BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Expanded Interconnection Phase II and Local Transport Restructure	Docket No. 921074-TP Docket No. 930955-TL Docket No. 940014-TL Docket No. 940020-TL Docket No. 931196-TL Docket No. 940190-TL
	Filed: May 23, 1994

DIRECT TESTIMONY

of

R. KIRK LEE

On Behalf of

GTE FLORIDA INCORPORATED

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is R. Kirk Lee. My business address is 600 Hidden Ridge, Irving, Texas 75038.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed as Section Manager-Intrastate Access Pricing for GTE Telephone Operations, representing GTE Florida, Inc. (GTEFL or Company) in this proceeding. I am responsible for the development of access pricing plans and rates for intrastate purposes in all states in which GTE Telephone Operations operates in its East Area, including Florida. My responsibilities also include testifying on access pricing and other related matters before regulatory bodies as appropriate.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND WORK EXPERIENCE.

A. I received a Bachelor of Arts degree in Business Administration (Accounting Concentration) from the University of Washington in 1978. In 1988, I received a Masters of Business Administration degree from Seattle University.

My work experience began with GTE Northwest

Incorporated in Everett, Washington in December 1978 as a Staff Accountant. At GTE Northwest I held various positions of increasing responsibility in payroll, cost accounting, general accounting, internal auditing and budget. In June of 1989, I was promoted to Staff Manager-Regulated Earnings Analysis in the Regulatory and Governmental Affairs department at GTE Telephone Operations Headquarters in Texas. My responsibilities in this position included the analysis and reporting of interstate access rates of return, providing support for the annual Interstate Access Tariff filing, and analyzing GTE liabilities and supporting Company negotiations resulting from FCC Docket 84-800 earnings levels and FCC Price Caps sharing requirements. In June 1992, I was promoted to my current position in the Access Pricing and Tariffs Department.

Q. HAVE YOU TESTIFIED PREVIOUSLY BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION (FPSC)?

A. No. However, I have testified previously before regulatory commissions in Indiana and Wisconsin.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my testimony is to address the issues raised by the Commission in its Order No. PSC-94-0277-PCO-TL of March 10, 1994 in Phase II of this docket, which pertains to the local transport restructure and additional pricing flexibility. Specifically, I will address issue numbers 1-2 and 18-24. Company witness Edward Beauvais will address the public policy and expanded interconnection matters identified as issue numbers 3-18.

Q. HOW IS SWITCHED ACCESS PROVISIONED AND PRICED TODAY?

A. Switched access is provisioned today under a feature group (FG) arrangement. Interexchange carriers (IXCs) who utilize the networks of the local exchange carriers (LECs) subscribe to either a premium (FGC or FGD) or non-premium (FGA or FGB) connection arrangement. There are several rate elements which apply to each feature group service, including End Office Switching (EOS), Local Transport, Information Surcharge, and Carrier Common Line Charge (CCLC). These rate elements are priced today under the equal charge rule. That is, each unit is priced the same as the next unit for a given rate element. For example, EOS is purchased on a minute of use (MOU) basis, with each additional minute priced the same as the last.

The equal charge rule is just one part of an antiquated set of fully distributed costing rules (FCC Parts 36 and 69) which have been utilized to price access rates in the past. These rules have not kept up with the fast-paced changes in the telecommunications industry and which are subjecting LECs to an increasing amount of competitive pressure today. Access reform, such as the FCC's local transport restructure (LTR), has helped address some of the types of structural flexibility and pricing flexibility that are needed for access services in today's competitive environment. The whole realm of access charges beyond LTR needs to be further examined by the FPSC.

Q. HOW IS LOCAL TRANSPORT STRUCTURED AND PRICED TODAY?

A. For GTEFL, the current intrastate local transport rate element is applied on a per minute of use per termination basis. Because GTEFL bills its IXC customers under a single bill/single tariff arrangement, two transport terminations per MOU apply since the Company bills the entire length of haul between offices. This is consistent with the Company's interstate rate structure and billing methodology for the transport termination rate element. The actual rate applied is, again, based on the equal charge rule.

Q. SHOULD THE COMMISSION MODIFY ITS PRICING AND RATE STRUCTURE REGARDING SWITCHED TRANSPORT SERVICE WITH THE IMPLEMENTATION OF SWITCHED EXPANDED INTERCONNECTION?

