State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: MARCH 18, 1999

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF COMMUNICATIONS (DOWDS, KING, OLILA, FOGLEMAN)
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (CAUSSEAUX, MAUREY, LEE)
DIVISION OF LEGAL SERVICES (COX)

RE: DOCKET NO. 980696-TP - DETERMINATION OF THE COST OF BASIC LOCAL TELECOMMUNICATIONS SERVICE, PURSUANT TO SECTION 364.025, FLORIDA STATUTES.

AGENDA: 03/30/99 - REGULAR AGENDA - POST HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\CMU\WP\980696RE.RCM

CASE BACKGROUND

Section 364.025(4)(b), Florida Statutes, requires the Commission to determine and report to the Legislature the total forward-looking cost of providing basic local telecommunications services on a geographic basis no larger than a wire center, using a cost proxy model to be selected by the Commission after notice and opportunity for hearing. As stated in the law, the purpose of this study is to assist the Legislature in establishing a permanent universal service mechanism. For small local exchange companies that serve fewer than 100,000 access lines, Section 364.025(4)(c), Florida Statutes, allows the Commission in its discretion to select a different proxy model or a fully distributed embedded cost allocation.

From October 12 through October 16, 1998, the Commission conducted a formal administrative hearing according to the

provisions of Chapter 120, Florida Statutes, and its rules. Twenty parties intervened and participated in the proceeding. There were many issues addressed at the hearing, including the fundamental issue of defining "basic local service" for the purpose of establishing a permanent universal service mechanism. The principal point of contention between the parties was which cost proxy model should the Commission select for the three major incumbent local exchange companies (LECs): BellSouth Telecommunications, Inc. (BellSouth), GTE Florida, Inc. (GTEFL), and Sprint-Florida, Incorporated (Sprint). BellSouth, GTEFL, and Sprint either sponsored or supported the BCPM 3.1 cost proxy model. AT&T Communications of the Southern States, Inc. (AT&T) and MCI Telecommunications Corporation (MCI) sponsored the HAI 5.0a cost proxy model. Both models contain highly complex algorithms and require thousands of discrete input values. Proponents of both models argued that while neither model was perfect, their model was superior and best met the requirements of Section 364.025(4), Florida Statutes.

On January 7, 1999, the Commission issued Order No. PSC-99-0068-FOF-TP in which it selected the BCPM 3.1 cost proxy model with modifications as the better model of the two proposed and also approved the many input values that are required to populate the model. This model is to be used for determining the cost of basic local telecommunications service for the three large LECs: BellSouth, GTEFL, and Sprint. For the small LECs, the Commission approved the proposed embedded cost methodology with several modifications and the necessary input values.

On January 22, 1999, Sprint filed a Motion for Reconsideration of Order No. PSC-99-0068-FOF-TP. Sprint's Motion addressed the limited issue of the Commission's decision to substitute a $4,350 Loop Cost Investment Cap for the $10,000 cap submitted as a default input in the BCPM 3.1. In conjunction with this filing, Sprint submitted a Request for Oral Argument on its Motion for Reconsideration. Also on that date, GTEFL filed its Petition for Reconsideration of Order No. PSC-99-0068-FOF-TP. GTEFL's Petition was limited to the Commission's recommended model inputs for depreciation and cost of capital.

On February 1, 1999, AT&T, e.spire Communications, Inc. (e.spire), the Florida Competitive Carriers Association (FCCA), the Florida Cable Telecommunications Association (FCTA), MCI, and Worldcom Technologies, Inc.(Worldcom) (collectively, "Joint Respondents") filed their Joint Response to the Sprint and GTEFL Requests for Reconsideration, requesting that the Requests for Reconsideration be denied.

On February 3, 1999, GTEFL filed its Response in Support of Sprint-Florida's Motion for Reconsideration of Order No. PSC-99-0068-FOF-TP. GTEFL supports Sprint in requesting the Commission to reconsider its decision to apply a $4,350 loop investment cap to all carriers in Florida. GTEFL urges adoption of the $10,000 cap supported by Sprint and GTEFL during this proceeding.

On February 15, 1999, the Joint Respondents filed a Joint Response to GTEFL's Response in Support of Sprint's Motion for Reconsideration, requesting that the Commission disregard GTEFL's response, or in the alternative, consider this response of the Joint Respondents as a substantive reply to GTEFL's response. On February 22, 1999, GTEFL filed a Motion to Strike the Joint Petitioners' Joint Response to GTEFL's Response in Support of Sprint's Motion for Reconsideration.

Set forth below are staff's recommendations on Sprint and GTEFL's requests for reconsideration, Sprint's request for oral argument on its motion for reconsideration, and GTEFL's motion to strike the joint response to GTEFL's response in support of Sprint's motion for reconsideration.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission grant GTE Florida Incorporated's Motion to Strike the Joint Response of AT&T, e.spire, FCCA, FCTA, MCI, and WorldCom to GTE Florida, Inc.'s Response in Support of Sprint-Florida's Motion for Reconsideration?

