GTE NORTHWEST INCORPORATED

DIRECT TESTIMONY OF

ALLEN E. SOVEREIGN

WUTC UT-961632

INTRODUCTION

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

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

Q. WOULD YOU BRIEFLY DESCRIBE YOUR EDUCATIONAL BACKGROUND?

A. Yes. I received a Bachelor of Science Degree in Electrical Engineering from Michigan Technological University, Houghton, Michigan, in 1971. I received a Master of Science Degree in Business Administration from Indiana University, Bloomington, Indiana, in 1980. I have attended courses in depreciation and life analysis provided by Depreciation Programs, Inc., of Kalamazoo, Michigan. I have also attended and instructed basic and advanced GTE courses in depreciation life analysis. I am a Senior Member of the Society of Depreciation Professionals.

Q. BRIEFLY DESCRIBE YOUR WORK EXPERIENCE WITH GTE.

A. I have worked with GTE for 22 years, with 15 of those years in the Depreciation study area. I have held various positions in Engineering and Construction, Capital Budgeting, Marketing, and Product Development. I was named Manager of Capital Recovery in February 1994.

Q. WHAT ARE THE RESPONSIBILITIES OF YOUR CURRENT POSITION?

A. I am responsible for the preparation, filing, and resolution of capital recovery studies for GTE telephone operating companies and the determination of economic lives for financial reporting.

Q. HAVE YOU PREVIOUSLY TESTIFIED WITH ANY REGULATORY BODIES?

A. Yes, I have testified before the Texas, New Mexico, California, Idaho, Pennsylvania, Michigan, Indiana, South Carolina, Virginia, Kentucky, and the Hawaii state utility commissions.

Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?

A. The purpose of this testimony is to sponsor and support depreciation rates proposed for GTE Northwest Incorporated ("GTE") in the state of Washington and request the Commission to approve the proposed depreciation rates.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. In this testimony, I show that:

1) Mortality analysis used in the traditional historical methodology for developing depreciation rates is outdated and inappropriate.

2) The changing telecommunications environment must be considered when determining the proper recovery period of an asset.

3) The depreciation rates proposed by GTE are clearly reasonable when compared to unregulated telecommunications providers.

Q. WHAT IS THE PURPOSE OF DEPRECIATION ACCOUNTING?

A. According to Generally Accepted Accounting Procedures (“GAAP”), the objective of depreciation accounting is to allocate the cost of investment used to provide service over the useful life of the asset in a systematic and rational manner. This allocation implies that the purpose of depreciation accounting is to charge to

operations the cost of the service of an asset that is consumed during an accounting interval. The accepted method has been to use "straight line" depreciation. Simply put, this is a time based allocation, where, for example, a $100 investment would be allocated over a ten year period at $10 per year. Depreciation theory provides that plant costs should be allocated in proportion to the consumption of service capacity, however, the consumption of service capacity most likely will not be properly simulated using a straight line allocation. Because the use of straight line methods will continue, the determination of economic lives must retain the flexibility to adjust for the rapid changes in the economic value.

Q. IF USEFUL LIFE IS THE PERIOD OF TIME AN ASSET IS PROVIDING SERVICE, SHOULD THE PERIOD OF TIME THE ASSET IS "ON THE BOOKS" BE A SURROGATE FOR USEFUL LIFE?

A. No. The "useful life" of an asset may not correspond to the time an asset is "retired" on a regulated company's books. Rather, an asset's useful life should be evaluated on the basis on several factors, including some of those in the guidelines published by the National Association of Regulatory Utility Commissioners ("NARUC"). NARUC's factors are as follows[1]:

1. Physical Factors
   a. Wear and tear
   b. Decay or deterioration
   c. Action of the elements and accidents

2. Functional Factors
   a. Inadequacy
   b. Obsolescence
   c. Changes in art and technology

[1] National Association of Regulatory Utility Commissioners, Public Utility Depreciation Practices 15 (1996).

d. Changes in demand
e. Requirements of Public Authorities
f. Management discretion

3. Contingent factors
   a. Casualties or disasters
   b. Extraordinary obsolescence

I agree that these items are considered with appropriate weighting in the determination of useful or economic lives. However, I do not believe that booked retirements are reflective of the total impact on the consumption of service value caused by the above factors. For example, plant investment may remain on the books without any remaining economic life.

