

**LEWIS  
AND  
ROCA  
LLP  
LAWYERS**

Phoenix Office  
40 North Central Avenue  
Phoenix, Arizona 85004-4429  
Facsimile (602) 262-5747  
Telephone (602) 262-5311

Thomas H. Campbell  
(602) 262-5723

Tucson Office  
One South Church Avenue Suite 200  
Tucson, Arizona 85701-4620  
Facsimile (520) 622-3088  
Telephone (520) 622-2090

MCI ID  
697-6314

Our File Number  
20390-095



0000132250

November 8, 1996

**HAND DELIVERED**

Jerry L. Rudibaugh  
Chief Hearing Officer  
Arizona Corporation Commission  
1200 W. Washington Street  
Phoenix, Arizona 85007

Arizona Corporation Commission

**DOCKETED**

NOV 08 1996

DOCKETED BY

EA

Re: **MCImetro Access Transmission Services, Inc.  
1996 Consolidated Cost Docket with  
US West Telecommunications, Inc.  
Docket Nos. U-3175-96-448, et al.**

Dear Mr. Rudibaugh:

Pursuant to the August 30, 1996 Procedural Order, enclosed are the original and three (3) copies of the responsive testimony for the following MCImetro witnesses in the above consolidated arbitration.

1. Anthony J. DiTirro; and
2. Richard Cabe.

Very truly yours,

Thomas H. Campbell

THC:hjg  
Enclosures

ABB21E74

**COPY of the foregoing hand-  
delivered this 8th day of  
November, 1996, to:**

**Docket Control  
Arizona Corporation Commission  
1200 W. Washington Street  
Phoenix, Arizona 85007**

**Timothy Berg, Esq.  
Fennemore Craig, P.C.  
Two N. Central Avenue  
Suite 2200  
Phoenix, Arizona 85004**

**COPY of the foregoing hand delivered/  
mailed this 8th day of November,  
1996, to:**

**Gary L. Lane, Esq.  
US West Communications, Inc.  
5090 North 40th Street  
Suite 425  
Phoenix, Arizona 85018**

**Joan S. Burke, Esq.  
Osborn Maledon, F.A.  
2929 N. Central Avenue  
21st Floor  
Phoenix, Arizona 85067-6379**

**Daniel Waggoner  
Mary E. Steele  
2600 Century Square  
1501 Fourth Avenue  
Seattle, Washington 98101-1688**

Eric J. Brantman, Esq.  
Russell M. Blau, Esq.  
Douglas G. Bonner, Esq.  
Swidler & Berlin Chartered  
3600 K Street  
Suite 300  
Washington, D.C. 20007-5116

Bruce Meyerson, Esq.  
Stentoe & Johnson, L.L.P.  
40 N. Central Avenue  
24th Floor  
Phoenix, Arizona 85004-4453

Deborah S. Waldbaum, Esq.  
Western Region Office  
201 North Civic Drive  
Suite 210  
Walnut Creek, California 94596

Thomas L. Mumaw, Esq.  
Spall & Wilmer, L.L.P.  
One Arizona Center  
400 West Van Buren  
Phoenix, Arizona 85004-0001

Donald A. Low  
Sprint Communications Company, L.P.  
8140 Ward Parkway 5E  
Kansas City, Missouri 64114

Greg Patterson  
Residential Utility Consumer Office  
2828 N. Central Avenue  
Suite 1200  
Phoenix, Arizona 85004

Jerry L. Rudibaugh  
November 8, 1996 Page 4

Michael W. Patten  
Brown & Bain  
2901 N. Central Avenue  
Phoenix, Arizona 85012-2788

*Betty J. Griffin*

**BEFORE THE ARIZONA CORPORATION COMMISSION**

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26

**RENZ D. JENNINGS  
CHAIRMAN  
MARCLA WEEKS  
COMMISSIONER  
CARL J. KUNASEK  
COMMISSIONER**

**IN THE MATTER OF THE PETITION OF )  
AMERICAN COMMUNICATIONS SERVICES )  
INC. AND AMERICAN COMMUNICATIONS )  
SERVICES OF PIMA COUNTY, INC. FOR )  
ARBITRATION WITH U S WEST )  
COMMUNICATIONS, INC. OF )  
INTERCONNECTION RATES, TERMS, AND )  
CONDITIONS PURSUANT TO 47 U.S.C. )  
§252(b) OF THE TELECOMMUNICATIONS )  
ACT OF 1996. )**

