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**SUPPLEMENTAL TESTIMONY OF  
JOSEPH GILLAN  
ON BEHALF OF AT&T COMMUNICATIONS OF  
THE SOUTHERN STATES, INC.  
BEFORE THE  
FLORIDA PUBLIC SERVICE COMMISSION**

**Docket No. [REDACTED]**

**Filed: August 23, 1996**

**INTRODUCTION**

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

**A. My name is Joseph Gillan. My business address is P. O. Box 541038, Orlando, Florida 32854.**

**Q. IS THIS TESTIMONY SUPPLEMENTAL TO YOUR PRIOR DIRECT TESTIMONY IN THIS MATTER?**

**A. Yes.**

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

**A. The purpose of this supplemental direct testimony is to explain the impact of the Federal Communications Commission's ("FCC") Rules implementing Sections 251**

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1 and 252 of the Act on the policy prescriptions and recommendations contained in my  
2 prior direct testimony to this Commission. First Report and Order, Federal  
3 Communications Commission, CC Docket 96-98, August 8, 1996 ("FCC Order").

4

5 The recent FCC regulations provide additional detail concerning this Commission's  
6 role deciding the fundamental issues in this arbitration:

7

- 8 • Which network elements should be provided immediately;
- 9
- 10 • What cost standard should apply to their pricing;
- 11
- 12 • Which services should be resold at wholesale rates;
- 13
- 14 • How the wholesale price differential should be calculated; and
- 15
- 16 • What standards should be used to judge the adequacy of operational support  
17 systems.

18

19 The FCC Order moves the Act one step closer to implementation. However, it will be  
20 this Commission's resolution of the issues that actually determine the choices that  
21 Florida consumers face, and the prices that they pay.

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23 **Q. ARE THE RECOMMENDATIONS IN YOUR DIRECT TESTIMONY**  
24 **CONSISTENT WITH THE FCC'S RULES?**

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A. Yes, in virtually every respect. Overall, the FCC's rules reflect the Act's intention to rapidly open local markets to competition through the implementation of the principle that the incumbent's network should be available to new entrants on terms that are non-discriminatory when judged against the use of this network by the incumbent itself. This principle of non-discrimination is given effect through rules requiring that the price of carrier-to-carrier network arrangements be based on economic cost and the requirement that operational support systems -- the systems which support ordering, provisioning, billing and maintenance -- provide entrants access to network elements on the same basis that network elements are used by BellSouth to provide its own services.

In one respect, however, the FCC departed dramatically from these principles with its adoption of an interim surcharge that it will permit the incumbent LECs to impose on purchasers of the unbundled local switching element. 47 C.F.R. § 51.515(b). This temporary surcharge will last no later than June 30, 1997, but while it is in effect, the usefulness of unbundled local switching to provide competing local exchange services is drastically reduced. The FCC rules also provide the states the *option* of adopting a similar interim plan. 47 C.F.R. § 51.515(c). Such a plan is unnecessary and is likely to lead only to fewer choices to consumers and/or higher consumer prices. The Florida Commission should not adopt a transitional surcharge mechanism.

The FCC Rules Are Consistent with the Direct Testimony

Q. PLEASE SUMMARIZE THE POLICY RECOMMENDATIONS

1           **CONTAINED IN YOUR DIRECT TESTIMONY.**

2

3    A.    My direct testimony contained a number of policy conclusions and specific  
4           recommendations. To summarize, the testimony concluded that:

5

6           •    The fundamental intention of the Act is that local markets become  
7                competitive, not just for selected customers in certain metropolitan areas, but  
8                broadly throughout a state. The only way that ubiquitous competition can  
9                become a reality, however, is if the existing BellSouth network is available  
10              for other competitors to use in providing local exchange and exchange access  
11              services. This is the core objective of the arbitration: to establish the terms,  
12              conditions and prices under which BellSouth's network and services will be  
13              available to rivals, including AT&T.

14

15          •    The principal mechanism available to the Commission to influence the prices  
16                and choices experienced by *consumers* is through its role establishing the  
17                prices and choices available to *carriers*. Under the price cap regulatory  
18                system that BellSouth has elected, this Commission's authority to directly  
19                establish consumer-prices is severely restricted. The principal path to  
20                consumer protection is choice -- choice among competing providers that are  
21                able to offer services with equal quality and comparable prices to those of the  
22                incumbent local telephone company.

23

24          •    The pricing rules under which carriers obtain the use of the incumbent's

1 network and services provide the foundation for competition for end-users.  
2 Where the entrant purchases the network functionality or facility underlying a  
3 service, the price of these elements should be their economic cost. Where a  
4 carrier purchases a wholesale service, the price of the wholesale service  
5 should be calculated by fully removing retail-related costs. Only under these  
6 pricing rules will entrants have the ability to broadly approach the market and  
7 provide the choice of local service provider described above.