Q. PLEASE EXPLAIN.

A. As new providers enter the local service market, GTE will no longer be the sole provider of such services. If a new entrant, such as a cable television provider or a cellular provider, becomes the provider of choice for a portion of GTE's customers, and those customers end their relationship with GTE, the investment in plant formerly used to provide service to those customers may no longer be economically useful, but it will remain on GTE's books.

Q. HOW IS USEFUL OR ECONOMIC LIFE DETERMINED?

A. As discussed above, the factors listed in the NARUC publication are considered with proper weighting. In subsequent sections of this testimony, I will discuss these factors in more detail. In the section titled "Changing Telecommunications Environment," I discuss the factors "changes in demand" and "requirements of public authorities." "Technological Change" includes a discussion of how the industry studies prepared by Technology Futures Inc. were used in the determination of economic lives. The NARUC factors considered in this section

are inadequacy, obsolescence, and changes in the art and technology. Finally, the section "Historical Analysis is not Predictive of Future Events" is a discussion about why virtually no weight was given to the physical causes of retirement, namely wear and tear, action of the elements, deterioration, and decay.

Q. WHY IS THIS TYPE OF FILING NECESSARY?

A. Because of rapidly changing technology and the evolving competitive environment, detailed analysis of mortality data (i.e., historical asset retirements) in the traditional regulatory depreciation filing is no longer a viable tool for setting depreciation rates. The determination of proper depreciation rates must transition from heavily weighted historical analysis to forecasts more heavily weighted towards the impacts of the changing telecommunications environment. Traditional historical analysis is no longer appropriate or relevant in today's environment, much less tomorrow's. Economic life is the appropriate measure of the proper recovery period. Economic life measures the time period over which a new asset will produce a positive net revenue stream, such that the present value is equal to the original cost of the asset. This filing is a forward-looking prospective view that emphasizes factors of today's evolving competitive marketplace.

Q. IS THIS FILING REQUESTING CHANGES FOR ALL ACCOUNTS?

A. No. The filing, Exhibit AES-1, lists all accounts, but GTE is requesting changes only to the eight (8) accounts below:

2212.00 - Digital Switching Equipment
2232.00 - Circuit Equipment
2421.10 - Aerial Cable Metallic
2421.20 - Aerial Cable Non-metallic
2422.10 - Underground Cable Metallic

2422.20 - Underground Cable Non-metallic
2423.10 - Buried Cable Metallic
2423.20 - Buried Cable Non-metallic

The proposed changes in rates are provided on Exhibit AES-1.

Q. WHY WERE ONLY EIGHT ACCOUNTS REVIEWED IN THIS FILING?

A. These are the accounts that contain the telecommunications assets that are most impacted by the combined effects of technological change and competition.

Q. ARE THE CURRENT DEPRECIATION RATES SUFFICIENT IN TODAY'S ENVIRONMENT?

A. No. Current depreciation rates will fail to achieve the goals and objectives of depreciation accounting and will deny GTE an opportunity for capital recovery under competitive market pricing.

Q. WHAT ARE GTE'S ESTIMATED ECONOMIC LIVES FOR THE ASSET CATEGORIES IN THIS FILING?

A. The estimated economic lives for GTE are: copper cable 15 years, digital switching 10 years, circuit equipment 8 years, and fiber cable 20 years.

Q. DID YOU ALSO ESTIMATE ECONOMIC REMAINING LIVES FOR THESE ACCOUNTS?

A. Yes. The estimated economic remaining lives are: copper cable 6 years, digital switching 6 years, circuit equipment 4 years, and fiber cable 15 years.

Q. HOW WERE THESE ECONOMIC LIFE ESTIMATES DEVELOPED?

A. GTE consulted relevent studies produced by Technology Futures, Inc. (TFI) and evaluated the results of those studies based on GTE's engineering and planning expertise. We found the TFI results to be credible, and, again using GTE's expertise, selected lives within the ranges produced by the TFI studies. We then

checked our estimates against the lives used by other telecommunications companies, such as AT&T and Regional Bell Operating Companies, which validated our estimates.

Q. HOW DOES THE ECONOMIC LIFE RELATE TO THE ECONOMIC REMAINING LIFE?

A. The economic life is the total life expectancy at age zero. The remaining life is how much longer the asset will produce a positive net revenue stream beyond a given observed age. The remaining life calculation for a group of assets recognizes that some of the useful life has been consumed in prior periods.