**DOCKET NO. U-3021-96-448  
DOCKET NO. U-3245-96-448  
DOCKET NO. E-1051-96-448**

**IN THE MATTER OF THE PETITION OF )  
AT&T COMMUNICATIONS OF THE )  
MOUNTAIN STATES, INC. FOR )  
ARBITRATION WITH U S WEST )  
COMMUNICATIONS, INC. OF )  
INTERCONNECTION RATES, TERMS, AND )  
CONDITIONS PURSUANT TO 47 U.S.C. )  
§ 252(b) OF THE TELECOMMUNICATIONS )  
ACT OF 1996. )**

**DOCKET NO. U-2428-96-417  
DOCKET NO. E-1051-96-417**

**IN THE MATTER OF THE PETITION OF )  
MFS COMMUNICATIONS COMPANY, INC. )  
FOR ARBITRATION WITH U S WEST )  
COMMUNICATIONS, INC. OF )  
INTERCONNECTION RATES, TERMS, AND )  
CONDITIONS PURSUANT TO 47 U.S.C. )  
§ 252(b) OF THE TELECOMMUNICATIONS )  
ACT OF 1996. )**

**DOCKET NO. U-2752-96-362  
DOCKET NO. E-1051-96-362**

**IN THE MATTER OF THE PETITION OF )  
TCG PHOENIX FOR ARBITRATION WITH )  
U S WEST COMMUNICATIONS, INC. OF )  
INTERCONNECTION RATES, TERMS, AND )  
CONDITIONS PURSUANT TO 47 U.S.C. )  
§ 252(b) OF THE TELECOMMUNICATIONS )  
ACT OF 1996. )**

**DOCKET NO. U-3016-96-402  
DOCKET NO. E-1051-96-402**



**RESPONSIVE TESTIMONY OF ANTHONY J. DITIRRO  
ON BEHALF OF  
MCI TELECOMMUNICATIONS CORPORATION**

**Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND BY WHOM  
ARE YOU EMPLOYED.**

A. My name is Anthony J. DiTirro. My business address is 201 Spear Street, 9th Floor, San Francisco, California. I am employed by MCI Telecommunications Corporation ("MCI") as a Regulatory Manager.

**Q. ARE YOU THE SAME ANTHONY J. DITIRRO WHO PROVIDED  
DIRECT TESTIMONY IN THIS PROCEEDING?**

A. Yes, I am.

**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A. The purpose of my testimony is to respond to the testimony of Dr. Robert G. Harris, Ms. Susanne J. Mason, and Ms. Geri G. Santos-Rach on behalf of U S WEST Communications, Inc. ("USWC").

**Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

A. USWC, through both the testimony of Dr. Harris and Ms. Mason, attempts to argue for an avoided cost concept which would place the Incumbent LECs ("ILECs") in control of the determination of the resale discount for its reseller competitors. I will explain the obvious anticompetitive impact of such a plan. I will also explain why the pricing

restrictions proposed by USWC will undermine competition. I will then point out the serious flaws in USWC's avoided cost study.

A detailed discussion of MCI's avoided cost model is included in my direct testimony. Consequently, I will not discuss our methodology here except to contrast it with USWC's. However, before I address these substantive issues, I must comment on USWC's opposition to the FCC Interconnection Order ("FCC Order") and its recommendation that the Board disregard the portions of this decision which are at odds with USWC's anticompetitive resale strategy.

**Q. PLEASE EXPLAIN USWC'S OPPOSITION TO THE RECENT FCC ORDER.**

A. Dr. Harris discusses the wholesale pricing issues at pages 75 through 87 of his testimony. Dr. Harris spends the majority of this testimony arguing that the FCC Order does not comply with the resale provisions of the Act. He expresses his clients opposition to three specific areas of the decision regarding pricing and costing:

1. He opposes the FCC's proxy discount of 17-25% as an unduly expansive definition of "cost that will be avoided;"
2. He opposes the FCC's proxy wholesale price discount inclusion of an allocation of joint and common costs, which he claims will not be avoided;

3. He opposes the alleged double-discounting;

I believe Dr. Harris' arguments in opposition to the FCC Order should be directed to the FCC or the courts rather than confusing the record of this proceeding. However, I would note that USWC witnesses in this proceeding frequently cite the FCC Order to support their positions when it suits their purposes.

