

Exhibit No. ___ (JAR-7)
Docket No. UT-040788
Witness: James A. Rothschild

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

VERIZON NORTHWEST INC.,

Respondent.

DOCKET NO. UT-040788

**EXHIBIT TO TESTIMONY
OF
James A. Rothschild**

**EXPERT WITNESS FOR
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

**Re: Cost of Capital
Verizon NW Response to Staff Data Request No. 306**

November 22, 2004

Data Requests Directed to Verizon Witness Dr. Vander Weide:

DATA REQUEST NO. 306:

Regarding Dr. Vander Weide's testimony in Exhibit No. ____ (JVW-1T), at page 14, lines 4-8, Dr. Vander Weide says that rapidly changing technology reduces the cost of entry for competitors. a) Please explain whether the cost of new equipment that can be purchased by competitors has dropped enough so that the cost of the new equipment is less than what it cost Verizon after subtracting accumulated depreciation and accumulated deferred income taxes from Verizon's original cost? If your answer is in the affirmative, please provide the basis for that belief. b) Please explain whether it would be more economical for Verizon NW to take advantage of the cost reduction feature of new equipment by immediately replacing that equipment with the newer, less costly equipment? If not, please explain why not. c) Please explain whether lowering costs for equipment also benefits Verizon because it means that when the time comes for Verizon to replace its equipment, it will be able to do so at a lower cost?

RESPONSE:

- (a) Dr. Vander Weide has not studied whether the cost of new equipment that can be purchased by competitors has dropped below the book value of the equipment Verizon NW currently uses to service its customers.
- (b) If it is more economical for Verizon NW to replace existing equipment with new less-costly equipment, it will certainly do so.
- (c) If equipment prices decline, Verizon NW will be able to replace its equipment at the time it becomes economical to do so at a lower cost. However, in a world of declining equipment costs, as Dr. Vander Weide explains in his testimony, Verizon NW's ability to recover the investment costs of new telecommunications plant becomes more uncertain and the entry costs of competitors are greatly reduced. Thus, rapidly changing technology increases Verizon NW's risk.

Prepared By: James H. Vander Weide
Date: June 28, 2004
Witness: James H. Vander Weide