Q. HOW WERE THE PROPOSED RATES DEVELOPED?

A. The rates were developed by using the remaining life formula:

(100% - FNS% - Reserve Ratio%) / Remaining Life.

The proposal retains the existing currently prescribed regulatory Future Net Salvage ("FNS"). The reserve ratio was updated to reflect actual year end balances. The existing currently prescribed regulatory remaining life was replaced by the GTE estimated economic remaining life.

Q. PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY.

A. Plant retirement patterns are no longer a viable method for projecting the useful life of plant investment in a competitive environment. GTE, in this filing, has proposed economic lives for the eight plant categories most impacted by technology and competition. Technology forecasting studies and other forward-looking factors were used to determine the economic lives. The resulting economic remaining life, approved future salvage, and current accounting data were used in the traditional remaining life formula to determine the proposed

rates.

CHANGING TELECOMMUNICATIONS ENVIRONMENT

Q. WHAT ARE SOME OF THE CHANGES THAT ARE OCCURRING IN THE TELECOMMUNICATIONS INDUSTRY?

A. One only need read the newspapers and magazines to see that the telecommunications industry is in the process of a significant history-making change. AT&T, among others, has stated that it intends to offer local exchange service in all states by the end of the year, and predicts taking a significant market share from local exchange companies. The Telecommunications Act of 1996 and various state proceedings are expected to accelerate these changes.

Q. COULD YOU GIVE YOUR VIEW OF HOW COMPETITION COULD AFFECT THE ECONOMIC LIFE OF THE EXISTING NETWORK?

A. Yes. The new competition in the local service market coming from interexchange carriers ("IXCs") such as AT&T and from competitive local exchange carriers ("CLECs") is well known. Regional Bell Operating Companies ("RBOCs") are also seeking to compete as CLECs outside their traditional service areas. Some of the earliest CLEC activitiy was in Washington. Other competitors are now also appearing. As an example, in many areas personal communication system ("PCS") providers and cable television telecommunications providers will be offering services in competition with GTE. These competitors are likely to bypass much, if not all, of GTE's distribution facilities. A PCS provider would have no need for any GTE cable facilities, and cable television providers could offer service over their own existing coaxial cable and fiber optic cable networks. If these alternative providers capture 20% of the market, for example, the net

revenue stream available for capital recovery would be reduced and the remaining economic life of these facilities would most likely be shorter than it was prior to the emergence of competition.

Next, let us assume that an IXC, RBOC, alternative access provider, and an electric company decided to also offer local service in GTE's territory. The electric company could use its existing distribution facilities and bypass GTE's facilities, capturing more customers and resulting in a further reduction in the remaining economic life of the assets. An IXC or RBOC could either use or build its own facilities, or be a reseller. The IXC already has a customer base with its existing long distance service. The alternate access provider could provide access via its own fiber rings that already pass a significant portion of GTE's customers. In all these cases, capital recovery would be threatened by economic forces beyond GTE's control.

Q. HOW DOES THE INTRODUCTION OF LOCAL COMPETITION CHANGE GTE'S ABILITY TO RECOVER ITS CAPITAL INVESTMENT OVER TIME?

A. In a competitive environment, the opportunity for capital recovery which was premised on the regulatory compact associated with a single provider regulatory environment, no longer exists. Regulated lives approved by the Commission have been artificially long in order to keep customer rates lower. The shorter lives used by companies in a competitive environment result in more timely recovery of capital. As GTE enters the competitive arena, it becomes increasingly difficult to recover its investment in plant that no longer has economic benefit. Future pricing cannot include costs associated with plant rendered useless because of competition, technology, and regulatory changes.

Q. PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY.

A. Competition requires that the regulated depreciation process of the past be changed. Past practices did not consider competition in the timing of capital recovery. Recognition of the economic usefulness of plant must be the primary factor in recovering asset investment.

TECHNOLOGICAL CHANGE

Q. DID GTE RELY SOLELY ON IT'S OWN ANALYSIS OF FUTURE TRENDS?

A. No. In addition to GTE's own analysis of future trends, we relied on Technology Futures Inc. ("TFI") to quantify and collaborate our professional opinions. In a competitive market, it is vital to consider industry studies that depict the industry trends rather than looking at only individual GTE plans in a vacuum. Dr. Lawrence Vanston of TFI has also submitted testimony in this proceeding in support of GTE's proposed depreciation lives.