Of course parts of the FCC's decision were recently stayed. Although I am not a lawyer, my understanding of the stay is that the court is considering whether the FCC exceeded its authority and infringed on the authority of the states in setting rates and prices. The Court did not look to the reasonableness of the FCC's determinations regarding the appropriate calculation of avoided costs. The court did not address any of the issues opposed by USWC. The FCC's approach therefore is still a reasonable benchmark and one that this Commission can and should adopt. The FCC has addressed the same issues before this Commission and considered many of the same arguments. It is important to remember that the FCC adopted MCI's avoided cost study with modifications as reasonable. MCI has modified its original study to conform to the FCC's findings. Consequently, I believe MCI's avoided costs study represents a reasonable calculation of the retail costs USWC avoids in the provision of wholesale services.

**Q. PLEASE EXPLAIN WHAT CRITERIA YOU BELIEVE SHOULD BE FOLLOWED TO DEVELOP A VALID AVOIDED COST DISCOUNT.**

**A. The most obvious criteria is that the avoided cost study must comply with the Act. Section 252(d)(3) of the Act makes it clear that:**

**a state commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.**

**I believe that this requires the avoided cost calculation to be based on those same costs and costing methods employed to set the retail rates.**

**Consequently, a tops-down study using accounting data used to set the ILEC's rates is the appropriate costing methodology.**

**I believe that a correctly devised avoided cost study eliminates all the retailing costs which are avoided when the ILEC wholesales services. Anything short of this saddles the new entrants with duplicative retailing costs creating an anticompetitive price squeeze for these new entrants.**

**I believe that a proper avoided cost study will identify both direct and indirect avoided costs. Clearly as direct costs fall because of the avoidance of these costs indirect costs should fall as well.**

And last, but certainly not least, a valid avoided costs study should be verifiable and well documented.

MCI' avoided cost study meets all these criteria and results in a reasonable avoided costs discount of 22.5% for USWC in Arizona.

**Q. DOES USWC'S AVOIDED COSTS STUDY MEET THESE CRITERIA?**

A. No. In fact, USWC's avoided cost study fails to meet any of these criteria. USWC incorrectly uses forward looking costs on a "bottoms-up" basis. Consequently, USWC's uses costs that are different the those costs and costing methodologies used to set the rates to which the discount will be applied. USWC does not eliminate all the costs avoided when wholesaling services and USWC proposes to add back costs it allegedly incurs in wholesaling. USWC fails to properly identify indirect avoided costs. Finally and most importantly, USWC's avoided cost study is not verifiable or adequately documented. Consequently, the Commission cannot rely of USWC's cost study to set the avoided costs discount for Arizona.

**Q. PLEASE EXPLAIN WHY YOU BELIEVE USWC'S AVOIDED COST METHODOLOGY IS ANTICOMPETITIVE.**

A. USWC believes that the ILEC should determine the appropriate amount of avoided costs based on its unilateral determination what costs its

chooses to shed in wholesaling its services. USWC's proposal ignores the realities of the marketplace as it fails to recognize that an ILEC has a real incentive to burden its reseller competitors with inflated costs. For example, under USWC's approach an ILEC could choose to continue to attribute some of its advertising costs to resold services even though the advertising is retail oriented. Under USWC's approach such costs would not be eliminated as avoided merely because the ILEC chooses to continue to attribute those costs. Consequently, the ILEC is in control of the determination of the resulting discount. Such an approach allows the ILEC to burden its reseller competitors with duplicative costs which ultimately create an anticompetitive price squeeze.

**Q. PLEASE EXPLAIN HOW USWC'S SCHEME WILL CREATE AN ANTICOMPETITIVE PRICE SQUEEZE.**

A. While USWC's argues that the amount of avoided costs should be determined by the ILECs, it again completely ignores the reality that the reseller will also separately incur many of these same retailing costs. If the reseller must cover a portion USWC's advertising costs while incurring its own separate advertising costs, the reseller must pay twice for such retailing expenses. Not only would resellers pay excess and duplicative retailing costs which creates the anticompetitive price squeeze, the reseller would end up subsidizing the ILECs retailing

costs, an additional advantage for the ILEC. Clearly, such a scheme will undermine the development of resale competition by placing reseller competitors at a pricing disadvantage to the ILEC's.

