibit 362?

02722

1 A. Yes, I do.

2 Q. And do you recognize that as the
3 publication that you quote in your testimony on page
4 9?

5 A. It is the same.

6 Q. And you quote from page 112, and this
7 exhibit contains that page and the following page 113;
8 is that correct?

9 A. That's correct.

10 Q. And am I correct that on that page 113 Dr.
11 Baumol notes that government regulation in fact
12 imposes an overall ceiling on company profits such
13 that the possibility of using monopoly service
14 revenues to cross subsidize competitive services
15 cannot be ruled out a priori?

16 A. That's true, and that's in reference to
17 either a revenues or earnings constraint, and that is
18 precisely why price floors are established as to avoid
19 that form of subsidy.

20 MR. SMITH: Your Honor, I would move for
21 admission of Exhibit 362.

22 MR. SHAW: No objection.

23 JUDGE WALLIS: 362 is received.

24 (Admitted Exhibit 362.)

25 Q. Dr. Emmerson, you also indicated on Friday

02723

1 in your surrebuttal that the benchmark cost model
2 would be the wrong cost standard to use for U S WEST?

3 A. For purpose of establishing competitive
4 safeguards that would be correct. One should use the
5 costs of the firm providing the service. Benchmark
6 cost model is more general. Certainly Mr. Copeland
7 can speak to that issue.

8 Q. Do you think the benchmark cost model might
9 be useful to the Commission for other purposes?

10 A. Well, I guess design purpose was to try to
11 avoid the use of proprietary information in
12 establishing a basis for funding universal service
13 policies, and for that purpose it may be appropriate.
14 I wasn't suggesting that it was inappropriate for all
15 purposes. I was suggesting it was inappropriate for
16 the establishment of price floors and competitive
17 safeguards.

18 Q. With regard to the use of engineering
19 intervals in cost studies?

20 A. Yes.

21 Q. I believe you spoke to this on Friday night
22 in reference to Mr. Spinks's testimony?

23 A. Yes.

24 Q. Did you understand Mr. Spinks's testimony
25 to require the use of engineering intervals in studies

02724

1 or to require consistency between the engineering
2 interval and the study period?

3 A. I understood it to be the former. But I
4 would also suggest that my answer would remain the
5 same under both interpretations.

6 Q. Why not use the engineering interval for
7 the cost study period?

8 A. Primarily because of the L in TS LRIC, the
9 long run. A long run cost study should not be
10 truncated based on an engineering practice or an
11 engineering interval. It should look to all costs
12 caused by the cost object, even those which may occur
13 outside of any particular engineering interval.

14 Q. From that answer, I take it you're treating
15 the study period as longer than the engineering
16 interval?

17 A. Well, sometimes the word study period is
18 used to refer to the period from which one gets data.
19 In other cases the study period is used to refer to
20 whether the study is long run in nature or something
21 less than long run in nature, and very typically
22 engineering intervals won't match either of those
23 interpretations. I don't know that that was
24 responsive to the question, but if you could ask the
25 question again perhaps I can be more responsive.

02725

1 Q. Are you assuming in your question or in
2 your answer that the study period was longer than the
3 engineering interval?

4 A. It may be longer or shorter. There's no
5 uniform relationship.

6 Q. And whether it's longer or shorter doesn't
7 change your testimony. Is that what I understood you
8 to say?

9 A. That's correct. Again, the engineering
10 interval, as I understand it is the period over which
11 one engineers and relieves their plant, and one would
12 normally want to look out over several engineering
13 intervals in order to capture long run costs, because
14 one would certainly want to take account of any
15 advancement of construction or any additional sizing
16 of future construction that would be necessary to
17 accommodate the increment of output being studied and
18 one can only do that if one looks at least past a
19 single engineering interval.

20 Q. Are you familiar with how long the study
21 period was in the company's loop cost study?

22 A. I didn't review the loop cost studies or
23 any of the Washington state cost studies specifically.

24 MR. SMITH: Thank you. That's all I have.

25

1 CROSS-EXAMINATION

2 BY MR. TROTTER:

3 Q. Dr. Emmerson, I would like to refer you to
4 Exhibit 361 where you discuss capacity issues, and on
5 page 4 of that exhibit the answer beginning on line 20
6 you refer to another reason for having spare capacity
7 relates to wires which may deteriorate over time. Do
8 you see that?

9 A. Yes. More generally it pertains to
10 survivor characteristics.

11 Q. With respect to deterioration, do you know
12 what percent on average wires in a particular -- wires
13 in the company's service territory are subject to
14 deterioration?

15 A. No, but engineers typically maintain what
16 they call survivor curves with respect to various
17 categories of plant.

18 Q. Are we talking 2 to 3 percent here or --

19 A. I don't know.

20 Q. You also talk on page 5 about -- your
21 answer beginning on line 20 about sporadic use. Do
22 you know what percentage of the loop plant reflects
23 that characteristic?

24 A. I don't know the numerical values. I know
25 that loop plant is subject to sporadic use.

02727

1 Q. For each of those you didn't discuss with
2 the company with respect to these type of loop plants,
3 did you discuss with the company these two types of
4 characteristics that lead to spare capacity and see
5 what their experience was in their loop plant?

6 A. No, I did no qualitative analysis in this
7 regard.

8 Q. On page 3 of the exhibit, line 2, you say
9 the average amount of spare capacity expected to be on
10 hand at any point in time is one half of one unit of
11 the average capacity addition regardless of the volume
12 of output. Do you see that?

13 A. Yes, I do.

14 Q. And by that document that if the average
15 capacity additions were 1100 units that on average the
16 amount of spare capacity expected to be on hand at any
17 one time would be one half that amount or 550 units?

18 A. Yes. If one were to add 100 units at a
19 time and one were then to wait until that capacity is
20 fully utilized then at another 100 units, if one were
21 to go out and simply sample the spare capacity on one
22 hand at any one time one might get near zero, near
23 all, half the expected value of that amount on hand
24 would be one half of a capacity addition. Exactly
25 like management accountants treat inventory

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1 calculations.

2 Q. Turn to page 17 and 18 of your testimony.

3 At the bottom of page 17 you indicate that for broadly

4 defined services such as 1FR the appropriate

5 measurement of the spare capacity cost to include an

6 incremental cost study utilizes actual figure factors.

7 Do you see that?

8 A. Yes.

9 Q. Do you know what the actual fill factor is
10 for U S WEST in the test year or in any other period?

11 A. No, I do not.

12 Q. And by actual do you mean the fill factor
13 that was experienced during the historical period or
14 as it exists at a point in time?

15 A. Yes, or is expected to be experienced in
16 the future, as well in a forward looking cost study it
17 would be the last of those.

18 Q. On page 25 of your testimony you indicate
19 that the -- let's start with a different question.
20 On lines 5 through 14 you refer to an example used by
21 Mr. Dunkel in a response to a data request regarding
22 an apartment building and you characterize his
23 illustration as a pricing exercise not a costing
24 exercise; is that correct?

25 A. That's correct.

1 Q. Did you agree with his response to the
2 extent of pricing exercise?

3 A. I didn't necessarily agree or disagree with
4 it. I don't have knowledge of how apartment buildings
5 are priced, but it certainly is an example where one
6 would engage in the practice of what I call target
7 pricing.

8 Q. Turn to page 19 of your testimony.

9 A. Yes, I have it.

10 Q. And I guess starting at the bottom of the
11 prior page you indicate in the discussion of ASIC and
12 ADSRC that U S WEST has been very clear -- quote, very
13 clear in how these two distinct numbers are to be
14 used, unquote, and you say ASIC is to be used as a
15 price floor and ADSRC is a target price and not a
16 price floor?

17 A. That's correct.

18 Q. Did you review U S WEST's testimony on this
19 particular issue?

20 A. Yes. That was the basis for my having
21 concluded that I thought they were quite clear on that
22 matter.

23 Q. So when Mr. Scott on page 46 of his direct
24 said, "for most services the LRIC as measured by ADSRC
25 represents the appropriate price floor," you think

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1 that's a clear statement of the concept that you're --

2 A. I'm sorry, I don't have that testimony
3 before me. Whose testimony again?

4 Q. Mr. Scott.

5 A. I don't believe I have that testimony.

6 Q. Let me just quote it again. "For most
7 services the LRIC as measured by the ADSRC represents
8 the appropriate price floor."

9 A. I don't recall having seen that quote at
10 all. In fact I'm not sure I even saw Mr. Scott's
11 testimony. I don't have any comment on that.

12 Q. So when you said in your testimony at page
13 18, line 24 that U S WEST has been very clear in how
14 these two distinct numbers ASIC and ADSRC are to be
15 used you did not have in mind the testimony I just
16 quoted?

17 A. No. I specifically was referring to Mr.
18 Farrow's testimony and some of the criticisms of that
19 testimony by Mr. Wood.

20 Q. And was the testimony that I quoted you,
21 assuming I quoted it correctly, clear on the issue of
22 the difference between ASIC and ADSRC?

23 A. No, not taken out of context.

24 Q. But your focus was Mr. Farrow and not other
25 witnesses?

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1 A. That's correct.

2 Q. If a telephone pole -- two telephone poles
3 are holding up cables between two interoffice
4 facilities, would that be an example of a shared
5 residual cost?

6 A. You would have to be more specific about
7 the cost objects for me to answer that question.

8 Q. A shared residual cost of basic exchange
9 service?

10 A. It may or may not be. Depending on whether
11 or not the facilities are considered to exhaust. If
12 the facilities are considered to exhaust then the
13 capacity cost would be included in the direct cost not
14 in the shared residual cost. If it were --

15 Q. I'm talking about the telephone pole at
16 this point.

17 A. Yes. And again, I'm not an engineer but my
18 understanding is poles can, quote, exhaust meaning
19 that one needs to have larger poles to accommodate
20 heavier cables and that will perhaps pull us closer
21 together. By exhaust I simply mean is there a
22 capacity constraint.

23 Q. Let's assume there is not. Then would it
24 be in shared residual?

25 A. If there is not then it would be in shared

02732

1 residual. If it does exhaust the capacity cost would
2 be indirect and only the spare capacity other than
3 administrative spare would be in the shared residual.

4 Q. Now, in your testimony you referred to the
5 Smith V Illinois Bell case and Commission counsel
6 asked you a couple of questions about that?