Q. WHY HAS GTE USED STUDIES PREPARED BY TECHNOLOGY FUTURES, INC.?

A. TFI studies quantify the uncertainties of the future through the use of tested modeling and forecasting tools. TFI replaces judgmental adjustments with a more disciplined approach based on mathematical predictions of technological advances as well as other developments in the industry. In its studies, TFI employs proven modeling tools and has demonstrated its reliability in predicting the future substitution of technologies.

Q. PLEASE EXPLAIN THE SIGNIFICANCE OF THE STUDIES DONE BY TFI.

A. TFI is an independent corporation that utilizes substitution analysis in technology forecasting and strategic planning for several industries, including technology

forecasts for the telecommunications industry since 1984. These studies provide quantitative forecasts for the adoption of new technology, primarily for switching equipment, outside plant, and circuit equipment.

Q. WHAT IS SUBSTITUTION ANALYSIS AND HOW WAS IT USED?

A. Substitution analysis is used to project remaining lives for plant investment when technological change is driving a shortening of asset lives. The use of technological substitution models employed by TFI is superior to the mortality models previously used under regulation without competition. To quantify this technological change, TFI employs a model to analyze remaining economic lives using patterns of technological substitution observed in other industries, as well as the communications industry. The substitution analysis conducted by TFI recognizes the combined effects of competition and technological change. The total impact generally projects shorter lives than those currently prescribed by the Commission.

Q. GIVEN THE NEED TO INCLUDE THE IMPACT OF THE CHANGES THAT ARE OCCURRING CURRENTLY, AND ARE LIKELY TO OCCUR IN THE FUTURE IN THE TELECOMMUNICATIONS INDUSTRY, WHEN DEVELOPING DEPRECIATION RATES, PLEASE EXPLAIN HOW GTE INCLUDED THOSE FACTORS IN ITS PROPOSED DEPRECIATION RATES.

A. As I stated earlier, an important component of a prospective depreciation proposal is to not only look at GTE plans but to also look at industry patterns and trends. The TFI study presents a thorough and proven analysis of such trends.

Q. WHY DO YOU BELIEVE THE TFI STUDY UTILIZED BY GTE IN DEVELOPING ITS PROPOSED DEPRECIATION RATES PROVIDES A RELIABLE OUTLOOK

APPLICABLE TO GTE?

A. TFI relies on data collected from many sources, including regulatory reports such as those provided in the Automated Reporting Management Information Systems ("ARMIS"). Data from GTE, as well as from numerous other providers, serves as the basis for the study's conclusions.

Q. WHAT DOES TFI RECOMMEND FOR CENTRAL OFFICE EQUIPMENT, COPPER CABLE AND FIBER CABLE ACCOUNTS AND HOW DO THEY COMPARE WITH GTE'S PROPOSAL IN THIS PROCEEDING?

A. The chart below compares TFI recommended ranges[2] with GTE's economic life proposal:

	LIFE		REMAINING LIFE	
	TFI	GTE	TFI	GTE
CENTRAL OFFICE EQ.				
Digital	9-11	10	6.3-6.9	6
Circuit	6-9	8	2.8-3.7	4
COPPER CABLE				
Aerial	14-16	15	2.9-8.7	6
Underground	14-16	15	2.9-8.7	6
Buried	14-16	15	2.9-8.7	6
FIBER CABLE				
Aerial	15-20	20	na	15
Underground	15-20	20	na	15
Buried	15-20	20	na	15

TFI specifically addresses the appropriate lives to be used for Outside Plant cable, Central Office Switching, and Circuit Equipment accounts, as these are the accounts that are most impacted by changes in technology and competition.

Q. PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY.

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[2] Larry K. Vanston and Ray L. Hodges, Depreciation Lives For Telecommunications Equipment: Review and Update 33 (Technology Futures, Inc. 1995).

A. Technology forecasting models and studies such as those used by TFI are superior to the traditional mortality models for determining depreciation lives in an environment of rapidly changing technology and mandated competition. The lives proposed in this filing are generally consistent with the ranges recommended in these detailed studies that utilized extensive industry data.