RECOMMENDATION: Yes. The Commission should grant GTE Florida Incorporated's Motion to Strike the Joint Response of AT&T, e.spire, FCCA, FCTA, MCI, and WorldCom to GTE Florida, Inc. Response in Support of Sprint-Florida's Motion for Reconsideration. **(COX)**

STAFF ANALYSIS: As stated above, on February 3, 1999, GTEFL filed its Response in Support of Sprint-Florida's Motion for Reconsideration of Order No. PSC-99-0068-FOF-TP. GTEFL filed its response in support of Sprint in requesting the Commission to reconsider its decision to apply a $4,350 loop investment cap to all carriers in Florida. GTEFL urges adoption of the $10,000 cap supported by Sprint and GTEFL during this proceeding.

On February 15, 1999, the Joint Respondents filed a Joint Response to GTEFL's Response in Support of Sprint's Motion for Reconsideration. The Joint Respondents contend that GTEFL's Response is a Second Petition for Reconsideration and not a response as would be proper under the Commission's rules. The Joint Respondents contend that GTEFL's filing contains an excessive amount of arguments and therefore moves beyond what is properly contained in a response. In the alternative, should the Commission consider GTEFL's response valid the Joint Respondents ask that their response be treated as a substantive reply to GTEFL's filing.

Finally, on February 22, 1999, GTEFL filed a Motion to Strike the Joint Respondents' Joint Response to GTEFL's Response in Support of Sprint's Motion for Reconsideration. GTEFL argues that the Joint Response is improper under the Commission's rules as a response to a response to a motion for reconsideration.

Staff believes that the parties have created their own procedural quagmire, which deserves little time and consideration by the Commission. The parties are both walking on the edge of what is permissible motion and response practice under the Commission's procedural rules. GTEFL appears to have legitimately filed a response in support of Sprint's Motion for Reconsideration. The Joint Petitioners' argument that the response is too long to be a response is completely without merit.

There is question, however, whether GTEFL is truly responding or instead filing a second petition for reconsideration. Sprint's Motion for Reconsideration does ask that the $4,350 loop cost investment cap be applied to BellSouth, and not GTEFL and Sprint. Therefore, any party to the proceeding, such as GTEFL, has a procedural right to respond in opposition or support of the motion. It simply happens that in this case Sprint's motion for reconsideration, if granted, may benefit GTEFL. Accordingly, the Commission need not disregard GTEFL's response in support of Sprint's motion.

Based on that analysis, GTEFL's motion to strike the Joint Response to GTEFL's response to Sprint's Motion for Reconsideration should be granted. A response to a response to a motion for reconsideration is not valid under Commission Rule 25-22.0376, Florida Administrative Code. This rule allows parties to file a response to a motion for reconsideration. GTEFL's response does "push the line" with respect to what is procedurally proper but does not cross it in this case. The Joint Respondent's response to a response clearly crosses the line. Accordingly, the Commission should grant GTEFL's Motion to Strike.

ISSUE 2: Should Sprint-Florida, Inc.'s Request for Oral Argument on its Motion for Reconsideration of Order No. PSC-99-0068-PCO-TP be granted?

RECOMMENDATION: No. Sprint's Request for Oral Argument should be denied. **(COX)**

STAFF ANALYSIS: Sprint requests that the Commission permit a brief opportunity for the company to present oral argument in support of its motion for reconsideration. Sprint believes that oral argument is necessary for several reasons. First, Sprint was unaware that the loop investment cap was a disputed issue, or that the Commission might intend to apply the BellSouth study proposed value to Sprint. Second, Sprint believes that the Commission may have been unaware of the material effect that this decision would have on the company due to the lack of notice and the late nature of the issue being raised. Finally, Sprint believes that the complexity of the issue and the limitations of written explanation necessitate discussion of the matter. No party responded to Sprint's request for oral argument.

It appears that Sprint would like the opportunity to argue the merits of the loop cap investment issue through the vehicle of its request for oral argument. Furthermore, Sprint wants this opportunity because it did not present evidence or testimony to support its position on this issue through the hearing process because it believed that the issue was not in dispute. The reality is that the selection of a model and the necessary input values were clearly at issue in this proceeding, as plainly evidenced by the volume of testimony, exhibits, and filings in this proceeding. The loop investment cap is an input value that was at issue. BellSouth addressed this issue through its witness, Witness Caldwell, and accordingly, staff addressed the issue in its recommendation. (Caldwell, EXH 75, pp.52-53). Sprint's failure to put on its case on the loop investment cap is insufficient grounds to grant its request for oral argument.

Furthermore, Sprint's contention that the Commission's alleged failure to consider the significance that this input would have on the company is simply another excuse to give Sprint a second chance to proffer its case. Again, this excuse does not warrant granting Sprint's request for oral argument.