7 A. Right.

8 Q. And you are discussing that from your
9 perspective as an economist not as an attorney; is
10 that correct?

11 A. Absolutely.

12 MR. TROTTER: Those are all my questions.
13 Thank you.

14 JUDGE WALLIS: Further questions from
15 counsel? Mr. Nichols.

16 MR. HARLOW: Your Honor, I do have a cross
17 although the length of it will vary considerably
18 depending on your ruling on my objection to the oral
19 surrebuttal Friday night which was based on two
20 grounds. Just very briefly the first was that the
21 surrebuttal responded to an imputation methodology
22 that Ms. Murray filed in August and there have been --
23 should have been filed as written testimony in
24 December, and secondly that it raised issues that had
25 been decided by the Commission in July and U S WEST

02733

1 has appealed those issues and so it should be reserved
2 for the courts. I have obtained copies of the
3 transcript and can specify the testimony that my
4 motion addresses. That would be the question on page
5 1995 beginning at line 8 and ending at line 14, and
6 the questions and answers beginning on page 1996, line
7 3 through 1999, line 10. And as I recall you had
8 reserved ruling on that objection. I don't know
9 whether there was an intention to rule on it at this
10 time or not.

11 JUDGE WALLIS: We have reviewed the
12 questions and answers and the argument of counsel
13 as set out in the transcript and believe that the
14 objection should be denied.

15

16 CROSS-EXAMINATION

17 BY MR. HARLOW:

18 Q. Dr. Emmerson, it's my understanding that
19 you have reviewed all of U S WEST's cost studies that
20 have been used to support this general rate filing?

21 A. No, I have not.

22 Q. Which ones have you not reviewed?

23 A. I've reviewed none of the cost studies.

24 Q. Are you familiar with cost study
25 methodologies?

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1 A. Yes.

2 Q. But I take it you're not familiar with the
3 specific studies themselves?

4 A. That's correct.

5 Q. Is there one particular U S WEST witness
6 that's familiar with all of them or do different
7 witnesses have responsibility for different cost
8 studies?

9 A. Mr. Farrow would be the closest to general
10 familiarity.

11 Q. Can you explain the difference -- strike
12 that. In your oral surrebuttal you talked about
13 counting toll and operator service revenues towards
14 support of the U S WEST pay phone. Do you recall that?

15 A. Yes, I do.

16 Q. Does U S WEST have to place the pay phone
17 itself to get operator service revenues?

18 A. No, but certainly they would need to place
19 the phone to control which operator service revenues
20 would be selected.

21 Q. And otherwise they would have to compete
22 with the pay phone provider itself to obtain the
23 operator service traffic for the toll traffic?

24 A. I'm not familiar with whether or not pay
25 phone providers also supply operator services so I

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1 don't know that the answer to that question.

2 Q. Are you familiar with whether or not a pay
3 phone provider could select U S WEST as its toll
4 carrier?

5 A. I would assume there's no prohibition on
6 that selection. However, I would say that's also not
7 relevant to the point I was trying to make when I
8 suggested that all revenues should be included in an
9 imputation test.

10 Q. Well, the Commission will determine the
11 relevance. Are you familiar with operator service
12 providers such as U S Long Distance, International
13 Pacific, Fone America? Have you heard of some of
14 these?

15 A. No. I've heard of them but not familiar
16 with them.

17 Q. Do you know if Encore provides operator
18 services to pay phone providers?

19 A. I do not.

20 Q. Basically U S WEST when it places a pay
21 phone obtains toll and operator service revenues
22 because U S WEST has decided to bundle those services
23 with its pay phone services; isn't that correct?

24 A. No. It simply receives those because it
25 has the site. Whomever has the site receives the

02736

1 revenue from that site with respect to any services it
2 may sell whether they were their own services or
3 others.

4 Q. Are you aware of any requirement that
5 requires U S WEST to provide the toll and operator
6 service to the pay phones that it provides?

7 A. I am not aware of that requirement.

8 Q. And in fact with regard to interLATA calls,
9 U S WEST does not provide the toll services to its pay
10 phones; isn't that correct?

11 MR. SHAW: I will object. The question is
12 misleading. That's prohibited as a matter of law.

13 MR. HARLOW: I wasn't asking the reasons.
14 I'm simply asking for the facts.

15 JUDGE WALLIS: The witness may respond.

16 A. I don't know.

17 MR. HARLOW: I think Mr. Shaw has answered
18 the question for you.

19 Q. Mr. Farrow referred to the nine cost
20 principles and I asked him whether you had worked with
21 Terry Murray on those. Do you recall that?

22 A. Yes, I do.

23 Q. In fact wasn't she central to the drafting
24 of those nine cost principles in California?

25 A. Yes. She, in conjunction with others,

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1 myself included, drafted those principles.

2 MR. HARLOW: That's all the questions I
3 have, Mr. Emmerson. Thank you.

4 A. You're welcome.

5 JUDGE WALLIS: Mr. Nichols.

6

7 CROSS-EXAMINATION

8 BY MR. NICHOLS:

9 Q. Dr. Emmerson, I just have a few questions
10 to clarify the extent of your role in oversight or
11 involvement in general with U S WEST's cost studies in
12 this docket. I understand from your oral surrebuttal
13 of January 12th I believe that you were retained by U S
14 WEST to review the cost studies of that company; is
15 that correct?

16 A. Yes, and as I said in that response that
17 was with respect to other jurisdictions. I was not
18 retained to review the Washington cost studies in this
19 case.

20 Q. And you haven't reviewed those cost
21 studies?

22 A. That's correct.

23 Q. When were you retained by U S WEST to
24 perform that function?

25 A. That function being reviewing of cost

02738

1 studies?

2 Q. Reviewing of cost studies in general by the
3 company.

4 A. It would be many, many months ago, perhaps
5 up to a year ago. I'm not certain.

6 Q. Did you have any involvement at all in any
7 of the testimonies submitted in this docket other than
8 your own?

9 A. No.

10 Q. Did you have any -- were you asked to or
11 did you review any of the work papers, data requests
12 responses of U S WEST with regard to their cost
13 studies in this docket?

14 A. None other than my own.

15 Q. Are you aware of the or were you made aware
16 of the existence of the ninth supplemental order of
17 the Commission in this docket wherein the Commission
18 expressed some concerns about cost studies and
19 provided for the submission of supplemental testimony
20 on December 15 on costing methodology?

21 A. I believe I only had the fourth and sixth
22 supplemental orders. I don't recall the ninth, no.

23 Q. So no one from the company supplied you the
24 ninth supplemental order dated October 19, 1995?

25 A. They may have but I don't recognize that

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1 name.

2 Q. The one I have in mind did address the
3 Commission's concerns and mentioned topics like
4 wanting to have a transparent, rational, stable,
5 consistent and understandable costing approach. Do you
6 recall that?

7 A. I do recall words to that effect, which may
8 or may not have been in conjunction with that order.
9 I just don't recognize the name of the order.

10 Q. So you just don't recall that matter in
11 terms of its particularity?

12 A. No, but I certainly am aware of the desire
13 for consistent, transparent, et cetera, cost studies.

14 Q. Did U S WEST ask you to perform any
15 additional analysis or review of its cost studies
16 submitted in this docket --

17 A. No.

18 Q. -- as a result of that order requesting
19 transparent, rational, stable, consistent and
20 understandable costing methodologies?

21 A. No, or if they did I was unavailable for
22 that task so I did nothing on their behalf.

23 Q. So you have done nothing on U S WEST's
24 behalf with regard to, shall I say, reviewing or
25 auditing either their costing methodology or the actual

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1 cost studies in this docket really before or after the
2 October order of this Commission; is that correct?

3 A. That's not quite correct because many of
4 U S WEST's methodologies are in fact region wide and I
5 was reviewing those, not with respect to any particular
6 jurisdiction, but I would say I was not asked to review
7 anything that was specific or unique to Washington.

8 Q. So you didn't even review those cost
9 studies to see if they in fact did follow the
10 methodologies that U S WEST was following generally;
11 is that correct?

12 A. I reviewed the methodologies. I did not
13 review the studies.

14 Q. Did you have any involvement in the
15 preparation or review of Mr. Farrow's Exhibit 485C that
16 we discussed this morning which showed results of cost
17 study information and a bunch of work papers?

18 A. No. I had no involvement.

19 Q. To your knowledge, has U S WEST made any
20 changes in its costing methodology as pertains to the
21 Washington jurisdiction since the Commission's ninth
22 supplemental order in October?

23 A. Well, I'm only familiar with the
24 accommodation of the Commission's specific requests or
25 requirements, but I'm not familiar with any changes

02741

1 that may have been made in direct response to that
2 order.

3 Q. In your oral surrebuttal testimony on the
4 12th you proffered several criticisms, I will put it,
5 and you tell me if that's correct, with regard to U S
6 WEST's costing -- the support for U S WEST's costing
7 studies as presented in this docket; is that correct?

8 A. Yes. I characterize them as areas that I
9 would recommend improvement with respect to.

10 Q. And when did you give the Commission your
11 opinion that these were areas that required improvement
12 in this proceeding?

13 A. Friday. I'm sorry, maybe I misunderstood
14 you.

15 Q. I'm sorry. I misspoke. When did you tell
16 U S WEST about those criticisms of their costing
17 support and general work paper production as regards
18 to their cost studies in this docket?

19 A. It would have been after having testified
20 in Iowa and prior to testifying here which would have
21 been over the last week.

22 Q. To your knowledge, have any changes been
23 made in U S WEST's cost supporting information in this
24 docket as a result of your criticisms?

25 A. I'm sure they would not have had time to

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1 make any changes. I don't expect that there would
2 have been any by now.

3 Q. Thank you.

4 MR. NICHOLS: I have no further questions.

5 JUDGE WALLIS: Other questions from
6 counsel?

7

8 CROSS-EXAMINATION

9 BY MS. PROCTOR:

10 Q. Dr. Emmerson, I'm Susan Proctor from AT&T.

11 A. Good afternoon.

12 Q. Were you aware that U S WEST responded --
13 let me back up. You're probably not familiar with the
14 data requests in this case. Were you aware that U S
15 WEST is considering and has at least in Wyoming
16 changed its methodology on how it handles spare
17 capacity?

18 A. No. I am aware in general that with the
19 change in the portrayal of costs broken down into
20 finer categories, that is, the volume sensitive,
21 volume insensitive, et cetera, that the spare capacity
22 was more carefully sorted out but I am not aware of
23 anything that's specific to Wyoming.

24 Q. And therefore you would not know whether in
25 the Washington studies U S WEST had treated spare

02743

1 capacity in the same way that it did in Wyoming or
2 differently?