8

- 9 • A competitive local environment requires operational support systems that  
10 enable entrants to translate these new carrier-to-carrier arrangements into end  
11 user services and easily implement a consumers' decision to change its local  
12 service provider without extensive delays or unnecessary costs.

13

14 Each of these core conclusions is reflected in the rules adopted by the Commission.

15

16 **Q. WHAT SPECIFIC AREAS OF YOUR DIRECT TESTIMONY WERE**  
17 **ADDRESSED IN THE FCC'S RULES?**

18

19 **A.** The FCC rules addressed the following areas of my direct testimony:

20

21 1. The scope of BellSouth's obligation to permit the resale of its local exchange  
22 services at wholesale rates and the methodology to calculate wholesale rates.

23

24 2. The appropriate economic costing standard for the pricing of network

1 elements and interconnection.

2

3 3. The appropriate economic costing and pricing standard for the transport and  
4 termination of "local" traffic.

5

6 4. The need to establish operational systems that accommodate customer choice  
7 and enable entrants to provide service using unbundled network elements and resale.

8

9 5. The ability to combine network elements to form exchange platforms to offer  
10 local exchange and exchange access services.

11

12 In the testimony which follows, I explain how each of the recommended policies  
13 contained in my prior direct testimony is either required by, or consistent with, the  
14 FCC's rules. These rules, when fully implemented, will provide the foundation for the  
15 competition that lies at the heart of the Act and my earlier testimony.

16

17 Before beginning, however, it is useful to place the FCC's rules and this arbitration  
18 into perspective. Although the FCC's rules provide additional detail concerning this  
19 Commission's role under the Act, these rules in no way diminish the importance of the  
20 decisions that will be reached here. This Commission is charged with translating this  
21 basic framework into a system of carrier-arrangements that will decide the choices  
22 and prices faced by Florida consumers. Thus, while the rules clarify that BellSouth's  
23 obligations under the Act, it is this Commission that will establish the prices and  
24 specific terms that will make local competition a reality.

25

1 Q. HAVE THE FCC'S RULES REQUIRED ANY CHANGES IN YOUR  
2 ORIGINAL RECOMMENDATIONS?

3

4 A. Yes. The one area of my direct testimony which the FCC's rules apparently preclude  
5 is the suggestion in my direct testimony that the Commission adjust the wholesale  
6 discount to correct for the above-cost pricing of access service. The FCC indicated  
7 that the wholesale discount should not consider factors other than the removal of costs  
8 avoidable by the ILECs. As a result, my earlier alternative suggestion that the resale  
9 discount be adjusted would not be in accord with the FCC's recent order.

10

11 Q. WHAT IS THE BASIC COSTING METHODOLOGY APPLICABLE TO  
12 CARRIER ARRANGEMENTS FOR NETWORK ELEMENTS,  
13 INTERCONNECTION, TRANSPORT AND TERMINATION REQUIRED  
14 BY THE FCC'S RULES?

15

16 A. The FCC's rule require that the basic components of exchange networks -- unbundled  
17 network elements, interconnection, transport and termination -- be priced according to  
18 economic costing principles, labeled by the FCC as "Total Element Long Run  
19 Incremental Costs" ("TELRIC"). FCC Order, ¶ 678. TELRIC is the application of  
20 the TSLRIC pricing principles to *network elements* as recommended in my prior  
21 direct testimony.

22

23 Under the FCC's "TELRIC" methodology, the price of network elements should  
24 collectively recover the forward-looking, long-run costs of providing network  
25 elements, including the costs of the managerial and administrative functions necessary

1 to support a network-element company. These managerial and administrative costs  
2 are directly caused by network elements in the aggregate, but cannot easily be  
3 attributed to specific, individual, network elements. Because of the presence of these  
4 “forward looking common costs” of providing network elements, the FCC's rules  
5 permit the price of each *individual* network element to be increased above its  
6 individual “TELRIC” to recover a portion of the *network-element-related* common  
7 costs. This pricing rule is identical to the recommendation of my prior direct  
8 testimony.

9  
10 **Q. DID THE FCC RECOGNIZE THE IMPORTANCE OF EASILY**  
11 **ACCOMMODATING CUSTOMER CHOICE?**

12  
13 **A.** Yes. Two provisions of the FCC's rules, in particular, assure that consumer choice  
14 can be easily accommodated. First, the Commission's rules require that operating  
15 systems be nondiscriminatory in comparison to the use of these systems by the  
16 incumbent LEC itself. As the FCC explained in its recent Order:

17  
18 We thus conclude that an incumbent LEC must provide  
19 nondiscriminatory access to their operations support systems  
20 functions for pre-ordering, ordering, provisioning, maintenance and  
21 repair, and billing available to the LEC itself.