Finally, the argument that may deserve some consideration is the complexity of this issue. Sprint cites to the nature of the proxy model as the reason for the complexity of this issue and thus a reason for oral argument on its motion for reconsideration. Staff acknowledges that the proxy model is a complex animal. Staff, however, fails to see any inherent complexity in the loop investment cap issue. Simply stating that the cost proxy model is complex does not adequately support the need for oral argument on the specific issue of loop investment cap. Staff believes that Sprint's Motion and the resulting pleadings from other parties provide sufficient and clear information upon which the Commission can make its decision on the motion for reconsideration. Accordingly, staff recommends that Sprint's request for oral argument be denied.

ISSUE 3: Should Sprint-Florida Incorporated's Motion for Reconsideration of Order No. PSC-99-0068-FOF-TP be granted?

RECOMMENDATION: Yes. Staff recommends that Sprint's Petition for Reconsideration be granted so that the $4,350 loop cost investment cap should only be applied in modeling the cost of service in BellSouth's territory. **(COX)**

STAFF ANALYSIS: The proper standard of review for a motion for reconsideration is whether the motion identifies some point of fact or law which was overlooked or which the Commission failed to consider in rendering its order. See Diamond Cab Co. v. King, 146 So. 2d 889 (Fla. 1962); Pingree v. Quaintance, 394 So. 2d 161 (Fla. 1st DCA 1981).

SPRINT'S MOTION FOR RECONSIDERATION

As indicated in the Case Background, on January 22, 1999, Sprint filed its Motion for Reconsideration. Sprint specifically requested reconsideration of the Commission's decision to adopt the loop investment cap value proposed by BellSouth for all carriers required to use the BCPM 3.1 cost proxy model. BellSouth proposed a cap of $4,350. Sprint contends that the Commission should have adopted the BCPM 3.1 default input value of $10,000. Sprint contends that the issue was not in dispute, and Sprint had no opportunity to present evidence on the matter. Sprint notes that all parties, with the exception of BellSouth, supported the default value. Sprint notes that MCI/AT&T witness Wells testified that the $10,000 default value had been accepted in many proceedings, and that BellSouth provided no explanation or supporting documentation for the $4,350 cap. (Wells TR 2520) Therefore, Sprint believes that the issue was essentially stipulated.

Sprint believes that the Commission misapprehended the nature of the evidence offered in this proceeding on this issue. Sprint claims that the Commission based its decision on testimony from a BellSouth witness pertaining to a survey that presumably gathered information from BellSouth's own territory. Sprint argues that there is no basis to support the notion that the geography of Sprint's service territory is sufficiently similar to BellSouth's service territory. Furthermore, Sprint believes that there is no basis for the Commission's conclusion that BellSouth's cap value is Florida-specific. These points are important when one looks at BellSouth's reasoning for its $4,350 cap value. BellSouth used

this value because its own survey, which was not provided as a part of the record, indicated that $4,350 was a wireless crossover point whereby it would be more cost-effective to deploy wireless technology rather than wireline facilities when the loop investment would exceed this level. Sprint contends that the $4,350 cap is not economically achievable in its territory. In conclusion, Sprint argues that the $4,350 cap value should only be applied to BellSouth and not the other carriers, Sprint and GTEFL.

Finally, Sprint contends that the Commissioners may have been under the false impression that the number of affected lines was minimal for all LECs. Sprint bases this contention on discussion by the Commissioners at the Agenda Conference when the cap value issue was discussed. At one point, the Commissioners were led to believe by staff's revised recommendation on December 17, 1998, that Sprint had 0 lines above the $10,000 default cap value. Sprint's subsequent compliance value indicated 8,987 lines above the $10,000 cap value. More importantly, over 56,000 lines exceeded the $4,350 cap. Sprint provides this information to show the material effect on the company. Sprint believes that the Commission could have been understandably confused about whether the existing $10,000 cap was, in fact, actually capping loop cost investment at all.

JOINT RESPONSE

The Joint Respondents request that the Commission deny Sprint's motion for reconsideration. The Joint Respondents contend that Sprint's motion does not meet the standard of review for reconsideration. The Joint Respondents assert that Sprint fails to bring to the Commission's attention matters overlooked or not considered but simply attempts to reargue issues that were decided differently by the Commission than advocated by Sprint. It is noted that Sprint did not dispute the fact that BellSouth provided record investment of a $4,350 loop cost cap. The Joint Respondents contend that Sprint, not the Commission, therefore misapprehended the evidence and the purpose of this proceeding.

First, the Joint Respondents state that Sprint's motion relies on outside the record discussion about wireless service to contend that the $4,350 per line cap is not an economically achievable alternative for Sprint. This information cannot be considered in the record information that the Commission overlooked. Second, the Joint Respondents contend that it was appropriate for the Commission to rely on witness Caldwell's testimony even though it may not be Florida-specific or Sprint-territory specific. The purpose of this case is modeling and not rate setting; therefore,

for modeling purposes, the BellSouth data/survey is more precise and localized than the national default.