3 A. I would not know.

4 JUDGE WALLIS: Anything further from
5 counsel? Commissioners?

6

7

EXAMINATION

8 BY COMMISSIONER HEMSTAD:

9 Q. The company is proposing a residential
10 pricing of \$21 and \$26 in two zones. Do you have a
11 figure for -- it's in the record of course -- as to
12 what the company is proposing for pricing for single
13 business lines in those two areas?

14 A. I'm sorry, I don't know.

15 Q. Let's for this purpose take a figure. Say
16 the price for single business line is \$30, proposed to
17 be \$30. Do you have any opinion what the price would
18 be for a single business line, say, in zone one if
19 there were a robustly competitive market for that
20 service?

21 A. No. And the reason for that is that we
22 have only just now begun to experience real local
23 competition in the sense of alternative providers of
24 local telephone services entering into what were
25 previously franchise territories, monopoly franchise

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1 territories, and it's very difficult at this early
2 stage to predict where competition is going to push
3 prices. I would predict that very shortly we will
4 find that prices will have to be deaveraged by cost,
5 density and other variables and that would result in
6 likely more than one price for both business and
7 residence customers, depending on geographical
8 location. How far that goes, of course, depends on
9 the structure of universal service funding mechanisms
10 and the ability of those mechanisms to maintain
11 averaged rates or at least low rates and high cost
12 areas. I would expect that the competition will force
13 down prices in the most densely populated and most
14 competitive areas. I have a question in my mind about
15 that.

16 Q. But that's what zone one and zone two as
17 proposed by the company are intended to do, isn't it?

18 A. Yes. And I am suggesting that the
19 competitive prices that result will largely be
20 determined by the costs of the new entrants as much as
21 anything, and those costs could be very low, for
22 example, for a selected site like a university campus
23 or an industrial park targeted, and I suspect those
24 prices will be driven down in those easily accessible
25 highly dense areas. I don't know how far. I can't

02745

1 give you a number. I would be very surprised if rates
2 of \$30 a line are sustained in the competitive
3 environment in business concentrated geographical
4 areas.

5 Q. So then that price reflects the company's
6 estimated ADSRC price, so then it would be driven to
7 its TS LRIC cost, wouldn't it?

8 A. Well, I don't think it will be driven to. I
9 don't think any company can really live without
10 contributions towards other costs.

11 Q. I'm sorry. Something approaching TS LRIC?

12 A. Yes. My suspicion is and my best guess is
13 it will be driven below the ADSRC, remembering that
14 the ADSRC even for a perfectly competitive firm is
15 still a number that has to be attained by the firm and
16 there will be some services that will be highly
17 competitive and they won't attain that level. Other
18 services will have to be above that average for the
19 firm to remain financially viable.

20 Q. But you don't have any professional opinion
21 as to where that competitive price of an efficient new
22 entry will drive the price?

23 A. I do have a professional opinion but it is
24 based on proprietary information and I would be
25 hesitant to specify a price that might reveal

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1 proprietary information. We do work for competitive
2 new entrants, newly entering competitive as new
3 competitors in incumbent local exchange markets, and I
4 wouldn't want to share that proprietary information.

5 Q. Is it fair to say that it would be visibly
6 below ADSRC at least as the company calculates?

7 A. It's fair to say that it will certainly be
8 below in the most desirable areas, and by most
9 desirable I mean those that are desirable from the
10 perspective of a new entrant.

11 Q. I believe there is testimony in the record
12 from I think one of the AT&T witnesses that estimates
13 an average total bill per month for residential user
14 of something I think in the neighborhood of \$55 a
15 month. Is that a reasonable approximation?

16 A. That's very consistent with the data with
17 which I am familiar which is available on a nationwide
18 basis. I don't know in the state of Washington, but
19 that's certainly consistent with the national data.

20 Q. Obviously from your testimony it's your
21 view that the entire cost of the local loop should be
22 not shared but be applied entirely to the residential
23 line?

24 A. I would say it slightly differently. The
25 cost of the local loop is what it is. There's no way

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1 around the fact that one has to dig a trench to
2 provide service to a home and one has to lay material
3 in that trench and one has to incur certain costs that
4 are clearly associated with giving that home access to
5 the public switched telephone network, and that is the
6 unambiguous piece. The remaining issues are who
7 should pay. Should that be charged to the end user in
8 the form of monthly recurring prices, should it be
9 charged in part to carriers in the form of
10 interconnection charges or from some other source.

11 What my testimony says is that in a
12 competitive environment it cannot be supported by
13 competitive services such as voice mail and features
14 that could be offered in a competitive marketplace. It
15 must come from ideally end user charges or sources that
16 are not subject to competitive erosion.

17 Q. But most of that \$55 price or typical bill,
18 once you exclude the charge for the line itself would
19 be those potentially or actually competitive services.
20 Is that a fair statement?

21 A. Well, that total bill I am assuming is not
22 just the bill of a single company. That would include
23 as well long distance charges which may be offered by
24 other companies, so I am not expecting that that would
25 be the average residential bill of the local exchange

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1 company in the future.

2 Q. And do you have an approximation for what
3 that figure is currently for U S WEST in the state?

4 A. I have the information at home in my
5 office. I did not bring it with me and I would be
6 hesitant to guess at it without referring to it.

7 Q. Well, let's assume hypothetically, say it's
8 \$30. And it's the company's position that the costs
9 of providing that service, at least the ADSRC target
10 price, I guess, is a better way to phrase it, in zone
11 one is \$21. Now, staff and public counsel take the
12 position that it's under \$10, at least for the
13 incrementally based pricing, or costing I should say.
14 Just assuming hypothetically we conclude and adopt the
15 position of the staff and public counsel and determine
16 that the price should be \$10. Would it then be a
17 rational economic decision on the part of the company,
18 however it would be accomplished technically and in
19 the sense of a regulatory environment, to try to exit
20 the residential exchange market?

21 A. I don't think that would be the first
22 course of action. I think for a variety of reasons,
23 not the least of which is the kind of public reaction
24 that might generate and the kind of reaction that the
25 Commission might have to that type of proposal, it

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1 may in the end be the final result out of a financial
2 necessity.

3 Q. What I'm trying to get to, is there an
4 advantage to the company to have access to the other
5 vertical profit centers that follow on from having
6 access to that residential market?

7 A. I think there may be isolated advantages.
8 I don't think it's a general advantage and the reason
9 is that all of the components, at least the major, the
10 most profitable components which are providing the
11 most contribution with which to cover the cost of the
12 loop, are the very things that are attractive to
13 competitors. That's why we see so much competition in
14 the toll markets is that that's a very profitable
15 market. Those revenues were used in the past to fund
16 the local loop, and those sources of funding are going
17 to be rapidly taken away through competition. The
18 same thing will be true as companies come in with one
19 stop shop options, whether that's through a resold
20 loop, which they then brand as if it were their own.

21 Say AT&T is coming in and selling a
22 customer a full array of services utilizing U S WEST's
23 loop. In essence U S WEST would get whatever price is
24 on that wholesale loop and virtually nothing else
25 since the other services would be offered by the

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1 competitor. That certainly is not a viable situation
2 if U S WEST continues to incur the \$30 of digging the
3 trench and laying the cable and only has access to a
4 \$10 wholesale price of the loop. That's what I meant
5 by financial necessity. They may have to say we can't
6 survive that environment and we can't continue to
7 operate in that manner, but that is the direction that
8 competition is clearly forcing most companies.

9 COMMISSIONER HEMSTAD: That's all I have.

10

11 EXAMINATION

12 BY COMMISSIONER GILLIS:

13 Q. My questions are similar to Commissioner
14 Hemstad. I want to follow up a little bit on that.
15 In the market where a firm faces effective competition
16 for its service I think I understood you to say that
17 they would likely price it somewhere below ADSRC but
18 above TS LRIC?

19 A. For some services but again remember that
20 every time one goes below ADSRC something else has to
21 go above to hit that average and that still is not
22 enough to cover the common costs of the company so
23 while they may go below for certain services. For
24 example, the airlines I'm sure go below their ADSRC
25 when they have deeply discounted prices on tickets,

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1 over Saturday night stays or 14 day prices. They have
2 to make that up with higher than ADSRC prices
3 elsewhere. The same thing will happen in any
4 competitive environment, telecommunications included.

5 Q. To make it simple in a market where the firm
6 has two products and they both face effective
7 competition, how would they make the choice of how to
8 allocate those common costs between those two
9 products?

10 A. They generally would not and do not
11 allocate the common costs. I worked for a large
12 number of competitive firms and while they may
13 allocate the common costs in the same spirit that
14 ADSRC is calculated, they don't impose that as a rigid
15 pricing rule. They realize some things are going to
16 generate only pennies contribution and some things
17 will generate more so they don't really allocate the
18 common costs. They price the products sufficiently
19 below the ASIC in order to accumulate the common costs
20 over all their products.

21 As an exercise not long ago for a class I
22 had students go out to two local grocery stores --
23 this is near the University of California, San Diego
24 -- located within three miles of one another and check
25 prices on standard items like T bone steaks and

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1 bananas and standard brands of bread and the like and
2 the prices varied surprisingly. In fact the only
3 thing that was 100 percent consistent between the
4 stories was Budweiser beer for some reason, but
5 everything else had varying markups. If you averaged
6 it all out the total revenue that one would have to
7 part with for the basket was about the same, but if
8 you took any individual item, bananas, they might be
9 priced at 59 cents a pound in one store and 47 cents
10 in another.

11 So the firms picked flexibly, based on
12 their own customers' tastes and their own niches in
13 the market, what they chose to mark up more or less.
14 The real competitive force was to make sure the basket
15 wasn't substantially different and there was enough
16 contribution in those items to compensate the stores
17 for its common costs. That's the way a competitive
18 process will work in telecommunications. Some people
19 will choose to mark up their features more and their
20 lines less and others will do the reverse. The
21 consumer will decide who to buy services from based on
22 whether the basket of goods they buy is a better
23 bargain from one source or another, and that kind of
24 flexibility is going to be essential in
25 telecommunications.

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1 Q. In pricing the competitive service or the
2 service facing effective competition, the company will
3 need to take into account then what the competitor can
4 supply that for, the cost?

5 A. Precisely and what contribution the
6 competitor must have towards its common costs as well.

7 Q. In an environment where a firm sells to
8 multiple markets, to two markets, one is competitive
9 and the other there is ineffective competition in the
10 other market how do you believe -- what basis is it
11 appropriate to allocate common costs between the
12 competitive service and the service that isn't facing
13 competition?