The FCC considered the arguments of the parties on this issue and its conclusion was very clear:

There has been considerable debate on the record in this proceeding and before the state commissions on whether section 252(d)(3) embodies an "avoided" cost standard or an "avoidable" cost standard. We find that the portion [of the retail rate] ... attributable to costs that will be avoided" includes all of the costs that the LEC incurs in maintaining a retail, as opposed to a wholesale, business. In other words, the avoided costs are those that an incumbent LEC would no longer incur if it were to cease retail operations and instead provide all of its services through resellers. Thus, we reject the arguments of incumbent LEC's and others who maintain that the LEC must actually experience a reduction in its operating expenses for a cost to be considered "avoided" for the purposes of section 252(d)(3). We do not believe Congress intended to allow incumbent LEC's to sustain artificially high wholesale prices by declining to reduce their expenditures to the degree that certain costs are readily avoidable. We therefore interpret the 1996 Act as requiring states to make an objective assessment of what costs are reasonably avoidable when a LEC sells its services wholesale. We note that Colorado, Georgia, Illinois, New York and Ohio commissions have all interpreted the 1996 Act in this manner. (FCC Order, Paragraph 911)

MCI proposes an avoided cost study which is objective, verifiable and consistent with the FCC Order. Moreover, neither the ILEC nor the reseller can execute undue control over the study results as is the case with USWC's scheme.

**Q. PLEASE EXPLAIN HOW USWC HAS MISREPRESENTED MCI'S  
AVOIDED COST METHODOLOGY.**

1400 \* MCI \* 004

A. First, USWC asserts that MCI's plan is theoretic. While it never fully explains exactly what is meant by theoretic, this assertion does not accurately describe MCI's methodology. MCI employs USWC's actual 1995 expenses and identifies the avoided costs consistent with the FCC's Order. MCI employs a "tops down" methodology which is easily verifiable and is consistent with the FCC Order unlike USWC's scheme. As I will explain below, in fact, MCI's plan is much less theoretic than USWC's own plan.

Moreover, USWC, through the testimony of Ms. Mason, incorrectly states that MCI "proposed that the discount should be calculated by subtracting out all "retail" expenses, but without adding in any "wholesale" costs."

A correct reading of my testimony would find that MCI does propose inclusion of a reasonable amount of wholesaling costs. On page 4 of my direct testimony I state that "MCI treated only 90% of these expenses as avoided to recognize the costs that the ILECs do not avoid in wholesaling these services."

I submit that MCI's methodology is very conservative in that it does not eliminate costs which I believe would be totally avoided in a resale environment. As an example, USWC will NOT be incurring advertising costs for resale services. Certainly, USWC need not advertise to attract MCI to its

services. MCI is coming to USWC with this petition to request its services.

MCI does not have any plans to co-sponsor advertising with USWC.

Consequently, I cannot see any reason USWC would incur advertising expenses for the services it wholesales to MCI. I believe that same argument could be made for sales costs because USWC is not executing a sales effort to attract MCI to its door. Yet, MCI's study only deducts 90% of these advertising and sales costs.

MCI purposely included these costs to cover any wholesaling costs the ILEC may incur in serving reseller customer. I submit that this approach results in a favorable outcome for ILECs.

**Q. PLEASE EXPLAIN THE ERRORS IN USWC'S MISGUIDED "DOUBLE DISCOUNT" ARGUMENTS.**

A. It appears that USWC witnesses Dr. Harris and Ms. Mason cannot distinguish the difference between a retail volume discount and a wholesale discount. The distinction is simple. A retail volume is offered when retail customer buys in volume but is still trading on a retail basis. While Ms. Mason ventures into the sporting goods industry to explain her misguided view of volume/wholesale discounts, I believe an understanding of the basis for discounts typically offered in this industry would be more useful information.

In the telephone business, higher volumes of traffic allows the carrier to employ efficiencies in its network to reduce costs of serving a high-volume customer. A prime example of the efficiencies sought by carriers is the ability to use special access to serve a customer, rather paying the exorbitant per minute switched access rates charged by ILECs. While the carrier still incurs its retailing costs for high-volume customers, it can save a significant portion of its network costs by serving the high-volume customer using a dedicated facility directly from the customer to the carrier.