Next, the Joint Respondents disagree about Sprint's contention that some Commissioners may have misapprehended the materiality of the cap value. The Joint Respondents note that the Commission speaks through its orders and not its conversation at agenda. See Section 120.52(7), Florida Statutes. Sprint cannot question how each Commissioner weighed the evidence so long as there is a proper evidentiary basis for the Commission's decision.

Finally, the Joint Respondents argue that the parties in no way stipulated this issue of the loop cost investment cap. No party has accepted or proffered any stipulation on this subject. Sprint's entire argument seems to indicate that an extraordinary evidentiary burden must be overcome in order to deviate from the $10,000 default value. This is simply not the case, as Sprint and every other party must put on witnesses and evidence for issues that are in dispute. Sprint did not put on its case, and its arguments do not meet the requirements for reconsideration.

CONCLUSION

Staff has reviewed the arguments of Sprint and the Joint Respondents. Staff finds several of the arguments of Sprint to be most compelling. Most importantly, staff believes that there was no evidence in the record to support that 1) BellSouth's study was Florida-specific, and 2) the study was reasonably applicable to the territories of any carrier other than BellSouth. Arguably, the BellSouth study results as presented by BellSouth witness Caldwell may be more Florida-specific than the national default values. The record is not completely clear on that issue. However, there is no record evidence to support that the $4,350 cap value is appropriate for modeling the cost of basic local telecommunications service in either Sprint or GTEFL's respective territories/service areas. Staff agrees with Sprint that the evidence can only reasonably support the use of the $4,350 cap for modeling BellSouth's territory. Staff, therefore, recommends that Sprint's Petition for Reconsideration be granted so that the $4,350 loop investment cap should only be applied in modeling the cost of service in BellSouth's territory.

ISSUE 4: Should GTEFL's Petition for Reconsideration of Order No. PSC-99-0068-FOF-TP be granted?

RECOMMENDATION: No. The Commission should deny GTEFL's Petition for Reconsideration of Order No. PSC-99-0068-FOF-TP in its entirety. **(COX)**

STAFF ANALYSIS: The proper standard of review for a motion for reconsideration, as indicated above, is whether the motion identifies some point of fact or law which was overlooked or which the prehearing officer failed to consider in rendering her order. See Diamond Cab Co. v. King, 146 So. 2d 889 (Fla. 1962); Pingree v. Quattlebaum, 394 So. 2d 161 (Fla. 1st DCA 1981).

As indicated in the Case Background, on January 22, 1999, GTEFL filed a Petition for Reconsideration of Order No. PSC-99-0068-FOF-TP. GTEFL seeks reconsideration of the Commission's decisions on cost model inputs for depreciation and cost of capital. GTEFL believes these aspects of the Commission's decision overlooked or failed to consider legal and factual points, such that reconsideration is justified. Staff's recommendation will address the depreciation issues and cost of capital issues separately.

DEPRECIATION

GTEFL

Essentially, GTEFL believes that the Commission's decision on depreciation issues is arbitrary and lacking in evidentiary support. First, GTEFL contends that the decision arbitrarily departs from the depreciation lives GTEFL uses for financial reporting and that this Commission approved in the past. GTEFL argues that the Commission's departure from GTEFL's depreciation lives used for financial purposes and also lives inherent in this Commission's 1992 GTEFL depreciation prescription was impermissibly arbitrary. Further, the Commission overlooked and failed to consider GTEFL's evidence that many of the rates it proposed in this proceeding were the same as those reflected in the 1992 prescription. (EXH 35, pp. 4, 21)

Second, GTEFL argues that the Commission never explains in its Order why devising depreciation inputs for a cost model is different from setting depreciation rates to be factored into retail rates, or what effect this difference had. Further, GTEFL

argues that the Order never discusses any considerations in the proxy model context that might be distinct from those used for the purposes of financial reporting or even depreciation prescription.

Next, GTEFL argues that the Commission's assumption that the FCC prescriptions are forward-looking is arbitrary and simply a supposition. It does not reflect the "considered response to the evidence" that is a fundamental requisite of administrative rulings. It is therefore not a sufficient basis for decision-making.

In addition, GTEFL argues that the Commission's depreciation ruling violates the requirements and intent of the 1995 revisions to Chapter 364, Florida Statutes. In return for opening the local exchange market to competition, the Legislature eliminated depreciation prescriptions and other remnants of rate base regulation for price cap carriers. The Florida Legislature therefore cannot have intended for the Commission to revert to depreciation prescriptions in selected contexts.

Finally, GTEFL argues that the Commission has not adequately justified its depreciation inputs. In comparison to the 1992 prescription, the Commission's decision in this current proceeding is backward-looking. The Commission has offered no basis for ordering depreciation parameters that depart from those the Legislature permits the company to use for financial reporting purposes.