14 A. Again, I would suggest not thinking of it
15 in terms of the allocation of the common costs but
16 thinking of it in terms of encouraging the company to
17 get as much contribution as they are able to get from
18 the competitive services and then obviously tending to
19 the issue of whether the firm needs -- how much the
20 firm needs from its monopoly services to remain
21 financially viable, but I think it's important to let
22 the marketplace govern the pricing in the competitive
23 side of the business and, as I say, provide incentives
24 to get what one can. Incentive regulation, for
25 example, is one way of doing that where the firm can

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1 keep part of the earnings that are obtained from all
2 of its markets, therefore, it has incentives to
3 maximize contribution from the competitive services.

4 Q. So we want the firm recover as much from
5 common costs on top of its direct costs that they can
6 in the competitive market on the competitive side, is
7 what you're saying, and then the residual in the
8 market that isn't facing effective competition it
9 would need to recover the rest if the firm is able to
10 survive?

11 A. In essence that's right. Now, the danger
12 of trying to get the maximum recovery of common costs
13 from competitive services through allocation is
14 portrayed in the various Harvard business cases as the
15 death spiral. By assigning an amount, a
16 responsibility for common costs, it can force a firm
17 to try to get an unrealistic amount of contribution.
18 And in doing so it really doesn't get the revenues
19 that the prices -- from the prices it calls out. It
20 loses the market altogether and by losing all the
21 contribution it ends up literally driving itself out
22 of business on the competitive services, so one simply
23 has to say -- one has to give the firm enough
24 flexibility to be able to stay in the market and get
25 as much common costs as they can, not force an

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1 unrealistic level of common costs to be contained from
2 the competitive side.

3 Q. If it's a situation where we can be assured
4 that the conditions are adequate that we're
5 comfortable there's effective competition in that
6 market, is there an incentive for the profit
7 maximizing firm that's serving both of these markets
8 to shift common costs on to the other segment, the
9 noncompetitive segment, or will they naturally seek to
10 recover their maximum common costs they can in that
11 kind of environment?

12 A. The answer to that question depends
13 entirely on what happens to the profits the firm
14 acquires from the markets. If it's an earnings
15 constraint and it simply says whatever profits you get
16 you're not going to get any more or less than an
17 allowed return then there is little incentive to go
18 acquire additional profits. If there is some benefit
19 to the firm, whether it's through regulatory lag or
20 through an incentive regulation plan or some other
21 mechanism to acquire extra profits, then of course the
22 incentive would be there to get as much as possible
23 from the competitive services, for that matter, from
24 all of the services of the firm, but certainly there
25 would be no incentive to sacrifice profits on the

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1 competitive services.

2 COMMISSIONER GILLIS: Thank you.

3 MR. SHAW: Couple of questions.

4

5 REDIRECT EXAMINATION

6 BY MR. SHAW:

7 Q. Couple of questions about questions you
8 received from the bench and from other counsel.
9 Counsel for MCI talked to you about the ninth
10 supplemental order issued in this case, and I will
11 represent to you that in that order the Commission
12 directed the company to file testimony regarding the
13 appropriate costing methodology to be used in this and
14 future proceedings. Have you reviewed the LRIC
15 costing methodology that the company uses in all of
16 its jurisdictions including Washington?

17 A. Yes.

18 Q. Is that methodology the appropriate costing
19 methodology to be used in this and future proceedings
20 in your opinion?

21 A. Yes, it is. Again, without seeing the
22 specifics of how it's implemented in Washington, the
23 methodologies and the description of those
24 methodologies are correct.

25 Q. For the record to be clear, what is your

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1 definition of methodology when you're talking about
2 cost studies?

3 A. The manner in which the costs are
4 calculated. For example, I would ask whether or not
5 the company has adequately included the effect a
6 service might have on the need to expand facilities
7 and the cost of that expansion, the effect a service
8 might have on the need to advance the placement of
9 expanded capacity and the present value of that
10 advancement. I would be sure that those calculations
11 were correctly represented in the company's
12 methodologies. Where the line is drawn is I did not
13 look at the calculations themselves.

14 Q. The Commission further ordered the company
15 in the ninth supplemental order to file testimony
16 including adequate information to allow parties to
17 proceedings involving cost issues to have the ability
18 to understand assumptions used, to review and analyze
19 the effect of inputs and outputs and to modify and
20 model different inputs and assumptions. Did you
21 review the testimony of Mr. Farrow filed in response
22 to this Commission directive?

23 A. Was that the supplemental testimony?

24 Q. Yes.

25 A. Yes.

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1 Q. In reviewing that information that he
2 referred to as being supplied in this docket and the
3 additional information that was supplied in his
4 supplemental testimony, would you as an independent
5 analyst be able to understand the assumptions the
6 company used, review and analyze the effect of inputs
7 and outputs and modify and model different inputs and
8 assumptions?

9 A. By and large, yes, but as I said in my
10 earlier testimony there certainly is room for
11 improvement in being able to more efficiently review
12 those studies. I did not address the question in my
13 review of those materials as to whether or not
14 modification of the inputs and outputs was possible so
15 I don't know the answer to that.

16 Q. Commissioner Hemstad asked you a question
17 about business rates, and you didn't have the
18 company's proposed business rates at the tip of your
19 tongue and he asked you to assume a proposed business
20 rate of \$30 in the urban zone. Let me ask you this
21 just directly. Do you know what the company's
22 calculation of business ADSRC costs are?

23 A. I am afraid I don't.

24 Q. Would you expect it to be less than \$20
25 given the density and so forth of business loops?

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1 A. I don't know. I'm not familiar enough with
2 Washington.

3 Q. Thank you.

4 MR. SHAW: That's all I had.

5 JUDGE WALLIS: Follow-up questions? It
6 appears that there are none. Dr. Emmerson, thank you
7 for coming back with us. You're excused from the
8 stand at this time.

9 THE WITNESS: Thank you for accommodating
10 my schedule.

11 JUDGE WALLIS: Let's be off the record.

12 (Recess.)

13 JUDGE WALLIS: Let's be back on the record,
14 please. The company is calling as its next witness
15 Peter B. Copeland.

16 Whereupon,

17 PETER COPELAND,
18 having been first duly sworn, was called as a witness
19 herein and was examined and testified as follows:

20 JUDGE WALLIS: In conjunction with the
21 appearance of this witness we have previously at page
22 1783 of the transcript identified his rebuttal
23 testimony, supplemental testimony, benchmark cost
24 model and an exhibit not brought forth by him of white
25 paper entitled loop dreams as Exhibits 355 through 358

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1 respectively.

2

3

DIRECT EXAMINATION

4 BY MR. SHAW:

5 Q. Could you state and spell your name for the
6 record?

7 A. My name is Peter B. Copeland. My name is
8 spelled C O P E L A N D.

9 Q. Could you state your employer and your
10 business address.

11 A. I'm employed by U S WEST Communications at
12 1801 California Street, Room 4740, Denver, Colorado.

13 Q. In what capacity are you employed?

14 A. I'm employed as an issues manager in the
15 public policy department of U S WEST.

16 Q. Mr. Copeland, did you cause to be prepared
17 or prepared under your direction your rebuttal
18 testimony and supplemental testimony in this case and
19 the exhibits benchmark cost model No. 3 for
20 identification, and are you familiar with the white
21 paper loop dreams that you are refer to in your
22 rebuttal testimony marked 358 for identification?

23 A. Yes.

24 Q. Are the questions and answers in your
25 narrative testimony, your answers to those questions

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1 true and correct to the best of your knowledge and
2 belief?

3 A. Yes, they are.

4 Q. And you're familiar with the benchmark
5 costs model and the Loop Dream memorandum as related
6 in your testimony?

7 A. Yes.

8 MR. SHAW: Your Honor, at this time I would
9 move the admission of 355T, 356T, 357 and 358, and as
10 previously requested we have oral rebuttal of the
11 Mercer testimony which the company has not had a
12 chance to rebut in this proceeding.

13 JUDGE WALLIS: Is there objection to the
14 exhibits?

15 MS. PROCTOR: Your Honor, I don't object to
16 the exhibit but this is the first I'm hearing of any
17 oral surrebuttal.

18 JUDGE WALLIS: Let's deal with the exhibits
19 first. It appears that there is no objection to the
20 exhibits and the exhibits are received.

21 (Admitted Exhibits 355T, 356T, 357 and
22 358.)

23 JUDGE WALLIS: Now, Ms. Proctor.

24 MS. PROCTOR: I had not received any notice
25 of this request for surrebuttal, and I have certainly

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1 have not been provided pursuant to the bench's earlier
2 direction of some idea of what they were going to be
3 inquiring about.

4 MR. SHAW: Your Honor, we informed Mr.
5 Waggoner of this fact last week after you had
6 requested that we do tell counsel of our intent, and
7 Mr. Copeland was here last week and we had prepared
8 him to go ahead with that then, so I know we told Mr.
9 Waggoner.

10 MS. PROCTOR: I think you advised Mr.
11 Waggoner that there was going to possibly be some
12 surrebuttal. There certainly wasn't anything more
13 definitive than that.

14 MR. SHAW: On the situation we have here on
15 the simultaneous supplemental testimony, Mr. Copeland
16 has filed his benchmark cost model that he
17 participated in filing with the FCC. Dr. Mercer has
18 taken his previous model, combined it with the
19 benchmark cost model, made different changes to it and
20 come up with different outputs. The purpose of the
21 oral rebuttal is to point out problems with what the
22 company understands Dr. Mercer did. We have the right
23 to rebut that and I think that AT&T has been on notice
24 that we are going to rebut that and it's just an
25 obvious rebuttal for the company to engage in.

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1 JUDGE WALLIS: The issue that I am most
2 concerned with is notification to opposing counsel,
3 and that I think we made it clear early on last week
4 that while we felt it was appropriate for the company
5 to offer surrebuttal it was also necessary in
6 conjunction with that opposing parties be given an
7 opportunity to at least determine whether their
8 experts needed to be around by disclosure of the fact
9 of surrebuttal and the nature of the topics if
10 necessary going to the disclosure of specific
11 questions that would be asked. And I guess my question
12 for you at this point is whether that information was
13 provided to Mr. Waggoner or sufficient information
14 that Mr. Waggoner could follow up on it?