A. Yes. It is imperative that the Commission allow the restructuring of the LECs' local transport services in accordance with the FCC's LTR methodology if it also approves expanded interconnection and colocation for switched access. To do otherwise would leave the LECs on an unlevel playing field in which they could not compete fairly with entities like alternative access vendors (AAVs). For example, these AAVs would be able to interconnect with the LECs networks and offer lower priced dedicated transport to the IXCs. A LEC must be able to offer similar flat-rated transport options to its customers to be able to have a reasonable chance of retaining traffic on its network.

Q. SHOULD THE COMMISSION MODIFY ITS PRICING AND RATE STRUCTURE REGARDING SWITCHED TRANSPORT SERVICE EVEN IF SWITCHED EXPANDED INTERCONNECTION SERVICE (EIS) IS NOT IMPLEMENTED?

A. Yes. With or without switched expanded interconnection, local transport is subject to substantial competitive pressure. The FCC has recognized this fact and, as a result, approved LTR to go into affect ahead of switched EIS. The FCC, in its October 16, 1992 order (paragraph 2) in CC Docket No. 91-213 regarding the Local Transport Restructure stated that "Even without expanded interconnection, LECs are already facing access competition, for example, as reflected in the proliferation of "closet POP" arrangements. A POP is an IXC's point of presence. With "closet POPs," access customers purchase flat-rate special access from CAPs or LECs and avoid paying a part of the LECs' per-minute transport rate. A rate structure change is necessary to promote more efficient use of LEC networks, and access competition."

AAVs operating in the Company's territories today are currently providing alternative services which compete with GTEFL's switched access services. Intermedia Communications Inc. of Florida (ICI), an alternative local transport provider, has a network in the Company's Tampa market which has been in service since November 1988. Other AAVs, including MFS Telecom, FiberNet, Jones Lightwave, and Florida Digital Media Partners either have a presence in or have announced expansion plans for the near future for the Tampa/St. Petersburg area. Other competitors such as cable television companies, PCN providers, STS providers, cellular companies, and VSAT providers are also competing for GTEFL's largest customers in the Tampa/St. Petersburg area. All are providing alternative sources of access which can bypass all or part of the Company's switched access network. Implementation of expanded interconnection for switched access will only serve to accelerate this competitive erosion of the Company's revenues. Company witness Beauvais further describes how this erosion will occur with switched EIS.

The FCC, in its October 16, 1992 order in CC Docket

91-213 regarding Local Transport Restructure, found that "the equal charge rate structure cannot remain in place if customers are to receive the benefits of switched transport competition." The FCC also found that "the current rate structure, under the equal charge rule, has promoted significant inefficient use of the LEC networks by IXCs and other access customers. The uneconomic pricing signals created by the equal charge rule have caused wasteful use of LEC facilities and higher rates for ratepayers. For this reason, it is critical that we [the FCC] adopt a new rate structure that will better match LEC transport rates and costs."

Elimination of the equal charge rule was found to be in the public interest and was accomplished at the federal level prior to implementation of switched interconnection. The FPSC should allow the ratepayers to benefit equally by allowing LTR to go into effect immediately.

Q. IF THE COMMISSION CHANGES ITS POLICY ON THE PRICING AND RATE STRUCTURE OF SWITCHED TRANSPORT SERVICE, WHAT SHOULD THE NEW POLICY BE BASED ON?

A. GTEFL believes the Commission's new switched transport policy should mirror each LEC's interstate tariff structure, terms and conditions. Mirroring can help reduce the potential for arbitrage, ease the burden of administration for tariffs and billing systems, reduce customer confusion, and increase the customer's ability to aggregate traffic and purchase the most cost efficient transport options.

Rates should not necessarily be mirrored but should be determined by market factors such as market demand, competitive conditions, and the number of available substitutes for transport services in a given market. Rates should also be supported by Long Run Incremental Cost (LRIC) as a price floor to prevent anti-competitive pricing. Market conditions should determine the actual prices and the level of contribution provided by each access service option.