Joint Respondents

The Joint Respondents state that GTEFL seeks reconsideration on the general grounds that the Commission's decisions regarding GTEFL's depreciation lives and cost of capital were arbitrary and without proper evidentiary support. The Joint Respondents contend that GTEFL's petition for reconsideration is mere reargument of the position it took in the hearing in this proceeding.

First, the Joint Respondents note that AT&T/MCI witness Majoros provided testimony to rebut GTEFL's contention that the Commission arbitrarily failed to utilize the depreciation lives GTEFL uses for financial reporting or which the Commission had approved in past proceedings. (TR 87-91; Majoros Rebuttal, pp. 9-13) Second, the Commission's Order in this case specifically discusses the FCC's Universal Service Order and how the FCC's Order lays the "groundwork" for the Commission's actions in this proceeding. Most importantly, GTEFL's Petition demonstrates GTEFL's fundamental misunderstanding of the purpose of this

proceeding -- to follow a specific, one-time 1998 legislative directive to model, on a forward-looking basis, the cost of basic local telecommunications services. (Section 364.025(4)(b), Florida Statutes; Order at p.9) Furthermore, the 1995 revisions to Chapter 364 do not bind the Commission given this later, specific legislative directive.

ANALYSIS

Staff will address each of GTEFL's arguments point by point in the underlying discussion and provide a concluding recommendation on the petition with regard to depreciation.

First, we will address GTEFL's argument regarding the Commission's decision to use depreciation lives other than those used for financial reporting purposes. As discussed in the recommendation and Order No. PSC-99-0068-FOF-TP (Order), AT&T/MCI witness Majoros testified that lives used for financial accounting are governed by Generally Accepted Accounting Principles (GAAP) and the conservatism principle would hold. For example, when alternative expense amounts are acceptable, the alternative having the least favorable effect on net income should be used. (Order, p. 70; Majoros TP 55-56) He also pointed out that GTEFL itself, argued to the FCC in 1993 that conservatism may not always serve the interest of ratepayers. (TR 56-57) The Commission's decision to use depreciation lives other than those used for financial purposes is therefore not impermissibly arbitrary.

Next, we turn to GTEFL's argument regarding the Commission's 1992 depreciation prescription regarding GTEFL. Although not specifically addressed in the recommendation or Order, Exhibit 35 from the hearing in this proceeding shows a comparison of the lives the Commission approved in GTEFL's 1992 prescription and those GTEFL recommended in this proceeding. The comparison addresses only eight of GTEFL's thirty-one accounts. According to GTEFL witness Sovereign, GTEFL addressed only the lives for the eight technology-sensitive accounts because these accounts were considered the most significant. (EXH 20, p. 20)

In its Petition for Reconsideration (Petition), GTEFL fails to point out that its 1992 depreciation prescription was the result of a stipulation (Stipulation) between GTEFL, the Office of Public Counsel, and the Florida Cable Television Association. (EXH 35, pp. 17-21) Further, the Stipulation addresses depreciation rates, not lives and salvage values. (EXH 35, p. 21) Additionally, the Stipulation states: "This Stipulation is based on the unique

factual circumstances of this case and shall have no precedential value in subsequent proceedings." (EXH 35, p. 19)

As pointed out in the Order in this current proceeding, the issue is the appropriate life and salvage parameters to use in a cost proxy model to determine the cost of basic local telecommunications service for establishing a permanent high cost funding mechanism as required by the Legislature. (Order, p. 65) AT&T/MCI's witness Majoros and GTEFL's witness Sovereign both agreed that, for purposes of this proceeding, the same depreciation parameters could be assumed for each of the large LECs. (Order, p. 71) Finally, the Order, pages 71-86, clearly shows the Commission considered the evidence presented by each party in support of its recommended depreciation parameters. (Order, pp. 71-86)

Based on the above, the record is clear that the Commission did not overlook or fail to consider GTEFL's 1992 depreciation rate prescription. The 1992 Stipulation need have no precedential value in this proceeding. The Commission's approved depreciation life and salvage inputs for the cost proxy model are based on the evidence presented by each party. (Order, pp. 65-86)

Furthermore, the depreciation parameters (lives and salvage values) approved in this proceeding are for a universal service provider. As discussed on pages 70 and 71 of the Order, there is record evidence to support the use of the same depreciation parameters for each of the large LECs. Additionally, in determining the reasonableness of each party's depreciation recommendations, the Order is replete with evidence as to why GTEFL's recommendations are not considered appropriate. (Order, pp. 72-81)

Next, we will address GTEFL's criticism of the Commission's use of the FCC's Universal Service Order. The Commission took official recognition at the hearing of the FCC's May 7, 1997, Universal Service Order. The Order discusses the Universal Service Order and how the FCC's requirements can provide insight and general guidance in selecting a forward-looking economic cost model. (Order, p. 21) The FCC's criteria number 5 requires that "economic lives and net salvage percentages used in the model to compute depreciation expense must be within the FCC-authorized range." (Order, p. 22) Therefore, with respect to depreciation parameters used in a cost proxy model for the purpose of determining a high cost funding mechanism, the FCC depreciation ranges can be characterized as "forward-looking."