Wholesale discounts, on the other hand, result from the service provider avoiding retailing costs, such as marketing, billing and collection costs, normally incurred to attract customers in a competitive market. The FCC recognizes that ILECs will avoid these retailing costs when they offer the mandated resold services because the ILECs will be the only service providers of these resold services. This is a key fact which USWC ignores in its discussion of discounts. USWC will not incur retailing costs in attracting resale customers. MCI is coming to USWC in this petition requesting these services at reasonable terms and conditions. Consequently, USWC avoids the majority of its retailing costs in serving MCI. This isn't theoretic any more than MCI's petition is theoretic.

Consequently, USWC's double-discounts are, in fact, created by two separate types of cost savings, volume generated network efficiencies and avoided retail costs and are separately legitimate.

Moreover, if one accepts USWC's double-discount prohibition, reseller competitors would be precluded from competing with USWC for the high-volume market. Since USWC is proposing to price its high-volume resale service offering to recognize only the volume savings offered to its resale customers and does not eliminate its retailing costs, reseller competitors, such as MCI, will suffer an anticompetitive price squeeze when pricing against USWC due to the burden of unnecessarily covering USWC's retailing costs. Specifically, if a reseller such as MCI would attempt to directly compete with USWC for a high-volume customer, MCI could not offer as low a price as USWC because of the duplicative retailing costs. USWC completely ignores these obvious anticompetitive results of its scheme but, instead, seems to believe that the relevant price of its resold service has no effect on the success of resale competition.

- .Q. DR. HARRIS STATES THAT NEW ENTRANTS WILL RESELL SERVICES AS LONG AS THEY CAN "BUY" SERVICE AT PRICES BELOW WHAT IT WOULD COST TO MAKE THEIR OWN FACILITIES BASED SERVICE. DO YOU AGREE?**

A. No. The prices of services provided for resale are a **CRUCIAL** consideration in the new entrant's decision to "buy" the resold service. Dr. Harris seems to ignore the possibility that competitors may simply choose not to enter the telecommunications market in a area where anticompetitive pricing like that proposed by USWC is the only immediately available alternative to market entry. I am not saying that competitors will never enter the market but the inflated resale rates will delay the implementation of competition.

**Q. DO YOU BELIEVE THAT NEW ENTRANTS WHO CHOOSE TO ENTER THE MARKET VIA RESALE WILL ALWAYS BE RESELLERS?**

A. No. Many resellers -- including MCI -- have evolved into facilities-based providers. Before and after divestiture, MCI resold AT&T service while it built out its own network. I expect the same type of behavior as competition develops in the local market.

New entrants must ultimately distinguish their service from that of the ILEC if they hope to grow market share. This can be done through marketing by creating perceptions and brand recognition, pricing and by providing portions of the service. For instance, a new entrant might provide its own billing with more features and detail than that provided by the ILEC. A new entrant might also provide its own switching and transport thereby allowing them to provide unique features and network intelligence that might not be available from the

ILEC. This is the way competition develops from resale to facilities-based competition. Until such competition develops, however, it is critical that the Commission ensure that the wholesale pricing discounts are set correctly.

**Q. DR. HARRIS STATES THAT SETTING THE AVOIDED COSTS DISCOUNTS TOO HIGH WILL HARM FACILITIES-BASED COMPETITION. PLEASE COMMENT.**

A. Setting the wholesale pricing discount too high would not be in the public interest. It would also not be in the public interest to set the discounts too low. In reviewing USWC's resale proposal in this proceeding, however, it would be good to remember the findings of the FCC:

As discussed above at sections II.A, II.B and V.B, we believe that incumbent LECs have little incentive to facilitate the ability of new entrants, including small entities, to compete against them... (FCC Order at Paragraph 307)

**Q. SHOULD THE COMMISSION SET ITS WHOLESALE PRICES TO ENCOURAGE FACILITIES BASED COMPETITION OVER RESALE COMPETITION?**

A. No. I do not believe the Commission nor any other regulatory body should attempt to pick winners and losers in the implementation of competition. In fact, the FCC Order specifically noted that resale was an important entry strategy in both the short and long-run:

Resale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities.

Further, in some areas and for some new entrants, we expect that the resale option will remain an important entry strategy over the longer term. Resale will also be an important entry strategy for small businesses that may lack capital to compete in the local exchange market by purchasing unbundled elements or by building their own networks. In light of the strategic importance of resale to the development of competition, we conclude that it is especially important to promulgate national rules for use by state commissions in setting wholesale rates. (Paragraph 907).

Moreover, USWC's argument presumes that potential competitors will choose resale over facilities based service, when, in fact, the resale entry strategy will encourage facilities based service. Competitors will be more likely to invest in facilities in an area after it has developed a customer base through resale. This strategy is considerable less risky for the new entrant than investing in facilities before the new entrant has any customer base.