Q. PLEASE EXPLAIN HOW GTEFL ESTABLISHED ITS INTRASTATE PRICES FOR ENTRANCE FACILITIES (EF), DIRECT-TRUNKED (DT), TANDEM SWITCHED TRANSPORT (TST) AND RESIDUAL INTERCONNECTION CHARGE (RIC) RATE ELEMENTS IN

FLORIDA.

A. GTE Florida's prices for its local transport rate elements for EF, DT, and TST mirror the Company's interstate LTR tariff. The interstate rates were, by FCC order, based on September 1, 1992 interstate special access rates, then adjusted if necessary for an FCC established benchmark DS3-to-DS1 crossover ratio of at least 9.6-to-1, and further adjusted for the 1993 price cap filing. GTEFL's intrastate RIC element was residually priced to maintain revenue neutrality to the Company's existing intrastate switched transport revenue streams.

Q. IF THE COMPANY BELIEVES THAT MARKET-BASED PRICING IS APPROPRIATE FOR SWITCHED TRANSPORT, WHY DID IT FILE ITS INTRASTATE LTR RATES TO MIRROR ITS INTERSTATE LTR RATES?

A. The FCC set its initial LTR rates based on equivalent special access rates in existence at a particular point in time (September 1, 1992). The Company believes these rates to be a close approximation to market based rates since special access has been a more competitive service and its rates are closer to their relevant economic costs.

The FCC thoroughly investigated the issues associated with LTR and determined that rates which met the minimum 9.6-to-1 crossover ratio would be reasonable and lawful in the absence of proof otherwise. Because GTEFL's rates met the FCC's requirements, the Company believes these rates are also appropriate for the "initial" implementation of LTR for intrastate purposes. The best short-term approach to implementing LTR is to mirror the interstate rates and structure, with the exception of the RIC, which was priced to maintain revenue neutrality with intrastate specific transport revenues.

However, the Company also believes that a number of enhancements to the LTR structure and pricing guidelines should be considered by the FPSC in these proceedings. These improvements to LTR serve to further promote economic efficiency, provide additional choices to customers in a competitive market, and eliminate the potential for arbitrage between switched and special access services.

Q. WHAT ENHANCEMENTS DOES GTEFL PROPOSE BE MADE TO LTR?

A. There are four primary enhancements. These enhancements are discussed further below:

1. Pricing Flexibility: Even before the implementation of expanded interconnection for switched access, LECs will need increased pricing flexibility in order to have a level playing field in a competitive market place. Volume and term discounts are one form of pricing flexibility that will be needed. GTEFL's proposed Switched Access Discount Plan (SADP) is an example of this type of pricing.

Since the current basis for switched dedicated transport rates and rate structure is the special access rates and rate structure, GTEFL believes it is also appropriate to include term and volume discounts for switched dedicated facilities (EF and DT rate elements) that are similar to those provided for special access customers today. An example is the Optional Payment Plans found in GTEFL's special access tariff today.

Zone pricing and other forms of pricing

flexibility such as contract service arrangements (CSAs) should also be allowed for switched access services to enable the Company to address competitive pressures. I will discuss GTEFL's specific proposals for pricing flexibility later in this testimony.

2. Matching Switched and Special Access Rates: GTEFL believes that the rates and charges for entrance facilities and direct trunked transport should be the same as those charges currently applicable for special access lines (SALs) and special transport, respectively. Switched entrance facilities and special access lines (SALs) are equivalent service offerings and therefore should reflect the same rates and charges. The same is true of switched direct trunked transport and special transport services. GTEFL therefore proposes that these two services be rated the same.

The FCC established September 1, 1992 special access rates as the basis for determining current entrance facility and direct trunked transport rates. Since that time, special access rates have changed significantly. The rates for switched and special transport need to be equivalent to help lessen the potential for uneconomic migration to special access services from switched access, since both switched and special traffic can be carried over the same facilities. Therefore, LTR rates should be updated to reflect the most current special access rates in effect.

3. Crossover Ratio Flexibility: GTEFL would propose that the crossover ratios between DS1 and DS3 switched services be flexible and that the market be allowed to drive the appropriate pricing of such services. Currently, the crossover ratio that exists between approved rates for special DS1s and special DS3s is appropriate and therefore should be the same for switched dedicated services. The FCC has chosen to require a minimum 9.6 to 1 crossover ratio between DS1 and DS3 services. This means that the price for one DS3 must be at least equal to or greater than the price total of 9.6 DS1 circuits.