This Commission's Order also addresses BellSouth's (BST) retirement rates that indicate that reliance on only history would

yield lives for metallic cables similar to those prescribed in the 1970s before the advent of fiber technology. (Order, p. 74) The Order also points out that while similar data was not available from GTEFL or Sprint, there was no reason for the Commission to believe that these companies would not exhibit similar indications. (Order, p. 74)

The issue is which "forward-looking" lives and salvage values are appropriate to use in this proceeding. The recommendation addressed this issue and cited transcript references. The Order, pages 71-86, clearly shows the Commission considered the evidence provided by each company in support of its recommended depreciation parameters. Additionally, page 70 of the Order reflects that GTEFL was unable to clearly indicate how competitive factors should be considered in the determination of lives and salvage values. Although not specifically addressed in the recommendation or Order, witness Sovereign's deposition indicates that the proper weighting of competitive factors was more a matter of GTEFL's reliance on opinions from industry such as a study performed by Technology Futures, Inc. (TFI). (EXH 20, p. 29) As clearly indicated in the Order, the Commission found the results of the substitution model used in the TFI studies not to be reasonable. (Order, pp. 72-75)

Finally, we will address GTEFL's argument that the Commission's depreciation ruling violates Chapter 364, Florida Statutes. Staff believes this argument is irrelevant. The Order is very clear that the purpose of this proceeding is not to prescribe depreciation rates for BST, GTEFL, or Sprint, but rather to determine the reasonableness of the depreciation life and salvage inputs to be included in the cost proxy model for establishing a permanent high cost funding mechanism as required by the Legislature. (Order, p. 70) Furthermore, the record evidence shows that, for purposes of this proceeding, the same set of life and salvage values could be used for each of the large local exchange companies. (Order, p. 71)

CONCLUSION

In summary, GTEFL's argument that the Commission has not adequately justified its depreciation inputs is without merit. As discussed in the recommendation and the Order, GTEFL was unable to clearly indicate how the various sources it used as benchmark comparisons entered into the development of its recommended life and salvage values. (Order, p. 67) Additionally, the Order is replete with discussions regarding the Commission's review and analysis of each party's recommended life and salvage value for each depreciable account. (Order, pp. 72-86)

GTEFL's argument that the Commission's decision in this proceeding is backward-looking compared to GTEFL's 1992 depreciation prescription is unfounded. As discussed above, the 1992 Stipulation was based on unique facts and circumstances and has no precedential value. (EXH 35, p. 21) Similarly, the Commission's decision in this current proceeding is based on a review and analysis of the evidence presented by the parties to address a legislative directive. (Order, pp. 71-86)

According to GTEFL's witness Sovereign, the recommended lives were developed using an industry analysis performed by TFI and professional opinions from GTE and the Regional Bell Operating Companies (RBOCs). (EXH 20, pp. 33-34) The Order clearly addresses the Commission's concerns with the substitution model used in TFI's studies and also addresses why the results were considered not reasonable. (Order, pp. 72-75) Accordingly, based on the above analysis, staff recommends that the Commission deny GTEFL's Petition for Reconsideration with regard to depreciation issues.

COST OF CAPITAL

GTEFL

GTEFL also seeks reconsideration on cost of capital issues. GTEFL argues that the capital structure ruling must be reconsidered because it overlooks GTEFL's evidence in favor of information outside the record of this proceeding and draws conclusions that are not justified by the evidence the Commission cited in its Order.

First, GTEFL contends that the Commission cannot rely on mostly unnamed orders from other states while ignoring information in its own record. Second, GTEFL argues that the Commission supported its rejection of GTEFL's proposed capital structure based on a source outside of the record in this proceeding. Third, because AT&T/MCI witness Hirshleifer's analysis is not grounded in the "statutory directive," the Commission's reliance upon his testimony and conclusions is ill-founded. Fourth, the Commission's cost of capital analysis overlooks or misconstrues risk evidence. Because witness Hirshleifer's testimony did not pertain to local service, the Commission's conclusions based on that evidence are unjustified. Moreover, the Commission apparently overlooked GTEFL's Florida-specific evidence of risk. Finally, the Commission's decision was skewed by its misapprehension of and failure to consider key points of fact.

Joint Respondents

The Joint Respondents state that GTEFL's primary argument with regard to the Commission's decision on cost of capital is that the decision lacks evidentiary support. The Joint Respondents note that the Commission specifically relied upon the testimony of AT&T/MCI witness Hirshleifer in rejecting GTEFL's cost of capital proposals. (TR 152-203, 209-250; Hirshleifer Direct, pp.5-56, Rebuttal pp. 2-42) The Joint Respondents stress that, on the question of business risk, GTEFL's own petition for reconsideration makes clear that GTEFL's complaint with the Order is the weight and interpretation given to the GTEFL testimony. The Commission clearly weighed the evidence and rejected GTEFL witness Vander Weide's testimony in favor of the testimony of AT&T/MCI witness Hirshleifer, which is the Commission's prerogative. Gulf Power Co. v. FPSC, 453 So.2d 799 (Fla. 1984); United Telephone Co. v. Mayo, 345 So.2d 648 (Fla. 1977). In conclusion, GTEFL's petition is

that the Commission based its decision upon competent, substantial evidence in the record, i.e., the testimonies of witnesses Billingsley and Hirshleifer, not the fact that all the other state regulatory commissions witness Vander Weide appeared before on behalf of GTE also rejected his recommended capital structure.