HISTORICAL ANALYSIS IS NOT PREDICTIVE OF FUTURE EVENTS

Q. HOW HAS GTE RECOVERED CAPITAL UNDER REGULATION?

A. Investors expect both a return on invested capital and the return of invested capital. In an unregulated competitive environment, the degree of success is determined by management decisions, associated depreciation practices, and competition. For a regulated company, both profits and depreciation rates are limited by regulation, which has generally been considered a surrogate for competition. Under regulation, depreciation rates are reviewed by the Commission periodically, customarily once every three years. Depreciation parameters are prescribed in these periodic reviews. This review process has provided a forum for all interested parties to express their opinions about the rate at which GTE's investment should be charged to operations. The Commission ultimately decides what depreciation rates should be used to determine the annual depreciation expense. This decision considers the associated impact on customer prices. A decision to shorten the lives of the assets would increase the expense level that would be charged in customer prices. Because GTE's ability to change customer prices is constrained by regulation, its ability to recover depreciation expense is also constrained. However, so long as a single provider environment remained for local exchange service, the implicit opportunity for

recovery of GTE's capital investment also remained. Capital recovery was based on mortality analysis, and because competition did not exist, only the timing of recovery was an issue.

Q. CAN YOU BRIEFLY EXPLAIN WHY THE USE OF HISTORICAL ANALYSIS TO PREDICT RETIREMENTS IS INAPPROPRIATE?

A. Yes. The models used for historical analysis assume that historical retirement trends will extend into the future. The telecommunications technology revolution, introduction of competition, and regulatory changes made that basic assumption invalid. Past trends will have little to do with future retirements. Therefore, mortality models are of little use in establishing depreciation parameters.

Q. WHAT IS PREDICTED USING MORTALITY ANALYSIS?

A. Physical life is predicted, but not economic life. At best, physical life can be predicted using retirements caused primarily by the physical factors mentioned earlier. These factors are wear and tear, decay, and action of the elements.

Q. WHY DO YOU DISTINGUISH BETWEEN THE PHYSICAL LIFE OF AN ASSET AND THE ECONOMIC LIFE OF AN ASSET?

A. The physical life is how long an asset remains capable of providing service. Mortality analysis does a good job of predicting when the asset retires from service if its economic life exceeds its physical life and must be replaced in kind. However, an asset will not likely provide service or remain useful over its physical life if the economic life is shorter.

Q. PLEASE PROVIDE AN EXAMPLE THAT WILL ILLUSTRATE HOW USEFUL LIFE CAN BE IMPACTED WHEN NO RETIREMENTS ARE EVIDENT.

A. Under current accounting guidelines, partial retirements are not allowed. If GTE

has a 1,000 pair cable with only 100 pairs working (as a result of 900 customers leaving for competitors' networks), retirement of the cable is not permitted. It is not allowed, under current procedures, to retire 90% of the investment. Mortality analysis assumes that everything still in service is useful. However, under this scenario only 10% of the original investment is actually useful. The useful life is severely impacted but there are no associated retirements.

Q. CAN A COMPANY'S CURRENT TECHNOLOGY DEPLOYMENT PLANS FULLY PREDICT RETIREMENTS, AND SUBSEQUENTLY BE USED TO PREDICT USEFUL LIFE?

A. No, not in today's environment. Such plans typically do not extend as far into the future as economic lives. Moreover, rapidly accelerating changes in technology, regulation, and competition have resulted in a dynamic network. Plans will constantly change to react to competitive market decisions, and construction decisions will occur in a shorter time frame than in the past. Again, retirements will not be determined by plans. Replacement of switches and cables will no longer be determined by growth and exhaustion, but by technology and competitive strategies.

Q. WOULD YOU PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY?

A. Yes. Models that attempt to project asset lives based on analysis of retirement trends are not valid in today's competitive telecommunications environment. The useful life of an asset will be determined by technology and competition, not retirements.

REASONABLENESS OF DEPRECIATION FILING

Q. ARE THE RATES AND PARAMETERS PROPOSED IN THIS FILING

CONSISTENT WITH WHAT GTE WOULD USE IF IT WERE NOT REGULATED?

A. Yes. GTE's financial books were adjusted to reflect the use of economic lives.[3]

Q. HOW DOES THE SHIFT FROM A REGULATED TO A COMPETITIVE AND DEREGULATED ENVIRONMENT AFFECT GTE?

A. Over the years GTE has made prudent investments to provide quality service to its customers and to fulfill its Carrier of Last Resort obligation in the context of being the sole service provider in its territory. As a consequence, the Commission regulated and controlled the prices of the services GTE charged its customers, as well as its depreciation rates associated with these investments. Under this regulatory compact, GTE has been assured the opportunity for full recovery of all of its investments over a Commission authorized period of time. This has helped to keep basic local exchange service rates affordable, in order to accomplish the Commission's universal service goal. This arrangement worked well in a single provider environment. However, the FCC and state commissions are now changing these policies to encourage competition in the marketplace. By allowing the introduction of competition, recovery of these investments is increasingly unlikely in future years.