Given the fact that new entrants have opportunities in various geographic areas, these competitors will enter where terms and conditions are most favorable. To the contrary, USWC seems to believe that new entrants will be willing to enter an area even though the adopted terms and conditions are unfavorable to resale competition. Again, USWC's resale pricing proposal is out of touch with the realities of a competitive market. USWC'S plan will discourage resale competition now and future facility-based entry by competitors whose strategy will naturally progress from resale to facilities-based service provision.

**Q. PLEASE EXPLAIN THE PROBLEMS YOU SEE IN USWC'S  
CALCULATION OF AN AVOIDED COST DISCOUNT.**

- A. USWC proposes an avoided cost study which is based on a bottoms-up basis - a plan which is poorly documented in the testimony of Geri Santos-Rach but appears to be in conflict with the Act. Although it is not fully explained, I believe that USWC is proposing an avoided cost study based on incremental costing. This bottoms-up incremental scheme is not only unverifiable, but is in direct conflict with the Act and the FCC order. The FCC Order, at paragraph 915, concludes that:

The 1996 Act requires that wholesale rates be based on existing retail rates and thus clearly precludes use of a "bottom up" TSLRIC study to establish wholesale rates that are not related to the rates for the underlying retail services.

Consequently, USWC's avoided cost study should be rejected by the Commission as violative of both the FCC Order and the Act.

**Q. DOES MCI'S AVOIDED COST STUDY COMPLY WITH THE FCC  
ORDER AND RESALE RULES?**

- A. Yes, it does. As noted by Dr. Harris, the FCC Order refers to the MCI approach to determining which expense accounts are avoidable.<sup>1</sup> The FCC decision regarding the appropriate model for calculating the wholesale pricing discount, however, was based on more than just MCI's proposal. The Order states as follows:

---

<sup>1</sup>Direct Testimony of Dr. Harris at 76.

925. We find that we can use MCI's model, with some modifications, along with the results of certain state proceedings, to establish a range of rates that would produce an acceptable default wholesale discount rate that reasonably approximates the amount of avoided costs that should be subtracted from the retail rate. ... The MCI model is a reasonable attempt at estimating avoided cost in accordance with section 252(d)(3) using only publicly available data. We find, however, that we should modify certain features of the model.

**Q. HAVE THE MODIFICATIONS DESCRIBED IN THE FCC ORDER BEEN INCORPORATED INTO THE MCI MODEL USED IN THIS PROCEEDING?**

A. Yes. As I noted in my direct testimony, the original MCI model has been modified to be consistent with the FCC rules.

**Q. SHOULD THE BOARD ADOPT THE WHOLESALE PRICING DISCOUNT OF 22.5 PERCENT AS RECOMMENDED BY MCI?**

A. Yes. I believe this is a reasonable resale discount consistent with the FCC Order and the Act.

**Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes.

STATE OF ARIZONA )  
 )  
COUNTY OF MARICOPA )

ss AFFIDAVIT OF ANTHONY J. DITIRRO

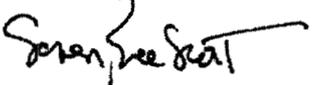
Anthony J. DiTirro, of lawful age being first duly sworn, deposes and states:

1. I am a Senior Manager of Regulatory Affairs for MCI Telecommunications Corporations ("MCI), and have caused to be filed written responsive testimony in support of MCI in Docket No. U-3021-96-448, et. al.
2. Such Testimony is true and correct as I verily believe.

Further affiant sayeth not.

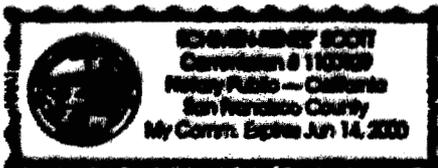
  
Anthony J. DiTirro

SUBSCRIBED AND SWORN to before me this 7th day of November, 1996.