GTEFL alleges that the Commission supported its rejection of GTEFL's proposed capital structure based on information not in the record of this proceeding. GTEFL's allegation is incorrect on two counts. First, the Duff & Phelps Credit Rating Company press release cited by GTEFL in its petition is in the record. This document was provided by GTEFL in response to a staff discovery request and was entered into the record as part of Exhibit 35. (EXH 35, p. 393) It is puzzling why GTEFL would now argue, as it does on page 10 of its petition, that it doesn't know what the press release says. But more importantly, as previously mentioned, the Commission based its capital structure decision on competent, substantial evidence in the record. The reference to the Duff & Phelps press release and how GTE planned to finance the failed acquisition of MCI was only provided to illustrate what the document says on its face.

Next, staff believes that GTEFL's argument regarding the Commission's failure to follow the statutory directive is without merit. Staff notes that this is a proceeding to select a cost proxy model that estimates the total forward-looking cost of providing basic local telecommunications service in Florida. The ultimate purpose of selecting such a model is to assist the Legislature in establishing a permanent universal service fund that will preserve and advance universal service, as required by Section 254 of the Telecommunications Act of 1996 ("Act") and Section 364.025, Florida Statutes. On page 1 of its Post-hearing Statement and Brief, GTEFL appears to recognize that the purpose of this proceeding is to determine and report to the Legislature the cost of basic local telecommunications service appropriate for establishing a permanent universal service mechanism and that the Commission's selection of a cost model should be predicated on this underlying purpose. (GTEFL Br 1)

Apparently, GTEFL has become so fixated on the references made in witness Hirshleifer's testimony regarding the business of leasing local exchange telephone network elements that it has completely overlooked the fact that his testimony also discusses at length the business of providing universal service. (TR 196-197, 246-247) In its Order, the Commission clearly states that it relied upon AT&T/MCI witness Hirshleifer's testimony regarding the provision of universal service, which GTEFL accurately points out

simply reargument, and reconsideration therefore is improper and should be denied.

ANALYSIS

Staff will address each of GTEFL's arguments point by point in the underlying discussion and provide a concluding recommendation on the petition with regard to the cost of capital issues.

GTEFL's claim that the Commission's capital structure decision lacks evidentiary support is unfounded. The Commission's decision to adopt a capital structure of 60% equity and 40% debt is clearly supported by the record. Appearing on behalf of Sprint, witness Billingsley relied upon a capital structure of 59.6% equity and 40.4% debt to estimate Sprint's weighted average cost of capital. (EXH 39, p. 546) Appearing on behalf of BST, witness Billingsley relied upon a capital structure of 60% equity and 40% debt to estimate BST's weighted average cost of capital. (EXH 30, p. 599) Finally, witness Hirshleifer, appearing on behalf of AT&T/MCI, relied upon an average capital structure of 61.5% equity and 38.5% debt for estimating the weighted average cost of capital for BST, Sprint, and GTEFL. (TR 192-195) Therefore, contrary to GTEFL's claim, the Commission's capital structure ruling is supported by competent, substantial evidence in the record.

As noted above, the Commission clearly relied upon evidence in the record in rendering its capital structure decision. The reference to orders from other state regulatory commissions was made as a point of comparison, not as a basis for the decision as GTEFL alleges. It is well within the Commission's prerogative to consider decisions regarding similar issues rendered in other jurisdictions. The Order referenced only the Hawaii and Alaska decisions by name because these decisions represented the range of equity ratios approved for GTE-affiliated companies in other states since the passage of the Telecommunications Act of 1996. In response to a staff discovery request for copies of all state commission orders issued since January 1, 1996, involving the GTE parent company (GTOC) or any of its affiliated companies in which cost of capital was decided, GTEFL provided 8 orders. These orders were entered into the record as part of Exhibit 14. In response to a staff discovery request regarding every state in which witness Vander Weide testified on behalf of GTE since January 1, 1996, GTEFL responded that he appeared on behalf of GTE in 13 states. (EXH 35, pp. 12-14) The case involving Massachusetts cited by GTEFL in its petition was not referenced in either response and therefore was never made available for consideration. It is evidence that is not in the record. However, the primary point is

in its brief is the "underlying purpose" of this proceeding. Moreover, GTEFL witness Vander Weide admitted that, in the context of a study to look into the possibility of a universal service fund, many people would use universal service and basic local telecommunications service as synonyms. (EXH 21, p. 9)