15 MR. SHAW: We informed Mr. Waggoner that
16 within the limits of what information that we had,
17 that Mr. Copeland had, there has been no opportunity
18 for discovery on this simultaneous supplemental cost
19 testimony. The cutoff for discovery had expired in
20 this case, and so we informed him that we were going to
21 rebut the Mercer study.

22 JUDGE WALLIS: We've discussed the matter
23 and I believe that it appears to be substantially if
24 not entirely a matter of communication among counsel,
25 as much as Mr. Waggoner was advised, according to the

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1 representation of the company, so the questions will be
2 allowed.

3 MS. PROCTOR: Your Honor, I wonder if I
4 might have leave to defer my cross-examination on him
5 because at this hour I will be unable to talk to Dr.
6 Mercer. I will be unable to get him on the bridge
7 because he's in Colorado and I am confident that he's
8 probably not still in the office. If Mr. Copeland
9 would be available tomorrow morning so that I could
10 complete cross-examination.

11 JUDGE WALLIS: I would prefer not to make
12 that ruling in advance of your hearing the questions
13 and determining that in fact your consultation is
14 necessary.

15 MS. PROCTOR: That's fine.

16 JUDGE WALLIS: But certainly would allow
17 you to repeat your request as soon as the question is
18 completed.

19 BY MR. SHAW:

20 Q. Mr. Copeland, have you reviewed Dr.
21 Mercer's direct testimony in this case where he shows
22 an estimated monthly cost per line of basic local
23 service in Washington of \$18.16?

24 A. Yes, I have.

25 Q. And did Dr. Mercer use the so-called

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1 Hatfield Associates cost model to develop those costs
2 sponsored in his direct testimony?

3 A. Yes, to the best of my knowledge he did.

4 Q. Is this the same Hatfield Associates cost
5 model that underlaid the cost of basic universal
6 service that was sponsored by MCI and filed in the FCC
7 proceeding concerning universal service funding which
8 you refer to as the proceeding where you developed the
9 benchmark cost model?

10 MS. PROCTOR: Excuse me, Your Honor. I am
11 going to object to this line of questioning because to
12 the extent that his testimony is directed to the
13 initial model filed by Hatfield and Dr. Mercer in this
14 case U S WEST has certainly had opportunity to reply to
15 that.

16 JUDGE WALLIS: Let me ask whether there is
17 a preliminary question.

18 MR. SHAW: This is just foundation just to
19 put the thing in context. It's not directed to the
20 direct testimony at all.

21 JUDGE WALLIS: Witness may respond.

22 A. Based on the documentation in Dr. Mercer's
23 direct testimony I would say it is.

24 Q. Is the \$18.60 cost the same cost as was
25 filed with the FCC by MCI in the cost of basic

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1 universal service?

2 A. I think in that MCI study there was only a
3 national cost in that average cost that I was aware
4 of, and it was in the similar area of \$18. I am not
5 exactly sure what it is.

6 Q. You filed in conjunction with three other
7 companies the benchmark cost model as you testified to
8 in your supplemental testimony, correct?

9 A. Yes.

10 Q. Did you use -- did you show a monthly cost
11 of \$17.02 using the MCI Hatfield annual cost factor?

12 A. Yes, it does show that.

13 Q. What do you mean when you say you used the
14 MCI Hatfield annual cost factor?

15 A. As I stated in my supplemental testimony,
16 the benchmark cost model used two annual cost factors
17 to convert the investment that is calculated by the
18 model into a recurring cost of service, and one of
19 these factors was the MCI Hatfield factor that they
20 used in their model, and that is based on some direct,
21 some historical expense, investment relationships and
22 also based on some other studies where they use a
23 direct amount per line, and based on investment
24 categories an expense additive to turn into a monthly
25 cost, and some of the other sources they use that are

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1 not nationally derived historical data from the ARMIS,
2 they're not well documented.

3 Q. In Dr. Mercer's supplemental cost testimony
4 of December does he introduce yet a third cost number
5 of \$11.15?

6 A. Yes, he does.

7 Q. And what changes were made to the Hatfield
8 model that produced the \$17.02 number that were made
9 to produce the \$18.16 number?

10 A. The numbers change from \$18.16 to \$11.15,
11 but the major change to the Hatfield model was the
12 incorporation of the benchmark cost model into the
13 Hatfield model. Within the benchmark cost model
14 Hatfield Associates then made changes to six areas of
15 the model. The first was the inclusion of business
16 lines. The second was modifying fill factors. The
17 third was the addition of the investment for the
18 network drop and network interface. The fourth was the
19 lowering of the digital line carrier equipment costs or
20 price inputs to the model. The fifth change was
21 reductions in the switching costs price inputs to the
22 model, and the final change was to lower some of the
23 recurring expenses associated with local service that
24 are part of our annual cost factors in the way the BCM
25 handles the annual cost.

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1 Q. Was the BCM designed to define individual
2 company costs such as U S WEST?

3 A. No. The BCM was designed to target high
4 cost census block groups and determine that there might
5 be a need to subsidize local service in these areas.
6 It was not designed to define any individual company's
7 cost of providing local service or its long-run
8 incremental cost of providing local service.

9 Q. Do any of the modifications to the
10 benchmark cost model identify any company's specific
11 cost for capitalized investment, network technology,
12 network structure or expense level?

13 A. No. None of the changes that I saw
14 performed by Hatfield Associates to the BCM, as they
15 include it in their model, seem to be made to produce
16 changes that would replicate U S WEST or any other
17 company's particular costs to serve -- provide local
18 service in the areas. Overall it appears the costs
19 will purely design or the changes are purely designed
20 to lower the monthly cost of service output from the
21 model.

22 Q. In your opinion are the modifications made
23 to the benchmark cost model unreasonable?

24 A. Yes, to a large extent they are.

25 Q. Can you give an example?

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1 A. The biggest example I could give would be
2 the changes in the digital line carrier equipment. In
3 those prices inputs to the model, which are variable,
4 they change the input price for digital line carrier
5 equipment by reducing the list price by approximately
6 50 percent from the list price that was within the
7 model, and secondly they doubled the discount from the
8 list price for that digital line carrier equipment
9 from the discount in the model from 20 percent to 40
10 percent.

11 The effect of this was to substantially
12 reduce the digital line carrier equipment costs.

13 Q. What was the impact on the calculated cost
14 per month?

15 A. This decreased the cost per month over
16 \$2.60 per month using the MCI Hatfield factor or
17 approximately 15 percent a month.

18 Q. Has Dr. Mercer used consistent DLC costs or
19 digital line carrier costs in the studies filed in the
20 direct testimony and the supplemental testimony?

21 A. No, he hasn't. In Dr. Mercer's direct
22 testimony utilizing Mr. Trotter's data request PC 36
23 that Dr. Mercer responded to in attachment A -- it's a
24 confidential exhibit, but by using the numbers within
25 there I calculated that the cost per line for DLC

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1 equipment in the original Hatfield study was \$267 per
2 line after the inclusion of a discount, and in the
3 supplemental testimony of Dr. Mercer where he used the
4 BCM he changed the after discount price for the DLC
5 equipment to \$150 per line so those should be
6 consistent but they were not.

7 MS. PROCTOR: Excuse me, can I ask for
8 clarification? I understood you to say that that was a
9 confidential exhibit. Were you just revealing
10 confidential numbers?

11 THE WITNESS: No, I wasn't. I was
12 calculating numbers that do not provide any of the
13 background that's provided within that document.

14 Q. How does the 150 per line digital line
15 carrier price compare to the default discount price
16 inputs or the digital line carrier type equipment in
17 the benchmark cost model?

18 A. Well, the \$150 per line price would equate
19 to a discount of over 60 percent from the list price
20 for such equipment, and what is problematic in putting
21 a discount of this magnitude in the model is that the
22 manner in which DLC equipment is handled in the model
23 is on a per line basis assuming an optimal fill. Now,
24 when you have an optimal fill that is more likely to
25 happen in urban areas than in rural areas and you

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1 would not see a price per line drop substantially
2 overall because in rural areas you will not be able to
3 achieve that optimal fill. Therefore, pricing changes
4 were made in the input section of the model by Hatfield
5 and Associates that was inconsistent with this internal
6 network logic structure of the model, and I feel it was
7 an inappropriate change.

8 Q. How did NYNEX, U S WEST, MCI and Sprint,
9 the joint benchmark cost model sponsors, develop the
10 fill factors that were used in the benchmark cost
11 model?

12 A. Each of the joint sponsors consulted with
13 their network engineers on their standard engineering
14 practices for fill factors in installing plant. They
15 also -- we also looked at the fill factors that are in
16 various journals and papers about placing plan, and as
17 a group the joint sponsors agreed that the default
18 values that were put into the BCM represented a
19 reasonable standard engineering practice of the four
20 parties.

21 Q. Were the fill factors as modified from the
22 benchmark cost model by Dr. Mercer achievable in
23 practice, in your opinion?

24 A. Well, yes. I feel that any fill factors
25 are achievable. However, there are side effects of

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1 going in with higher fill factors and installing plant
2 at that level. You run the risk of having premature
3 exhausted facilities, held orders and increased costs.

4 Q. I take it then that the fill factors used
5 in the modified Dr. Mercer model do not represent the
6 standard practices or planning horizons of the joint
7 sponsors?

8 A. No, they don't.

9 Q. What is your estimate of the sensitivity of
10 the benchmark cost model to the changes in the fill
11 factors made by Dr. Mercer?

12 A. Dr. Mercer stated in his supplemental
13 testimony that changing the fill factors as he did
14 reduced the monthly cost per line by 52 cents and that
15 equates to approximately a 5 percent reduction in
16 investment levels in the model.

17 Q. Does the benchmark cost model, as filed
18 with the FCC include service just to residential
19 households?

20 A. Yes, it does. It does not include any data
21 for business lines.

22 Q. And does Dr. Mercer's modified version of
23 your model include business lines?

24 A. Yes, it does.

25 Q. And why did the joint sponsors exclude

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1 business lines from the model filed with the FCC?

2 A. Well, the joint sponsors would like to have
3 included business lines by census block group in the
4 benchmark cost model. However, we have not been able
5 to find a source of information or methodology that
6 would provide accurate data in developing these
7 business line counts at a census block group level.

8 We have examined or looked at Dun &
9 Bradstreet data. For instance, there's a number of
10 vendors of business data. They provide geocoded data
11 for businesses and sometimes provide employee counts
12 and standard industry codes. However, there's no
13 reliable way of converting these employee counts into
14 business lines. You don't know if it's an 800 calling
15 telemarketing center for a company or a warehouse, so
16 it's difficult to determine if the number of business
17 lines you might add in converting, doing some standard
18 conversion of employees to lines, would be accurate.
19 And if you add lines in that manner at a census block
20 group level you can distort the data.

