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RECORDS AND REPORTING

June 9, 2000

Blanca S. Bayo
Director, Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: UNE Docket No. 990649-TP

Dear Ms. Bayo:

Enclosed for filing are the original and fifteen copies of rebuttal testimony of Carol Bentley and David Nilson.

By copy of this letter, these documents have been furnished to the parties to this proceeding as shown on the attached service list.

Sincerely,

Mark Buechele

Enclosures

cc: Parties of Record

- APP _____
- CAF _____
- ~~CMP _____~~
- COM 5/2/00
- CTR _____
- ECR _____
- LEG 2
- OPC _____
- PAI _____
- RGO _____
- SEC 1
- SER _____
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07100 JUN-98

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CERTIFICATE OF SERVICE

Docket No. 990649-TP

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by U.S. Mail to the following parties of record this 9th day of June, 2000.

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AT&T Communications of the
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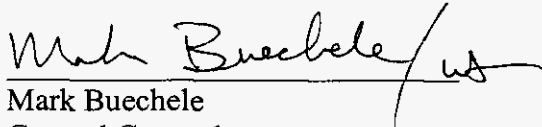
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A handwritten signature in cursive script that reads "Mark Buechele" followed by a flourish that looks like "us".

Mark Buechele
General Counsel
Supra Telecom
2620 SW 27th Avenue
Miami, Florida 33133
(305) 531-5286

1 SUPRA TELECOMMUNICATIONS & INFORMATION SYSTEMS, INC.

2 REBUTTAL TESTIMONY OF CAROL BENTLEY

3 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

4 DOCKET NO. 990649-TP

5 JUNE 9, 2000

6

7

8 Q. PLEASE STATE YOUR NAME AND ADDRESS

9

10 A. My name is Carol Bentley. My address is 2620 SW 27th Avenue, Miami, Florida
11 33133.

12

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

14

15 A. I am the Chief Financial Officer of Supra Telecommunications and Information
16 Systems, Inc. ("Supra").

17

18 Q. PLEASE DESCRIBE YOUR BACKGROUND AND WORK EXPERIENCE.

19

20 A. I attended University of Michigan and Eastern Michigan University, graduating
21 with a Bachelors degree with a double major in Mathematics and Finance and a
22 minor in Computer Science. I have also completed substantial coursework

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1 requirements toward a Masters in Business Administration. I have worked in the
2 telecommunications industry for over twenty years performing various financial,
3 treasury, business management and IT functions. Several of the companies I have
4 worked for include General Datacomm, Inc., Racal Datacom Industries, Inc. and
5 Supra Telecommunications and Information Systems, Inc.

6

7 Q. HAVE YOU EVER PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?

8

9 A. Not formally, but I have previously provided a presentation in a workshop before
10 this Commission in the current Operational Support Systems (OSS) Docket No.
11 981834-TP.

12

13

14 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

15

16 A. The purpose of my testimony is to address the issues identified in this proceeding.
17 I have reviewed the testimonies submitted by the ILECs (i.e. BellSouth, GTE and
18 Sprint) concerning Depreciation, Cost of Capital and Tax Rates. As a preliminary
19 matter, it is my opinion that the ILECs have both the incentive and means of
20 present cost models that inherently inflate and even "double count" actual costs.
21 Because the actual cost information is truly only available to the ILECs, it is
22 difficult for ALECs, particularly small ALECs to realistically challenge the cost

1 estimates generated. Therefore the purpose of my testimony is to rebut the
2 testimonies of the ILECs in reference to depreciation, cost of capital and tax rates;
3 and in the process, urge the Commission to stick closely to FCC guidelines on
4 these issues and heavily scrutinize both the assumptions and models presented by
5 the ILECs.

6

7

8 Q. WHAT ISSUES WILL YOU ADDRESS?

9

10 A. I will rebut the direct testimony of various BellSouth, Sprint and GTE witnesses
11 on issues 7(b) (depreciation), 7(c) (cost of capital) and 7(d) (tax rates).

12

13

14 Q. WHAT ARE THE APPROPRIATE ASSUMPTIONS AND INPUTS FOR
15 DEPRECIATION IN THE FORWARD-LOOKING RECURRING UNE COST
16 STUDIES?