Automatic application of the FCC's 9.6 to 1 or any other fixed crossover requirement, however, creates rate differences between switched and special services that are not justified. Again, different rates for substitutable services create tariff shopping or arbitrage opportunities. Switched dedicated transport and special access rates should be the same, since these are equivalent services. Fixed crossover points, such as those ordered by the FCC, or higher ones such as those advocated by the Interexchange Access Coalition (IAC), will only serve to widen the gap between these rates and ignore the real cost and market differences inherent in the development of DS1/DS3 prices.

4. Reconfigured vs. Current Network: GTEFL proposes that LTR units and rates be developed using a reconfigured optimal network. This approach assumes that customers will quickly optimize their transport services into the most cost-efficient and operations-efficient design up front. Under normal circumstances, once LTR is implemented, it is GTE's

assumption that this optimization process might take 6-12 months. However, the non-recurring charge (NRC) waiver currently in effect further encourages IXC customers to optimize their networks sooner rather than later. The Company began receiving LTR-related orders for transport services well in advance of the actual FCC effective date, which further supports this position.

To develop reconfigured network demand, the Company utilizes a model which looks at traffic volumes by customer and route, then determines the best mix of common transport and direct trunked transport per customer based on the least cost choice. Direct transport would be further reconfigured into an optimal voice grade, DS1, and DS3 mix based on combined switched and special access transport facility use.

Use of these reconfigured units in pricing helps to ensure that the initially proposed RIC rate maintains revenue neutrality for transport services as a whole. If the RIC were to be developed using a historical network approach, as soon as an IXC places an order to reconfigure a part of its network into a lower cost alternative, the Company is no longer revenue-neutral and the lost revenues will never be recouped. As a result, GTEFL has filed its LTR tariff rates using reconfigured demand. The Company's modeling of demand does not, however, take into account potential reconfiguration associated with hubbing and tandem direct transport options available with LTR. This has the effect of making the Company's reconfigured demand estimates more conservative.

Q. SHOULD THE LECs' PROPOSED LOCAL TRANSPORT RESTRUCTURE TARIFFS BE APPROVED? IF NOT, WHAT CHANGES SHOULD BE MADE TO THE TARIFFS?

A. GTEFL's LTR tariff should be approved as is and allowed to go into effect. The Company's rates have previously been found to be reasonable and lawful by the FCC after extensive review of the issues surrounding LTR. As such, they should be allowed to go into effect so that the Company's local ratepayers and access customers can begin to benefit immediately from elimination of the equal charge rule and an increasingly competitive market. The Commission should also allow the Company's proposed enhancements which were not included in the initial LTR filing to be put into effect.

Q. SHOULD THE MODIFIED ACCESS BASED COMPENSATION (MABC) AGREEMENT BE MODIFIED TO INCORPORATE A REVISED TRANSPORT STRUCTURE FOR INTRALATA TOLL TRAFFIC BETWEEN LECs?

A. GTEFL is not a party to the MABC agreement and therefore takes no position on this issue in this proceeding.

Q. HOW SHOULD THE COMMISSION'S IMPUTATION GUIDELINES BE MODIFIED TO REFLECT A REVISED TRANSPORT STRUCTURE, IF IT IS ADOPTED?

A. The Commission's current imputation guidelines should be left as is in this proceeding. The Commission's established policy for imputation can be utilized without modification by merely substituting the new transport rate elements for the old transport rate elements where appropriate. Since the RIC element constitutes the majority of the revenues now recovered for transport under LTR, GTEFL recommends that the RIC be used as a surrogate for the previously used transport rate elements in the imputation calculations. This method is easy to administer and could serve as an interim approach to imputation under LTR until the Commission can comprehensively address imputation in a more appropriate forum.

Further, the issue of imputation is associated with the setting of toll rates. This proceeding has been established to specifically examine the appropriateness of rate levels for local transport access rates. Introduction of the imputation issue into this docket will not help determine whether these access rates are appropriate or not. Instead, due to the contentious nature of the issues inherent with imputation, it will only result in unnecessary delays in getting these LTR tariffs approved and in attaining associated customer and ratepayer benefits.