21 Q. Have you been able to find any statistical
22 relationship between business lines and census block
23 group household density or between business lines and
24 any other census block group characteristics?

25 A. No, I haven't. I've examined proprietary

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1 data within U S WEST that had business location and
2 lines geocoded and tried to relate that to the
3 characteristics of census block groups and have found
4 no statistical correlation between either distance,
5 density or square miles of a census block group with
6 the number of business lines.

7 Q. Does the decision of the joint sponsors to
8 not include business lines compromise the benchmark
9 cost model's stated purpose of identifying high cost
10 census block groups in the country?

11 A. No. The joint sponsors feel that
12 identifying these high cost areas can be done without
13 the inclusion of business lines. In these high cost
14 rural areas we feel that there would be probably a low
15 number of business lines and they would have the same
16 characteristics as the residential lines in that
17 census block group, and based on that assumption there
18 is no impact of not including these business lines.

19 Q. What is the effect of Dr. Mercer including
20 business lines in his version of the benchmark cost
21 model?

22 A. Dr. Mercer included business lines with
23 varying factors based on the density group of the
24 census block group, so if the density of a block group
25 fell within a certain range in population per

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1 kilometer, square kilometer, he would include a
2 certain percentage of additional lines to represent
3 business lines and also additional residential lines,
4 second residential lines, and those factors range from
5 9 percent to 50 percent. Dr. Mercer used the 50
6 percent factor in the one density group, which I think
7 was 1,000 to 5,000 population per square kilometer,
8 and so that particular group had approximately 56
9 percent of the residential lines in the state.

10 So, using a factor of 1.5 to increase these
11 lines gave that cost grouping added weight in
12 determining the statewide average cost. That group
13 had approximately 86 percent of the statewide average
14 costs, so the net effect of the inclusion of business
15 lines in this way was solely to reduce your statewide
16 average cost because there is no way to determine that
17 the business lines are in any of these particular
18 census block groups.

19 Q. How many business lines did Dr. Mercer's
20 modified model attribute to the company's state of
21 Washington operations?

22 A. Dr. Mercer used approximately 608,000 lines
23 for additional lines for business in Washington state.

24 Q. How many business lines does the company in
25 fact have in Washington state?

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1 A. It's my understanding it has approximately
2 475,000 lines for business.

3 Q. Did Dr. Mercer also reduce the overhead
4 expense from 10 percent to 6 percent that you used in
5 the benchmark cost model filed with the FCC?

6 A. Yes, he did.

7 Q. And what was the justification that he
8 stated for that?

9 A. Dr. Mercer stated that he examined the
10 investment and revenue associated with specific firms
11 within the auto manufacturing and airline industry and
12 found a 6 percent overhead to be the appropriate level
13 of overhead for those firms. He then says that that's
14 the appropriate level for firms providing residential
15 local service. I do not see any similarity between
16 these two industry sectors and any firm providing
17 local residential telecommunications service.

18 Q. Are there any other inputs that, in your
19 opinion, are inaccurate changes to the benchmark cost
20 model that you filed with the FCC?

21 A. I feel Dr. Mercer's use of a recurring
22 expense factor varies greatly from the MCI Hatfield
23 factor and are inappropriately low. The MCI Hatfield
24 factor for a nationwide basis was approximately .23,
25 meaning that if you multiply the gross investment

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1 calculated by the model by .23 you come up with your
2 annual recurring cost. The historical relationship
3 between gross investment and expense for monthly cost
4 purposes based on national ARMIS data is approximately
5 .32, and so the MCI Hatfield factor is already lower.
6 The actual relationship in Washington in this
7 historical expense to gross investment is
8 approximately .36.

9 I estimated Dr. Mercer's annual cost factor
10 to be between .18 and .19. Based on the monthly cost
11 data provided I couldn't come up with an exact number
12 because of the constraints of the data that was
13 provided.

14 Q. Finally, in order to completely audit the
15 model offered by Dr. Mercer on supplemental testimony
16 filed in December, would you need access to the model
17 and the documentation such that you filed with the FCC
18 and made available to interested parties relating to
19 the benchmark cost model?

20 A. Yes, I would. The joint parties filed full
21 documentation of the algorithms and computer disks of
22 the model in CD format so people could see the actual
23 calculation done for each section of the model, as
24 well as full data inputs as well as outputs, and that
25 would be necessary to fully analyze the work that Dr.

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1 Mercer did to come up with his \$11.15 rate.

2 MR. SHAW: Thank you. That's all I have
3 and I would offer the witness for cross.

4 MS. PROCTOR: Your Honor, well, I think it's
5 obvious I am going to need the assistance of Dr. Mercer
6 to respond to this very detailed testimony. I noticed
7 that Mr. Shaw had prepared questions, which I
8 understood pursuant to the ALJ's earlier direction last
9 week should have been provided. Be that as it may, I'm
10 suggesting that perhaps a way to handle this, we'll
11 have a transcript for this tomorrow morning or around
12 noon or something like that and perhaps the most
13 expeditious way to handle this is I can get back to Dr.
14 Mercer and he could simply be prepared when he takes
15 the stand to respond to the comments of Dr. Copeland.
16 I think that that would perhaps elicit a fairest airing
17 of the issues and I am confident that Dr. Mercer can do
18 a better job of explaining these issues than I could
19 ever do on attempting to cross-examine. And I would
20 anticipate that we would, given the scheduling you had
21 suggested be able to have some written testimony
22 available to the company next week so that when Dr.
23 Mercer took the stand they would be able to have Mr.
24 Copeland review that and conduct some cross-examination
25 on that.

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1 MR. SHAW: Your Honor, there's no desire by
2 U S WEST to deprive AT&T of their right of
3 cross-examination. The problem with simultaneous
4 testimony is that we either orally rebut or there has
5 to be room in the schedule for another round of
6 testimony, so we really have no choice. I hate to
7 keep bringing Mr. Copeland back. He's been here for
8 many days, but we will do whatever the bench feels is
9 necessary to have a complete record in this case as
10 long as we are not deprived of our absolute right to
11 rebut as the party with the burden.

12 MS. PROCTOR: Mr. Shaw, I was not suggesting
13 that Mr. Copeland would have to return. I was
14 suggesting, and I hope I was clearer than this, that we
15 would simply allow Dr. Mercer to do some testimony in
16 response and provide that to you next week.

17 MR. SHAW: Your Honor, I will object and
18 make a record objection that we're not allowed to
19 rebut what Dr. Mercer ends up testifying to. We have
20 a right to rebut that, not just cross-examine but we
21 have a right to rebut that.

22 JUDGE WALLIS: The procedure that was
23 suggested by Ms. Proctor appears to be appropriate and
24 it will be allowed.

25 MS. PROCTOR: Thank you, Your Honor.

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1 JUDGE WALLIS: It is expected that the
2 extent of any additional testimony would be limited to
3 the response to Mr. Copeland's testimony today.

4 MS. PROCTOR: Certainly.

5 JUDGE WALLIS: Perhaps during a scheduling
6 discussion we can talk about timing. Very well. The
7 witness is available for cross-examination. Mr.
8 Smith.

9

10 CROSS-EXAMINATION

11 BY MR. SMITH:

12 Q. Good evening, Mr. Copeland. You indicate
13 in your testimony that you represent U S WEST on the
14 telecommunications industry analysis project; is that
15 correct?

16 A. Yes, I do.

17 Q. And on page 2 of your rebuttal testimony
18 you state that "The purpose of my testimony is to
19 briefly present an industry view as embedded by the
20 TIAP concerning loop costs." Do you see that on line
21 4?

22 A. Yes, I do.

23 Q. And you do not represent the TIAP in this
24 proceeding; is that correct?

25 A. That's correct.

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1 Q. And you're not purporting to testify on
2 behalf of TIAP in this proceeding; is that correct?

3 A. That's correct.

4 Q. Page 2 -- and all my questions will be
5 regarding your rebuttal testimony. There's a footnote
6 on page 2 where you cite to Carol Weinhaus in
7 connection with a publication of Loop Dreams. Who is
8 Ms. Weinhaus?

9 A. Ms. Weinhaus is the project director of the
10 telecommunications industry analysis project. I was
11 citing to the paper.

12 Q. And is it your testimony that Ms. Weinhaus
13 agrees with your representations of the
14 telecommunications industry's analysis project in your
15 testimony?

16 A. No, that's not my testimony.

17 Q. Is it your testimony that Ms. Weinhaus
18 supports your interpretation of the research results
19 of Loop Dreams?

20 A. No. I am representing my view of Loop
21 Dreams in the testimony.

22 Q. In fact, will you accept subject to your
23 check that Ms. Weinhaus has indicated her disagreement
24 both to the representation of the TIAP and the
25 research results of Loop Dreams? Will you accept that

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1 subject to check?

2 A. Subject to check.

3 MR. SHAW: How are we to check that,
4 Counsel?

5 MR. SMITH: I have a letter here from Ms.
6 Weinhaus which I can provide to witness and to
7 counsel.

8 Q. Mr. Copeland, if you would turn to Exhibit
9 358 which is the paper Loop Dreams, and specifically
10 appendix D which begins on page 30. Am I correct that
11 appendix D to the study shows the loop costs for each
12 state?

13 A. It looks like most states. I don't see
14 Wyoming on here.

15 Q. Well, on page 31 in any event it shows the
16 statewide average embedded costs of U S WEST loop in
17 Washington as \$16.87 including overhead costs and
18 \$11.77 without the overheads; is that correct?

19 A. Yes, that's what it shows on that page.
20 However, on page 23 it shows a different set of
21 embedded costs with and without overheads for
22 Washington state.

23 Q. Have you reviewed the company's estimated
24 statewide ADSRC for 1FR residence line and for 1FR
25 business line in this proceeding?

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1 not clear on whether it's just an individual LEC bill
2 or a bill including billings by other carriers.

3 Q. Do you have your work papers?

4 A. I have Loop Dreams.

5 Q. Well, you filed work papers with your
6 rebuttal?

7 A. It was --

8 Q. That was the Loop Dreams?

9 A. It was the Loop Dreams.

10 Q. Can you turn to page 17 of that document.
11 Near the bottom of that page do you see a line that
12 says residential bills for 1992?