  
Notary Public

My Commission Expires:

June 14, 2000



**BEFORE THE ARIZONA CORPORATION COMMISSION**

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26

**RENZ D. JENNINGS  
CHAIRMAN  
MARCIA WEEKS  
COMMISSIONER  
CARL J. KUNASEK  
COMMISSIONER**

**IN THE MATTER OF THE PETITION OF  
AMERICAN COMMUNICATIONS SERVICES  
INC. AND AMERICAN COMMUNICATIONS  
SERVICES OF PIMA COUNTY, INC. FOR  
ARBITRATION WITH U S WEST  
COMMUNICATIONS, INC. OF  
INTERCONNECTION RATES, TERMS, AND  
CONDITIONS PURSUANT TO 47 U.S.C.  
§252(b) OF THE TELECOMMUNICATIONS  
ACT OF 1996.**

**DOCKET NO. U-3021-96-448  
DOCKET NO. U-3245-96-448  
DOCKET NO. E-1051-96-448**

**IN THE MATTER OF THE PETITION OF  
AT&T COMMUNICATIONS OF THE  
MOUNTAIN STATES, INC. FOR  
ARBITRATION WITH U S WEST  
COMMUNICATIONS, INC. OF  
INTERCONNECTION RATES, TERMS, AND  
CONDITIONS PURSUANT TO 47 U.S.C.  
§ 252(b) OF THE TELECOMMUNICATIONS  
ACT OF 1996.**

**DOCKET NO. U-2428-96-417  
DOCKET NO. E-1051-96-417**

**IN THE MATTER OF THE PETITION OF  
MFS COMMUNICATIONS COMPANY, INC.  
FOR ARBITRATION WITH U S WEST  
COMMUNICATIONS, INC. OF  
INTERCONNECTION RATES, TERMS, AND  
CONDITIONS PURSUANT TO 47 U.S.C.  
§ 252(b) OF THE TELECOMMUNICATIONS  
ACT OF 1996.**

**DOCKET NO. U-2752-96-362  
DOCKET NO. E-1051-96-362**

**IN THE MATTER OF THE PETITION OF  
TCG PHOENIX FOR ARBITRATION WITH  
U S WEST COMMUNICATIONS, INC. OF  
INTERCONNECTION RATES, TERMS, AND  
CONDITIONS PURSUANT TO 47 U.S.C.  
§ 252(b) OF THE TELECOMMUNICATIONS  
ACT OF 1996.**

**DOCKET NO. U-3016-96-402  
DOCKET NO. E-1051-96-402**



**Q. PLEASE STATE YOUR NAME.**

A. Richard Cabe.

**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A. My testimony responds to US West's recent proposal to impose a surcharge on usage of US West's switching element in order to recover certain historical costs.

**Q. DOES THE US WEST PROPOSAL ADVANCE THE PROCOMPETITIVE AND DEREGULATORY PURPOSES OF THE TELECOMMUNICATIONS ACT?**

A. No. The proposal is to establish an administered price which could not be obtained in a competitive market. The surcharge amounts to a tax intended to provide a subsidy to US West which favors neither deregulation nor the development of competition.

**Q. WHAT IS THE NATURE OF THE COSTS WHICH US WEST SEEKS TO RECOVER THROUGH THE PROPOSED SURCHARGE?**

A. US West proposes to use the surcharge to recover its theoretical reserve deficiency. The theoretical reserve deficiency is the amount by which US West's rate base exceeds the economic value of its assets. This excess is not a cost, but an amount to be subtracted from the rate base valuation of assets. US West proposes amortizing this excess over five years and collecting the resulting amount from users at end office and tandem switching. The so-

called cost of amortizing any reserve deficiency is not part of the TELRIC of any unbundled network element, nor can it be regarded as a part of the company's forward looking common costs. The only sense in which this amortization can be regarded as a cost is by reference to a rate-of-return or other rate-based proceeding, contrary to the requirements of the Federal Telecommunications Act.

**Q. IS THIS THE PROCEEDING IN WHICH THE COMMISSION SHOULD CONSIDER US WEST'S PROPOSAL FOR AMORTIZATION AND RECOVERY OF AN ACCESS VALUATION OF ITS RATE BASE?**

**A. No.** The Act established an obligation for incumbent LEC's to interconnect and provide unbundled network elements and called for rates for interconnection and unbundled network elements to be established through interconnection agreements reached by negotiation or arbitration. If arbitrated, the Act calls for rates to be based on cost determined without reference to a rate-of-return or other rate-based proceeding. The FCC's interpretation of these and other provisions of the Act lead to the conclusion that rates for interconnection and unbundled elements are not the proper vehicles through which to recover any embedded cost which the incumbent LEC may be allowed to recover. The FCC has initiated a separate proceeding in which to consider issues such as the claimed reserve deficiency, and insofar as it is regarded as a problem this Commission should consider a similar approach.