22  
23 FCC Order, ¶ 523.

24  
25 Second, the rules include the requirement that, wherever the change in the customer's

1 local service provider is accomplished through a software event, (i.e., resale  
2 arrangements or configurations using unbundled local switching), the change in a  
3 customers' local service provider must occur in an interval no longer than the interval  
4 in which an incumbent LEC transfers end-users between interexchange carriers. 47  
5 C.F.R. § 51.319(c)(1)(ii).

6

7 These provisions of the FCC rules implement the environment that I described in my  
8 direct testimony that will be necessary for consumers to broadly, and quickly, benefit  
9 from local competition.

10

11 **Q. HOW DO THE FCC RULES TREAT THE PRICING APPLICABLE TO**  
12 **THE TERMINATION OF LOCAL TRAFFIC?**

13

14 **A.** The FCC requires that transport and termination charges be cost-based.  
15 Commissions may, however, implement bill-and-keep compensation if neither party  
16 can demonstrate that traffic will be out-of-balance or that costs will be different.  
17 Therefore, the rules permit the Commission to adopt the recommendation in my prior  
18 direct testimony that bill-and-keep compensation be used until a cost-based charge is  
19 established. Even then, however, the Commission may retain bill-and-keep for the  
20 transport and termination of local traffic so long as costs and traffic flows are roughly  
21 equivalent.

22

23 **Q. DO THE FCC'S RULES REQUIRE BELLSOUTH TO PROVISION**  
24 **COMBINATIONS OF NETWORK ELEMENTS, INCLUDING THE**  
25 **"PLATFORM" CONFIGURATION DESCRIBED IN YOUR DIRECT**

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**TESTIMONY?**

A. Yes. The rules clearly recognize the rights of new entrants to order combinations of network elements, including combinations of elements as they are presently configured in the LEC network. Specifically, the FCC rules require that an incumbent LEC:

(a) shall provide network elements in a manner that allows a requesting carrier to combine such elements,

(b) shall not separate requested network elements that the LEC currently combines,

(c) shall perform the functions to combine unbundled network elements in any manner, even if those elements are not ordinarily combined in its network, if the combination is technically feasible and will not impair other carriers from obtaining access or interconnecting.

47 C.F.R. § 51.315.

These rules enable an entrant to combine local loops, local switching and transport and termination to form a "virtual" exchange platform to offer local exchange (to end users) and exchange access (to other carriers) service. This flexibility is essential if consumers are to rapidly benefit from the introduction of local competition.

1           **The Interim Surcharge is Unnecessary and Would Raise Consumer Prices**

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**Q.    ARE THERE ELEMENTS OF THE FCC'S ORDER WITH WHICH YOU DISAGREE?**

**A.**    Yes. The FCC has implemented a temporary interstate surcharge on the price of unbundled local switching that substantially increases the cost of this network elements. 47 C.F.R. § 51.515. By increasing the cost to carriers that would otherwise use the unbundled local switching element to provide service, the FCC's interim surcharge will decrease consumer choices or result in higher consumer prices.

**Q.    IS THE UNBUNDLED LOCAL SWITCHING ELEMENT IMPORTANT TO LOCAL COMPETITION?**

**A.**    Yes. As I explained in my prior direct testimony, the local switching element is central to widespread local competition. By obtaining local switching from the incumbent, entrants should be able to quickly enter a market, providing local exchange and exchange access services to customers broadly throughout the territory. Unbundled local switching *does not* require a physical change in the loop serving the customer -- the customer can continue to be served from the same switch, even though the carrier providing the service has changed. Furthermore, unbundled local switching provides entrants the ability to determine what vertical features are included in their basic local offering, developing packages identical to, or different from, the incumbent.

1           The bottom line is this: unbundled local switching is the heart of ubiquitous local  
2           competition. If the cost to entrants of this element is artificially increased, then the  
3           entrant's ability to compete with the incumbent is compromised. The result is either  
4           fewer choices for consumers, higher prices, or both.

5

6   **Q.    WHAT IS THE NATURE OF THE FCC'S INTERIM SURCHARGE?**

7

8   **A.**    The FCC adopted a surcharge system (47 C.F.R. § 51.515(b)) which increases the  
9           price of the local switching element by a rate equal to the sum of two interstate access  
10          rate elements: the carrier common line charge and 75% of the residual  
11          interconnection charges. This surcharge is applied to any interstate minute of use that  
12          is switched through the unbundled local switching element. This interim surcharge  
13          has the effect of significantly increasing the price of unbundled local switching.