13 A. Yes. This amount includes local service as
14 well as long distance service.

15 Q. So it's total residential customer bill?

16 A. Yes.

17 Q. So that would be the toll whether it's
18 interexchange carrier company toll or local exchange
19 company toll as well as residential basic service?

20 A. Yes, including the subscriber line charge
21 as well.

22 Q. Does it include vertical services?

23 A. Yes, to my knowledge it does.

24 Q. Would it include information services?

25 A. If by information services you mean --

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1 Q. 900.

2 A. No, I wouldn't include that, I don't think,
3 because those are billed otherwise than the standard
4 telephone bill.

5 Q. I have a few questions regarding your
6 supplemental testimony Exhibit 356T. Turn to page 9.

7 A. Could you repeat the page number again?

8 Q. 9. And in the middle of that page you talk
9 about the BCM and indicate that the investment level
10 reflects plant as placed at a single point in time.
11 Do you see that?

12 A. Yes.

13 Q. Is that same assumption used in U S WEST's
14 LRIC studies?

15 A. I'm not familiar enough with the U S WEST
16 LRIC studies to know if that's how they place plant.

17 Q. On page 13 you refer to the BCM's highly
18 efficient theoretical investment level. Do you see
19 that?

20 A. Yes.

21 Q. Is it your testimony that U S WEST's LRIC
22 studies in this case are based on actual investments
23 of the company or are they assumed investments of the
24 company?

25 A. I am not an expert in our LRIC studies as I

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1 stated before and I think you need to refer to Mr.
2 Farrow's testimony to answer that question.

3 Q. On page 14 of your testimony supplemental
4 you indicate on line 18 that the BCM uses national
5 level cost data for the major network components where
6 individual company's material prices are based on
7 company specific contracts. Do you see that?

8 A. Yes, I do.

9 Q. Do you have any basis to claim that U S
10 WEST's material prices are not -- let me ask it a
11 different way. Is it your testimony that U S WEST is
12 not getting a better deal on its material prices than
13 the national average?

14 A. My statement was just that the BCM uses
15 national average data not to state what percentage any
16 company might face in their own contracts with
17 vendors.

18 Q. So you made no comparison between the BCM
19 model and U S WEST model to determine whether U S WEST
20 is getting a better deal or a worse deal than the
21 national average?

22 A. The benchmark cost model uses list prices.
23 Individual companies pay a contract specific price so
24 I made no comparison between essentially the list and
25 the discounted price that U S WEST might receive other

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1 than to check to see if the list price appeared
2 reasonable.

3 Q. On line 21 of that page you indicate that
4 the structure cost of the network are also based on
5 national data. Do you have any indication that U S
6 WEST's structure costs are more expensive or less
7 expensive than national average data?

8 A. I don't have any indication whether they're
9 more expensive or less because the structure costs in
10 the model are terrain specific, and I would have to go
11 back and check on the exact mixture of terrain that
12 U S WEST faces and the structural costs of putting in
13 that terrain and compare them again against the output
14 of the model. I have not made that comparison.

15 Q. On page 9 of that testimony you cite three
16 types of loop technology, analog, copper and two
17 different types of fiber based subscriber carrier
18 systems which you then specify on page 10; is that
19 right?

20 A. Yes.

21 Q. Does U S WEST use that technology?

22 A. U S WEST uses some SLC series 2,000 but
23 does not use the advanced fiber communications
24 systems, digital loop carrier systems, that the BCM
25 used in the very low density rural areas. They use

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1 other similar technologies but not that technology.

2 Q. Is this technology more or less expensive
3 than what U S WEST is using?

4 A. I don't know.

5 Q. Turning to your Exhibit 357 and going to
6 the very back of that, second page from the end
7 entitled attachment 2 density assumption tables. Do
8 you have that?

9 A. Yes, I do.

10 Q. And just taking the top table as a density
11 of zero to 5, does that mean zero to 5 households per
12 square mile or what?

13 A. Yes, that means zero to five households a
14 square mile on up to 2,550 households a square mile.

15 Q. Do you know which density arrangement
16 matches U S WEST design group 3 used in its cost
17 model?

18 A. Not specifically. I'm just somewhat
19 familiar with the five different density groups that
20 are used, but not intimately familiar.

21 Q. Is there a reason why U S WEST would not
22 compare the cost assumptions in this national average
23 type approach to its own costs to determine whether
24 there are scenarios or cost -- costs prices for
25 materials, supplies or designs that may be a better --

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1 lead to lower costs or better prices for U S WEST
2 customers?

3 A. We have made comparisons between the
4 architecture of the model and the architecture of the
5 model being the benchmark cost model and some of the
6 manners in which the LRIC studies in U S WEST handle
7 different types of plant such as how many legs are
8 there in a distribution system, how are they shaped,
9 what assumptions you make, but the general approaches
10 of the two models, two types of models are very
11 different and it makes it difficult to do direct
12 comparisons.

13 Q. But certainly if you're designing a
14 particular type of circuit, specific topology, that is
15 the type of analysis or type of model that you've done
16 here in your BCM, is that right, on a very high level?

17 A. This is a high level model engineering
18 process level. However it is not a means for an
19 engineer to design a loop.

20 MR. TROTTER: I have nothing further.

21 Thank you.

22

23 CROSS-EXAMINATION

24 BY MS. PROCTOR:

25 Q. Mr. Copeland, are you aware that the

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1 benchmark cost model was filed with the Pennsylvania
2 Commission by Sprint United in support of a
3 methodology for determining universal service funding
4 in that state?

5 A. The people I work with at Sprint informed
6 me that they did file the model there for universal
7 service purposes.

8 Q. Right. I thought I said in my question
9 that it was for universal service funding?

10 A. I agree.

11 Q. And were you aware that in that same
12 proceeding AT&T and MCI filed the new Hatfield model
13 in support of their position on universal service
14 funding?

15 A. Yes. I heard that Dr. Mercer filed
16 testimony in Pennsylvania that incorporates the BCM
17 into the Hatfield model there in a manner similar to
18 what he filed with Washington state.

19 Q. And you are aware that MCI joined in that
20 sponsorship with AT&T?

21 A. Yes, I was.

22 Q. In fact in your testimony you point out
23 that the joint sponsors at the federal level in
24 supplying the BCM simply supplied the model and each
25 separately filed its own recommendation and

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1 conclusions concerning that model, did they not?

2 A. They filed -- each member of the joint
3 sponsors group filed their own individual comment on
4 what would be a proper use of the BCM in a universal
5 service proceeding separately, yes.

6 Q. And in response to questions from Mr.
7 Trotter, you stated that the BCM uses list prices for
8 equipment; is that correct?

9 A. It uses list prices as one price input. It
10 also has discounts by plant type to apply against
11 that. The discounts apply separately for copper,
12 fiber cable, circuit equipment and switching
13 equipment.

14 Q. Is it fair to say that an individual
15 company regards the terms of its contract with the
16 equipment purchaser and the level of its discount as
17 extremely proprietary information?

18 A. I might put it another way. The
19 manufacturer or vendor considers the pricing
20 information extremely proprietary. I would say even
21 more so than the purchaser.

22 Q. And are you aware that that issue has been
23 of concern in this docket in the context of U S WEST's
24 cost studies, the protection of those discount levels?

25 A. I wasn't aware that it was an issue in this

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1 proceeding.

2 Q. Going back to the Exhibit 358, Loop Dreams,
3 you would agree that the results published in that
4 paper used publicly available data, wouldn't you?

5 A. Yes, it does.

6 Q. And would you also agree that it shows a
7 range of embedded forward looking and future looking
8 costs also all based on publicly available data?

9 A. Yes. Generally all the data within TIAP
10 papers is publicly available.

11 Q. And the same is true for the BCM model?

12 A. To a large extent, the data in the BCM is
13 all publicly available data.

14 Q. And the model itself has been provided by
15 the sponsors on a public basis. Anyone can have
16 access and use the BCM?

17 A. Yes. Subject to the licensing rights, the
18 standard software licensing rights that go with the
19 model, anyone can have use of it.

20 Q. And indeed on page 13 of your testimony
21 you've indicated that it's good to have a common data
22 source for all to use in examining costs, haven't you?

23 A. Is that the supplemental?

24 Q. I'm sorry. That's in your rebuttal
25 testimony. That's at line 21 to 23.

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1 A. Yes, I see it now.

2 Q. So you would agree it's good to have a
3 common data source for all interested parties to use
4 in examining costs?

5 A. I think I said a common data source for
6 developing universal service solutions in my
7 testimony.

8 Q. And isn't part of the -- an important part
9 of the universal service funding question the
10 determination of costs, the cost of universal service?

11 A. Yes.

12 Q. In fact part of the reason that you were
13 able to address Dr. Mercer's testimony was that much
14 of the information that he was using had been provided
15 to you; isn't that correct?

16 A. What was provided by Dr. Mercer in his
17 supplemental testimony appeared to be fairly limited,
18 and it was very difficult to discern how the expense
19 factors were derived and how the business line data
20 was actually applied at a census block group level, so
21 I would differ with you.

22 Q. So it would be important for you to be able
23 to see that information and how the model works and
24 how the inputs work and what inputs work, wouldn't
25 it?

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1 A. Yes, it would.

2 Q. Were you aware that AT&T and Dr. Mercer had
3 made the offer in December to make that model
4 available to all of the parties in this proceeding?

5 A. I was not aware of that.

6 Q. And that would be an offer that would be
7 valuable and important to you in being able to
8 determine how Dr. Mercer had done his studies and how
9 the models was being used and whether you could agree
10 with the conclusions, wouldn't it?

11 A. Yes, it would.

12 MS. PROCTOR: Thank you. Nothing further.

13 JUDGE WALLIS: Other questions from
14 counsel? Mr. Nichols.

15

16 CROSS-EXAMINATION

17 BY MR. NICHOLS:

18 Q. Mr. Copeland, I believe you testified that
19 you were one of the principal developers of what you
20 call the BCM studies; is that correct?

21 A. That's correct.

22 Q. And the BCM study, you testify, is a proxy
23 cost study; is that correct?

24 A. Yes.

25 Q. And by that I think you describe it as a

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1 method of estimating the costs to serve a specific
2 geographic area without using the booked cost data of
3 a telephone company; is that correct?

4 A. Or any other cost data of the company.

5 Q. And that's the definition that appears on
6 page 4 of your supplemental testimony 356T. I will
7 just ask you to turn to that. Is that accurate?