Imputation issues are important and need to be addressed. However, the Company recommends that these issues be treated in a separate docket or in toll rate proceedings for individual LECs, so that customers and ratepayers may begin receiving the benefits associated with LTR immediately.

Q. SHOULD THE LECs BE GRANTED ADDITIONAL PRICING FLEXIBILITY? IF SO, WHAT SHOULD IT BE?

A. Yes, the LECs should be granted additional pricing flexibility for switched access services immediately due to an already highly competitive environment in Florida. Implementation of expanded interconnection for switched access will tend to further accelerate competition. Additional pricing flexibility is necessary to allow LECs rates to become more competitive with the rates and service offerings of the AAVs. In addition to LTR, GTEFL has proposed three forms of pricing flexibility in the illustrative tariffs it filed on May 16, 1994 in this proceeding. These include a Switched Access Discount Plan (SADP), a Zone Pricing Plan for switched access, and CSA authority for switched access services. Each of these three plans is discussed in more detail below. Access reform, such as the LTR and Zone Pricing implemented by the FCC, is critical to the ability of the LECs to be able to effectively compete in today's environment. The Commission should grant GTEFL the authority to implement its flexible pricing proposals in order to be able to address competitive pressures in its markets.

Q. PLEASE DESCRIBE THE COMPANY'S PROPOSED SADP IN MORE DETAIL.

A. The Company is proposing two separate switched access discount plans within its SADP: a Term Plan and a Growth Plan. The plans may be subscribed to individually or in conjunction with each other. The Term Plan would provide savings to customers who commit to various time periods at specified usage and/or monthly recurring charge (MRC) levels; the longer the time period committed to at a specified usage or MRC level, the greater the discount.

The Growth Plan would provide savings to customers who commit to various percentages of usage/MRC growth over a one year time period; the greater the percentage of growth, the greater the discount. The plans are available on a statewide basis or by specific market areas within the state. The discounts would be overlayed on top of any zone prices the customer is already paying. Terms and conditions associated with both plans are detailed in the illustrative tariff filed by the Company on May 16, 1994 in this proceeding.

Q. PLEASE DESCRIBE THE ZONE PRICING PLAN FOR SWITCHED ACCESS PROPOSED BY THE COMPANY.

A. The Company's proposed Zone Pricing Plan was developed using similar methodology to the plan proposed to the FCC. First, a count of all equivalent switched and special access DS1 high capacity circuits was compiled for each end office. The offices were then sorted based on the equivalent DS1 facilities in each office. Finally, break points were established so that end offices and their associated revenues were spread to three zones. Zone 1 contains offices with more than 112 equivalent DS1s, Zone 2 contains offices with greater than 50 but less than or equal to 112 DS1s, and Zone 3 contains all offices with less than or equal to 50 DS1s. In addition, all Zone 2 offices that were contiguous to a Zone 1 office were also assigned as Zone 1, consistent with the FCC methodology.

This proposal is consistent with the plan filed with the FCC, except for the break points for each zone. However, the Company's FCC zone plan is being reworked and will be refiled with the FCC later this year to be identical to the intrastate filing proposed here. The Company proposes pricing flexibility within each zone based on market conditions rather than the strict limits placed on zone pricing bands at the federal level.

Q. WHAT CHANGES IS THE COMPANY PROPOSING TO THE CSA PROCESS FOR SWITCHED ACCESS?

A. In Section 12.3 ("Contract Service Arrangements") of its intrastate access tariff, GTEFL proposes additional language to make CSAs applicable for switched access services in addition to the provisions already in place for special access services. This will enable the Company to use CSAs in lieu of existing tariff offerings provided there is reasonable potential for uneconomic bypass of the Company's switched access services. As I've already indicated, significant competitive pressure on the Company's access revenues exist today. Switched EIS will accelerate these pressures even more. CSAs for switched access will help the Company to address this pressure, thereby increasing its ability to retain the revenues and contribution provided by switched access. Retention of this contribution will help lessen the upward pressure on local basic service rates.

Q. SHOULD THESE DOCKETS BE CLOSED?

A. Yes, with the adoption of the Company's recommendations regarding the issues addressed in this proceeding, these dockets should be closed.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.