14

15          The FCC's interim surcharge will expire on the earliest of three dates:

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17                   1.       June 30, 1997,

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19                   2.       the later of the effective date of a final Commission decision in CC  
20          Docket No. 96-45, Federal State Joint Board on Universal Service, or a final decision  
21          in a proceeding to consider access charge reform, or

22

23                   3.       the date that BellSouth is authorized to provide interLATA service  
24          pursuant to Section 271 of the Act.

25

1 In addition, the FCC has permitted states the *option of implementing a similar interim*  
2 *surcharge, subject to the requirement that any state surcharge expire before June 30,*  
3 *1997, or the date upon which BellSouth is authorized to provide interLATA service,*  
4 *whichever is earlier.*

5  
6 **Q. SHOULD THIS COMMISSION ADOPT AN INTERIM SURCHARGE**  
7 **SYSTEM?**

8  
9 A. No. The principal effect of the FCC's interim plan will be to delay carriers from  
10 providing service using unbundled local switching and, by doing so, delay the benefits  
11 of the ubiquitous competition that this network element could make possible.

12  
13 As I indicated earlier, the unbundled local switching element is the element that  
14 provides entrants the vehicle to offer service widely in the market. Furthermore, only  
15 through the shared use and software control of the unbundled local switching element  
16 can consumer choice can be implemented quickly, matching the ease and familiarity  
17 of the process used to change long distance carriers.

18  
19 By increasing the cost of the unbundled switching element -- however temporarily --  
20 these benefits are delayed and/or the price to consumers is increased.

21  
22 **Q. HAVE YOU QUANTIFIED THE IMPACT OF THE FCC'S INTERIM**  
23 **SURCHARGE SYSTEM?**

24  
25 A. Yes. Using data provided in 1996 BellSouth's interstate price cap filing, I estimate

1           that the cost increase caused by the FCC's interim plan is approximately \$3.82 per  
2           subscriber line served by an unbundled switch. Thus, the interim surcharge would  
3           raise the *cost* to other carriers to offer local exchange service -- and, ultimately, the  
4           *price* for local exchange service paid by consumers -- by almost \$4.00 per line. An  
5           increase in cost of this magnitude is significant.

6  
7           The distorting influence of the surcharge is even more dramatic when compared to the  
8           estimated cost of unbundled local switching. The FCC has concluded that default  
9           value for unbundled local switching is in the range of 0.2 cents to \$0.4 cents per  
10          minute, with the available evidence supporting a value at the lower end of the range.  
11          The surcharge, when expressed per minute of use is 1.56 cents -- or nearly 400%  
12          higher than the underlying cost!

13  
14          New entrants require unbundled local switching to provide competitive alternatives to  
15          BellSouth's local exchange service in those areas, and to those customers, where  
16          alternative networks are not yet justified or in existence. If the Commission  
17          arbitrarily increases the effective cost to new entrants beyond the economic cost of the  
18          elements they use, the effect will be felt by consumers. The temporary surcharge  
19          adopted by the FCC will seriously distort carrier choices and pricing; any state-  
20          adopted plan will curtail these choices further. The Commission should not adopt,  
21          even for an interim period, a surcharge on unbundled local switching.

22

23

#### SUMMARY

24

25    **Q.    PLEASE SUMMARIZE YOUR SUPPLEMENTAL TESTIMONY.**

1

2 A. The FCC rules pass to this Commission the critical decisions leading to local  
3 competition and the prices and choices that Florida consumers will experience in the  
4 local exchange market. Overall, the rules adopted by the Commission are consistent  
5 with my earlier testimony and I continue to endorse its recommendations and policy  
6 rationale.

7

8 The FCC's rules, while generally committed to cost-based pricing, do provide for an  
9 interim surcharge that I believe is ill-advised. Artificially increasing the cost to an  
10 entrant for *any* unbundled network element -- much less an element as critical to local  
11 competition as unbundled local switching -- will harm competition and, more  
12 importantly, consumers.

13

14 The Commission should not adopt, for even the interim period authorized by the FCC,  
15 a surcharge system. The best way to assure that consumers have low local exchange  
16 prices is to assure competitors that they have cost-based access to the network  
17 elements they will need to offer local exchange service. Cost-based network prices  
18 will provide the best possible environment for the greatest amount of competition and  
19 price protection.

20

21 Q. DOES THIS CONCLUDE YOUR SUPPLEMENTAL DIRECT  
22 TESTIMONY?

23

24 A. Yes.