8 A. Yes.

9 Q. And I assume that since U S WEST had you
10 become one of the principal developers of the BCM
11 study that U S WEST agrees that the use of a proxy
12 cost study is appropriate, at least with regard to its
13 filing at the FCC; is that correct?

14 A. Yes.

15 Q. I believe you explained that the purpose of
16 the FCC proceeding involved there, that is, involved
17 in which you filed the BCM model, was to help design
18 universal support mechanisms for high cost areas; is
19 that correct?

20 A. Yes, it is.

21 Q. And is it not true that the cost of the
22 local loop is the primary nontraffic sensitive cost
23 that is being measured when one estimates what the
24 cost -- what high cost areas are?

25 A. That is one of the major components, yes,

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1 it is.

2 Q. Is it not often if not usually the major
3 component?

4 A. Well, depending on densities and switching
5 arrangements, switching can be substantial amount of
6 funds, investment, but generally the loop is also one
7 of the if not the major component one of the major
8 components.

9 Q. So for purposes of estimating the costs of
10 the local loop and switching and a few other major
11 components the component has determined that a proxy
12 cost method is the appropriate procedure to follow; is
13 that correct?

14 A. The company has determined a proxy cost is
15 appropriate in order to measure across the nation high
16 cost areas based on certain characteristics in a
17 uniform manner, so a geographic area can be determined
18 that it would be high cost to serve, yes.

19 Q. Do you expect that the universal service
20 cost methodology that the FCC is anticipating
21 developing would result in actual payments to
22 individual companies in actual locales, say, in the
23 state of Washington?

24 A. If the FCC adopts some sort of proxy model
25 then eventually that would -- the reimbursements to

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1 carriers serving particular customers in
2 geographically defined high cost areas would be
3 reimbursed for a certain amount of their high cost.

4 Q. And U S WEST supports the use of a proxy
5 cost method to result in that kind of system of actual
6 payments to individual companies for high costs
7 support; is that correct?

8 A. Yes, it is.

9 Q. Would you expect that in the state of
10 Washington U S WEST would use a BCM cost or a proxy
11 cost method for determining a universal service
12 methodology here in Washington?

13 A. It's possible that a proxy model similar to
14 the BCM could be used in the state of Washington for
15 targeting high cost areas.

16 Q. You said it could be used. I was asking
17 you whether or not the company, to your knowledge,
18 intends to use such a cost method in developing
19 universal service mechanism in the state of
20 Washington?

21 A. I have no knowledge of a docket right now
22 in which U S WEST plans to propose it, but as a
23 general matter U S WEST considers the BCM the model it
24 would use for targeting high cost areas in developing
25 a state universal service fund or a federal universal

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1 service funds.

2 Q. What are the advantages of the proxy cost
3 method over actually using so-called actual or book or
4 embedded costs of an individual telephone company?

5 A. Well, there are a number of advantages, and
6 I think I discuss them in my supplemental testimony.

7 Q. What are the main ones?

8 A. Well, the main ones would include looking
9 at the territory in a uniform manner so you would have
10 a constant set of or a constant screen of data or
11 uniform screen of data to determine an area that might
12 be high cost to serve. That would be one. A second
13 advantage would be that it would encourage
14 efficiencies more in line with a price CAP approach to
15 regulation similar to the price CAP regulation that
16 exists -- regimen that exists for the large companies
17 on the interstate level. It would be more in line
18 with that. Those would be the two major advantages.

19 Q. So you see as one of the two advantages
20 that it would support a public utility Commission or
21 regulatory body in actually setting costs for a
22 company, is that correct, for its support services?

23 A. I see it as setting support levels for
24 services, explicit support levels.

25 Q. And support levels are payments made by

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1 some company or end user into some kind of pool which
2 is then paid to an individual company to support its
3 operations. Is that not right?

4 A. I personally have a different view. I look
5 at the support level as the level that a Commission
6 would deem would be appropriate to make residential or
7 local service affordable in a high cost area. I'm
8 looking at it from the funding side and not as
9 supplying the money to incident carriers to serve a
10 high cost area and to provide public support or
11 subsidy to the provision of local service.

12 Q. Do you look at it from the funding side
13 because U S WEST would in a regimen would most likely
14 be receiving money in some circumstances rather than
15 paying into the service fund?

16 A. I think U S WEST would be both a payor and
17 receiver and it would depend on the state on that mix.

18 Q. I believe you also testified that benchmark
19 cost studies are consistent with competition; is that
20 correct?

21 A. Yes.

22 Q. Why is that?

23 A. The reason that we feel that it's
24 consistent with competition is that any carrier that
25 says that it will serve or hold itself out to serve

02800

1 anyone in a high cost census block group would be
2 eligible to receive high cost support, that those
3 funds would not only go to the incumbent they would
4 go to anyone who holds themselves out to serve the
5 entire census block group that was identified as a
6 high cost area. In that way it provides -- it does
7 not eliminate competition in these areas due to one
8 carrier getting a subsidized -- providing a subsidized
9 service while its competitor might not be eligible to
10 receive that subsidy.

11 Q. But is it your testimony that the company
12 does not support any type of proxy cost methodology
13 study, be it BCM or others, for any other purpose
14 other than universal service mechanism creation?

15 A. I think my testimony states that proxy
16 model is not appropriate for use as a LRIC study of
17 company costs to develop a cost for local service
18 because the proxy model can't identify the costs
19 incurred by the company, so therefore you cannot
20 develop a LRIC price floor or a cross subsidy test
21 with a proxy because it does not reflect the costs of
22 the individual company, so therefore you cannot use it
23 that way.

24 Q. Has any party or any individual witness in
25 this docket proposed that a BCM study be used as a TS

02801

1 LRIC study? They haven't, have they?

2 A. I think when parties suggest that it be
3 used for pricing purposes they're suggesting it be
4 used as a TS LRIC study.

5 Q. Does U S WEST use the ADSRC studies as a
6 target price study that is useful to them and they
7 argue to this Commission in setting prices?

8 A. I think you need to refer to Mr. Farrow's
9 testimony on that.

10 Q. You've never performed a TS LRIC study,
11 have you?

12 A. No, I haven't.

13 Q. And you're not in a costing group that
14 performs TS LRIC studies, are you?

15 A. No, I'm not in a costing group.

16 Q. Have you examined the studies, the costing
17 studies, submitted by the company in this docket
18 submitted by U S WEST for pricing purposes?

19 A. No, I haven't.

20 MR. NICHOLS: I have no further questions.

21 JUDGE WALLIS: Commissioners.

22 CHAIRMAN NELSON: No.

23 COMMISSIONER HEMSTAD: No.

24 COMMISSIONER GILLIS: I have one.

25

02802

1 EXAMINATION

2 BY COMMISSIONER GILLIS:

3 Q. I'm just wondering, Mr. Copeland, do you
4 have an opinion about the implication of potential
5 wireless loop technologies for loop costs in low
6 density markets?

7 A. I think wireless loop services would
8 definitely change the cost curve, and if they become
9 available meeting the power and capacity requirements,
10 something like that, if a proxy model like the BCM
11 moves forward it would have to reflect those kinds of
12 costs.

13 Q. Would you see that as leading to sort of a
14 convergence in cost of loops in rural and urban areas
15 in a wireless technology?

16 A. I'm not sure if I know about the cost of
17 these upcoming technologies to really make a judgment
18 on that.

19 COMMISSIONER GILLIS: Thank you.

20 JUDGE WALLIS: Mr. Shaw.

21

22 REDIRECT EXAMINATION

23 BY MR. SHAW:

24 Q. Couple of questions. Mr. Copeland, are you
25 aware of any statement in writing or orally delivered

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1 to you or the company from AT&T or Dr. Mercer to make
2 any access available to a modified BCM model?

3 A. No, I am not aware of any such statement,
4 and I talked to Dr. Mercer fairly regularly and he
5 never mentioned it to me.

6 Q. Was AT&T invited to be a joint sponsor of
7 the BCM model to the FCC?

8 A. In the early days of the development of the
9 U S WEST high class targeting model, which I view as a
10 predecessor, we made a presentation of that
11 methodology to AT&T and MCI jointly, and from that
12 AT&T said they would study it but MCI thought we had
13 enough in common to join us as part of the joint
14 sponsors.

15 Q. Did AT&T decline to join it as a joint
16 sponsor or just did not follow up on the presentation?

17 A. I would characterize it more as they did
18 not follow up on the presentation.

19 MR. SHAW: Nothing further.

20 JUDGE WALLIS: Is there anything further?

21

22 RE-CROSS-EXAMINATION

23 BY MS. PROCTOR:

24 Q. Mr. Copeland, did you participate in a
25 conference call amongst all of the experts in this

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1 case, all of the experts who were interested in
2 costing issues?

3 A. In this particular case?

4 Q. That's correct.

5 A. No, I didn't.

6 Q. And no one from U S WEST, for example,
7 Mr. Shaw who participated in that call, conveyed to
8 you the offer by AT&T to make the model available to
9 anyone who wanted to run it?

10 MR. SHAW: Your Honor, I am going to object
11 at this point. I would like to testify a little bit
12 myself here. I was on that call and it was before Dr.
13 Mercer filed his supplemental testimony and there was
14 simply no offer to review something that we didn't
15 even know existed, so to the extent there's any
16 inference in these questions that Ms. Proctor made an
17 offer to me or any other representative of U S WEST to
18 review the supplemental testimony of Dr. Mercer in
19 depth is just simply not the case.

20 MS. PROCTOR: I think the question was, was
21 he made aware of that offer. I would expect his answer
22 would be no and that would be the end of the inquiry.

23 MR. SHAW: Well, I object to the
24 implication that there was ever such an offer made at
25 any such conference call because it's simply not true.

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1 MR. TROTTER: Your Honor, that causes me to
2 butt in because I was on that call, and it may even be
3 in the context of settlement, but whatever, I do
4 recall there being made an offer of a model and I
5 can't remember exactly what it was, but talking about
6 credibility of people here I will jump in and give my
7 two bits.

8 JUDGE WALLIS: We'll call these
9 representations of counsel rather than testimony,
10 unless you would all like to be sworn. I think under
11 the circumstances the witness may respond to the
12 question.

13 A. I was aware of no offer.

14 MS. PROCTOR: Thank you.

15 JUDGE WALLIS: All right. Is there
16 anything further for Mr. Copeland this evening? It
17 appears that there is not. Mr. Copeland, thank you
18 for appearing. You're excused from the stand. Let's
19 be off the record for a brief discussion on
20 administrative matters.

21 (Hearing adjourned at 5:40 p.m.)

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