Q. ARE THE DEPRECIATION RATES PROPOSED BY GTE REASONABLE WHEN COMPARED TO NON-REGULATED TELECOMMUNICATIONS PROVIDERS?

A. Yes. A good comparative measure is to look at differences in the overall composite depreciation rate that results from all of the individual rates proposed.

[3] GTE filed an 8K report reflecting this adjustment on November 9, 1995 with the Securities and Exchange Commission.

The Company's proposed composite rate in this filing is 11.0%. The following table compares rates used by other providers of telecommunication services.

Comparison of Composite Rates
to Other Telecommunications Providers

Company	Composite Rates[4]
AT&T	8.69%
MCI	9.89% Airtouch 10.77%
US Cellular	10.07%
TCI	9.05%
COX	11.99%
MFS	9.88%

The depreciation rates proposed by GTE are clearly reasonable as demonstrated by comparing the composite depreciation rate to the rate currently being used by competitors. In fact, having been denied the appropriate capital recovery rates in prior years, it is now reasonable that GTE's composite rate should be higher than its competitors in order that the existing plant may be recovered over its remaining economic life. GTE's proposed economic lives are also reasonable in comparison with the lives that the Regional Bell Operating Companies used to determine their economic depreciation.

Q. DO YOU HAVE FURTHER EVIDENCE OF THE REASONABLENESS OF GTE'S REQUESTED ECONOMIC LIVES?

[4] Source: Arthur Andersen report, Net Results 1996 The Arthur Andersen Annual Report on the Communications Industry.

A. Yes. Comparing the GTE economic lives with the lives used by AT&T is an excellent example of the reasonableness of GTE's economic lives. In fact, GTE's lives are even more conservative than the lives used by AT&T,[5] as illustrated by the chart below.

	AT&T LIFE	GTE LIFE
Digital Switching	9.7	10.0
Digital Circuit Equipment	7.2	8.0
Copper Cable	3.4-15.0	15.0
Fiber Cable	20.0	20.0

Q. PLEASE SUMMARIZE THIS SECTION OF YOUR TESTIMONY.

A. Competition, technology, legislation, and regulatory reform necessitated changes in the depreciation process. GTE's financial books were adjusted to reflect the reality of the competitive marketplace. GTE companies also have booked depreciation rates based on economic lives in all jurisdictions where allowed. Over 50% of GTE telephone operating companies' total investment is now being depreciated over economic lives on their regulated books. Economic depreciation filings are being submitted in all remaining jurisdictions.

SUMMARY

Q. WHY SHOULD ECONOMIC LIVES BE IMPLEMENTED FOR DEPRECIATION?

A. Economic depreciation measures the decline in an asset's market value from all causes, including competition and technological change. Capital recovery, consistent with economic depreciation, promotes efficient competition and consumer welfare. When all services were monopoly services, regulators could

[5] This information was taken from the publicly available documentation filed by AT&T in relation to FCC proceeding 95-32.

defer capital recovery without affecting the mix of customers or services that would end up paying. With the advent of local competition, regulators no longer have the luxury of postponing capital recovery. Doing so will inevitably expose ratepayers to higher telephone bills.

Q. HOW SHOULD THIS SITUATION BE CORRECTED?

A. GTE should be granted the depreciation rates set forth in Exhibit AES-1, or be granted the option to implement depreciation rates absent Commission review. The Commission must take responsibility for its past decisions and act to arrive at an equitable solution for both GTE and its customers.

Q. PLEASE SUMMARIZE YOUR TESTIMONY.

A. A proper analysis in the determination of depreciation expense must be multi-dimensional. The historical methodology for developing proposed depreciation rates is outdated. The changing telecommunications environment must be considered when determining the proper recovery period of an asset. Economic depreciation measures the decline in an asset's life from all causes, giving proper weight to the impact of competition and technological change, as well as the physical causes of retirements. GTE factored these changes into its depreciation proposal. GTE's proposed rates are consistent with the rates of nonregulated telecommunications providers.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.