17

18 A. In its First Report and Order (FCC 96-325), the Federal Communications
19 Commission (FCC) established various guidelines for forward-looking TELRIC
20 costs modeling. As result of this Order, various pricing rules were established,
21 which have subsequently been upheld by the United States Supreme Court in
22 January 1999 in the case of AT&T Corp., et al v. Iowa Utilities Board et al. These

1 pricing rules found in 47 C.F.R. Sections 51.503 - 51.513 provide guidance
2 regarding the assumptions and inputs to forward looking cost models. 47 C.F.R.
3 Section 51.505(b)(1) states that the TELRIC cost model assumes a network design
4 based upon the most efficient technology currently available. 47 C.F.R. Section
5 51.505(b)(3) states that depreciation rates used in calculating forward-looking
6 economic costs of elements shall be economic depreciation rates. The FCC's First
7 Report and Order states at footnote 1711, that "properly calculated economic
8 depreciation is a periodic reduction in the book value of an asset that makes the
9 book value to its economic or market value." Accordingly, it is clear that the FCC
10 has mandated that depreciation rates not be artificial, but must actually be based
11 upon the true service life of the asset. Any shorter periods of depreciate would
12 yield the ILECs an unwarranted profit on this cost element. If an ILEC continues
13 to use a piece of equipment after its depreciated life span, then ALECs will
14 continue paying for the cost of an unbundled network element which no longer
15 costs the ILEC anything. Thus this Commission must reject any assumptions
16 presented by ILECs that yield depreciation lives which are shorter than actual
17 equipment service lives.

18
19 I note that the ILECs, and in particular GTE, argue in favor of utilizing non-
20 standard accounting methods and the calculation of depreciation using economic
21 asset lives that are less than the true equipment service life. This Commission
22 should not accept any none standard accounting arguments, but rather should rely

1 solely upon standard accounting practices as embodied by the Generally Accepted
2 Accounting Principals (GAAP).

3
4 With respect to the calculation of depreciation, GTE argues that its depreciation
5 should be calculated at something less than the true useful life of the relevant asset.

6 GTE's rationale for this argument is that competition will result in a percentage of
7 its assets being underutilized or not used at all by the time the useful life expires.

8 GTE argues that as competition increases, facilities built by competitors will leave
9 many GTE assets unutilized. However, this assumption is flawed because in

10 reality competition has caused an explosion in new telephone numbers rather than

11 merely a shift in numbers from ILECs to ALECs (a fact made obvious by the
12 shortage in telephone numbers and the constant creation of new area codes).

13 Moreover, when talking about competition in the UNE environment, although a

14 customer may switch to an ALEC, the network elements used by the ALEC will
15 more likely than not still be owned by the ILEC. Thus if an ALEC takes away a

16 GTE customer, but provisions that service using UNE combinations, the customer

17 may belong to the ALEC, but the UNE elements and assets used to provision that

18 service are still owned by GTE. Thus it makes no sense to assume that customers

19 lost through competition will result in unused equipment.

20
21 GTE's depreciation argument also is flawed because it seeks to reward GTE for

22 being inefficient. The TELRIC model is a forward-looking cost model, thus any

1 future expenses incurred in providing UNEs will be incurred for the acquisition of
2 new equipment that will be purchased based upon an ILEC's forecast of future
3 needs and future demands. Therefore, an ILEC such as GTE will not incur
4 additional equipment expense if it properly plans for future demand. ALECs
5 should not have to pay for an ILEC's inefficient forecast of future demand.

6

7 The ILECs also argue that in the past, the FCC set artificially long depreciation
8 lives so that the cost of equipment would be expensed out over a longer period of
9 time; thereby allowing for lower long distance rates. However, the ILECs do not
10 argue that the actual life of equipment in the past was ever less than the FCC
11 standard. Nor do the ILECs seriously argue that equipment life will likely be any
12 shorter in the future. Indeed, the technology is moving towards
13 telecommunications equipment utilizing computer-based hardware that uses
14 software to provision features. Therefore upgrades are simply software changes
15 rather than equipment changes. Accordingly, it is doubtful that any ILEC assets
16 deployed in the future will have any material change in their useful life as
17 compared to assets already deployed.

18

19 BellSouth also argues that their networks in the process of being converted from
20 copper to fiber plant and from analog to digital networks and thus the future will
21 bring large deployments of assets and retirement of equipment. However,
22 BellSouth does not argue that such conversions will take place before the prior

1 FCC determined useful asset lives. Rather BellSouth concedes that such
2 conversions will take place only after the assets employing older technologies have
3 been fully depreciated. Thus BellSouth implicitly concedes that any alleged
4 competitive pressures in the market will not force them to retire equipment before
5 such assets are fully depreciated beyond their economic useful life.
6 Notwithstanding the above, any attempt to recover from ALECs the depreciation
7 of current assets that have not yet reach their useful life, simply to justify
8 deployment of new equipment, will be an improper attempt to recover past
9 embedded costs. Under the FCC's pricing rules, ALECs have no obligation to pay
10 the cost of an ILECs prior inefficiencies cause by monopolistic deployment
11 mentalities.