Next, GTEFL argues that the Commission misconstrued the risk evidence. It is GTEFL, not the Commission, that has misconstrued the risk evidence in the record. As noted in the Order and as GTEFL readily admits in its petition, the financial markets continuously absorb and incorporate information about competition and technological and regulatory change. Witness Hirshleifer testified that, when assessing the cost of capital of any publicly-traded company, the market accounts for all known risks existing currently and the possibility of risks that could develop or increase in the future. He further noted that the market continuously evaluates real-world information regarding all relevant risks, including those which may arise or increase in the future, and incorporates the likelihood of those risks occurring into the current costs of capital of the telephone holding companies. (TR 238; EXH 16, pp. 39-40, 71) Witness Vander Weide acknowledged that investors consider all risks, including industry changes, that a firm might incur over the future life of the company. (TR 263-264) Each of the witnesses in this proceeding relied upon market information in the analyses supporting their respective cost of capital recommendations. By relying upon the testimonies of witnesses Vander Weide, Billingsley, and Hirshleifer in rendering its cost of capital decision, the Commission has considered the relevant risk evidence in the record.

Similarly, GTEFL's claim that the Commission overlooked GTEFL's specific evidence of risk is unfounded. In its Order, the Commission states that to the extent the discussion of risk in witnesses Billingsley's and Vander Weide's testimonies addressed the global state of the telecommunications industry rather than the actual business of providing universal service in Florida, it was irrelevant to the determination of the cost of capital in this proceeding. This conclusion is supported by evidence in the record. (Hirshleifer TR 196-199; EXH 16, pp. 57-58) The Order goes on to state that, to the extent the market considers the risks referred to by witnesses Billingsley and Vander Weide relevant to the provision of basic local service, it has been accounted for in the financial measures used by the witnesses to estimate the cost of capital of these companies. This conclusion is also supported by evidence in the record. (Hirshleifer TR 238; EXH 16, pp. 39-40, 71) Simply because the Commission adopted a cost of capital figure different from what GTEFL recommended does not mean the Commission

did not consider GTEFL's Florida-specific evidence of risk as GTEFL alleges in its petition.

Continuing its familiar tune, GTEFL claims that certain aspects of witness Hirshleifer's DCF analysis are arbitrary and depart from market considerations and therefore, there is no basis for the Commission's reliance on his testimony. Clearly, the Commission simply disagreed with GTEFL's opinion on this point. Witness Hirshleifer testified that the form of the DCF model he used is well supported in the financial community. (TR 167-171) In addition, witness Hirshleifer testified that it was witness Vander Weide's analysis that was arbitrary and departed from market considerations because he did not demonstrate how his index of companies from such diverse industries as automobile manufacturers, oil companies, producers of food and food ingredients, publishing and entertainment companies, and pharmaceutical companies was comparable in risk to GTEFL. Witness Hirshleifer concluded that because witness Vander Weide's analysis was based upon the performance of large industrial companies rather than a group of comparable companies, his results were of no relevance to the business of providing universal service. (TR 244-246) The Commission's decision in this proceeding was not "skewed by its misapprehension of and failure to consider key points of fact" as GTEFL alleges, but rather was based upon evidence in the record with which GTEFL simply disagrees.

Finally, GTEFL incorrectly alleges in its petition that witness Vander Weide's testimony regarding the appropriate capital structure for calculating a firm's weighted cost of capital was not rebutted in this proceeding. Not only did witness Hirshleifer directly rebut witness Vander Weide's testimony, but as mentioned earlier, witness Vander Weide's testimony was de facto rebutted by the fact that no other state commission has accepted his recommended capital structure for purposes of determining the weighted average cost of capital in this type of proceeding. (TR 246-247; EXH 14)

Conclusion

In considering the evidence in the record when rendering its decision regarding the appropriate capital structure and overall weighted cost of capital for purposes of this proceeding, the Commission evaluated and weighed the evidence and testimonies provided by witnesses Vander Weide, Billingsley, and Hirshleifer. Such an evaluation is clearly the Commission's prerogative. After a careful review of the record in this case, it is clear the Commission did not rely upon information outside the record, draw

unwarranted conclusions from information in the record, or misapprehend evidence in the record, as alleged by GTEFL. Moreover, GTEFL's petition did not identify any points of fact or law which were overlooked or not considered by the Commission. GTEFL's arguments regarding the Commission's capital structure and cost of capital decisions are simply reargument of issues that were decided differently by the Commission than were advocated by GTEFL. For these reasons, GTEFL has not provided an appropriate basis for reconsideration of these issues.

ISSUE 5: Should this docket be closed?

RECOMMENDATION: Yes, this docket should be closed upon issuance of the Commission's Order on this recommendation. **(COX)**

STAFF ANALYSIS: Whether the Commission approves or denies staff's recommendations, this docket should be closed upon issuance of the Commission's Order on the recommendation.