The Commission should not allow the arbitration of interconnection agreements to be side tracked by US West's introduction of questions which are not properly at issue and which the Federal Telecommunications Act explicitly excludes from consideration in arbitration of interconnection agreements. US West's proposal raises public policy questions of much broader scope than are at issue in the interconnection agreements which are the subject of this arbitration.

**Q. YOU CLAIM THAT US WEST'S PROPOSAL WILL NOT ADVANCE THE PROCOMPETITIVE AND DEREGULATORY PURPOSES OF THE FEDERAL TELECOMMUNICATIONS ACT. PLEASE EXPLAIN.**

- A. The purposes of the Act are served by prices in interconnection agreements that are economically efficient and competitively neutral. US West's proposal fails both of these tests.

**Q. HOW DOES US WEST'S SWITCHING SURCHARGE PROPOSAL FAIL THE TEST OF ECONOMIC EFFICIENCY?**

- A. Any imposition of uneconomic costs as a surcharge on usage of a network element will discourage use of that element by end users who must ultimately pay for the element. This discouraging effect of the surcharge will create allocative inefficiency. Insofar as wholesale users of the element alter their choices in order to minimize costs as distorted by the surcharge, a productive inefficiency will also result.

**Q. IN WHAT WAYS DOES THE PROPOSAL FAIL TO BE COMPETITIVELY NEUTRAL?**

**A. First, it isn't clear that any mechanism which accomplishes the stated purpose of US West's proposal could be regarded as competitively neutral. This proposal is intended to provide a flow of funds into the incumbent to provide reimbursement of investment costs which are properly regarded as sunk. In a competitive market, when costs are sunk they are sunk; they are not recovered by any means because the market will not permit it. Entrants have incurred substantial costs of entry, such as the cost of participating in this arbitration, which become sunk as soon as they are incurred and not subject to any sort of reimbursement. Thus, reimbursing US West for this sunk cost amounts to a subsidy flow to US West which can only increase the financial strength of the dominant firm relative to new entrants.**

**Aside from the effect of providing a source of financing for the incumbent which is not available to entrants, the proposal is not competitively neutral if it places either entrants or the incumbent at a disadvantage. If this proposal were adopted it would put entrants at a competitive disadvantage because the surcharge becomes a real, forward looking cost which the entrants must bear in order to compete with the incumbent. My understanding of US West's proposal is that it does not include an increase in US West retail rates for all services which rely on the switching elements to which the surcharge would apply, so entrants would be facing a vertical price squeeze. Even if retail rates were increased as part of the proposal, or if an imputation requirement**

were imposed, from US West's point of view, the surcharge is not a part of the forward looking cost of providing services. This fact gives US West an incentive to exploit its advantage by undercutting its retail rates through discounts or other marketing devices, or avoid the requirement of imputation by misstating its costs.

Even if an imputation requirement were implemented perfectly, another way in which US West's proposal could have systematically different effects on entrants than on an incumbent is that the proposed elevation in usage prices could limit the viability or rate of adoption of new services. Opportunities for successful entry often come from new product ideas, and the inefficiency created by the surcharge could limit such opportunities. Insofar as new entrants are more dependent on the success of new product and service ideas that rely on efficient pricing of unbundled network elements, the proposal is not competitively neutral.

**Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

**A. Yes.**

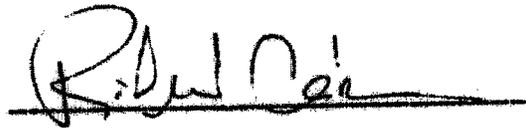
STATE OF NEW MEXICO )  
 )  
COUNTY OF DONA ANA )

ss AFFIDAVIT OF RICHARD CABE

Richard Cabe, of lawful age being first duly sworn, deposes and states:

1. I have caused to be filed rebuttal testimony in support of MCImetro Access Transmission Services, Inc. In Docket No. U-3021-96-448, et. Al.
2. Such testimony is true and correct as I verily believe.

Further affiant sayeth not.



Richard Cabe

SUBSCRIBED AND SWORN to before me this 7th day of November, 1996.



Notary Public

My Commission Expires:

11/27/99



OFFICIAL SEAL  
CLAIR A. LARKIN  
NOTARY PUBLIC  
STATE OF NEW MEXICO

My Commission Expires 11/27/99