12
13 In its First Report and Order, the FCC stated in paragraph 702 that the federal
14 depreciation rates were a reasonable starting point and ILECs had the burden of
15 demonstrating with specificity that the business risks they face in providing
16 unbundled network elements and interconnection services, justify a different
17 depreciation rate. In my opinion, the ILECs have not credibly met this burden.
18 Therefore, the only assumptions and inputs which this Commission should
19 consider regarding depreciation are the actual useful life of the asset based upon
20 FCC standards and the ILECs' historical data regarding the prior actual service life
21 of the same, similar or functionally equivalent assets. Any other assumptions
22 would simply give the ILECs an improper and unjustified windfall that would

1 allow ILECs to continue charging ALECs for the cost of equipment that although
2 may still be in service, has been fully depreciated by the ILEC.

3
4
5 Q. WHAT ARE THE APPROPRIATE ASSUMPTIONS AND INPUTS FOR COST
6 OF CAPITAL IN THE FORWARD-LOOKING RECURRING UNE COST
7 STUDIES?

8
9 A. In its First Report and Order (FCC 96-325), the FCC stated in paragraphs 699 and
10 700, that under the TELRIC model, no additional profit above a reasonable profit
11 found in the cost of capital is statutorily authorized. The FCC stated that the
12 forward-looking cost of capital should be equal to a normal profit given the risk
13 factors involved. The FCC also stated in paragraph 702 as follows:

14 **“[W]e conclude that the currently authorized rate of return at**
15 **the federal or state level is a reasonable starting point for**
16 **TELRIC calculations, and incumbent LECs bear the burden of**
17 **demonstrating with specificity that the business risks that they**
18 **face in providing unbundled network elements and**
19 **interconnection services would justify a different risk-adjusted**
20 **cost of capital.”**

21 In that same paragraph, the FCC noted that given the then current (1996) state of
22 the economy, the federally authorized 11.25 percent rate of return was arguably
23 too high given the marketplace cost of debt and equity. The economy has not
24 changed much since 1996 as the United States continues through the strong growth

1 periods experienced in throughout much of the 1990s. Interest rates are currently
2 low and investment opportunities yielding high rates of return are difficult to find.
3 The ILECs are still monopoly utility providers in the eyes of investors and thus the
4 capital markets still view investments into these companies as being essentially
5 risk-free. Based upon the above, Supra Telecom believes that shareholder
6 investments into ILECs should not be allowed more than an eight to ten percent
7 (8%-10%) rate of return. Even these rates of return, based upon the current
8 economy, are attractive given the low risk involved.

9
10 GTE's very creative arguments that cost of capital should be calculated using the
11 same cost of capital available to ALECs is ludicrous. The high cost of capital to
12 new entrants into any industry is one of the biggest barriers to entry. The intent of
13 the Telecommunications Act of 1996 was to level the playing field and in some
14 regard, tip the scales in favor of new entrants in an effort to encourage competition
15 by new entrants. GTE's arguments fly in the face of this intent. Contrary to the
16 assertions made by GTE, the risks faced by small ALECs are enormously greater
17 than those faced by the ILECs. Accordingly, it is ludicrous to allow GTE (or any
18 other ILEC) returns on investment greater than ten percent (10%). The ILECs are
19 still substantial monopolies who will surely always own the majority of the
20 physical local exchange plant. This reality will not change anytime in the
21 foreseeable future regardless of how many ALECs enter the market. Therefore,

1 for all practical purposes, it will be many years before investors view ILECs as
2 being anything but utility monopolies.

3
4 As for cost of debt, Supra Telecom agrees that the true cost of capital should be a
5 weighed average of the cost of equity together with the cost of debt. The cost of
6 debt should be based upon actual cost of debt to the particular ILEC, while the cost
7 of capital should be set at no greater than ten percent (10%). The weighed average
8 should then be used to calculate the actual forward-looking cost of capital under
9 the TELRIC model.

10
11
12 Q. WHAT ARE THE APPROPRIATE ASSUMPTIONS AND INPUTS FOR TAX
13 RATES IN THE FORWARD-LOOKING RECURRING UNE COST STUDIES?

14
15 A. None. There are currently two general types of taxes; (a) taxes on revenues or
16 gross receipts; and (b) taxes on income. Considerations for income taxes have
17 already been factored into the cost of capital. With respect to taxes on revenues or
18 gross receipts, these taxes (such as the federal excise tax and local and state sales
19 taxes) are charged to the ultimate provider of telecommunications service. In the
20 UNE environment, the pieces of the network are in essence being leased to the
21 ALEC and thus the ILEC is not longer the service provider. Thus the ILEC will
22 generally incur no tax liability in the UNE environment; rather the ALEC will

1 incur this liability. Where there is no tax liability to the ILEC, there should be no
2 inputs into the TELRIC model. In this instance, none of the ILECs have made a
3 credible showing that they will incur any tax liability (other than on net income) in
4 the UNE environment. Therefore, no consideration for taxes should be given to
5 the TELRIC cost model in determining the cost of unbundled network elements or
6 interconnection services.

7

8

9 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

10

11 A. Yes.