SUPREME COURT OF FLORIDA

VERIZON FLORIDA, INC., Appellant, v. LILA A. JABER, ET AL. Appellees.	)	CASE NO. SC02-2647

ANSWER BRIEF OF FLORIDA PUBLIC SERVICE COMMISSION

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SYMBOLS AND DESIGNATION OF THE PARTIES

Appellee, the Florida Public Service Commission, is referred to in this Answer Brief as the "Commission." Appellant, Verizon Florida, Inc., is referred to as "Verizon." References to Verizon's Initial Brief are designated "Brief at __."

References to the Record on Appeal are designated R. [Vol.: P.], e. g., R. 16: 2802; the Transcripts of the April 29-30, 2002, administrative hearing in the case are designated TR.: [Vol.: P.], e. g., TR. 3: 375. The Transcript of the Special Agenda Conference held October 14, 2002 is designated TRA.: [P]., e. g., TRA.: 34. Exhibits entered into the record at hearing are designated Exh.: [No.: P.], e. g., Exh. 5:43.

Unbundled Network Elements as that term is used in the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (Codified at various sections of 47 U. S. C. §152 et seq.), 47 U. S. C §§251-252, are referred to as "UNEs." The Federal Communications Commission is referred to as the "FCC", and that agency's UNE pricing methodology, the so-called "Total Element Long Run Incremental Cost" methodology is referred to as "TELRIC." The Commission's final order in this proceeding, Order No. PSC-02-1574-FOF-TP, issued November 15, 2002, in Docket No. 990649B, *In re: Investigation into pricing of unbundled network elements (Sprint/Verizon track*), is referred to as the "UNE Order." The Commission's order

in the BellSouth Telecommunications, Inc. phase of the UNE proceedings, Docket No. 990649A, Order No. PSC-01-1181-FOF-TP, is referred to as the "BellSouth Order."

Incumbent local exchange companies like Verizon are referred to as "ILECs"; competitor companies like MCI and AT&T are referred to as alternative local exchange companies or "ALECs".

STATEMENT OF THE CASE

The Commission accepts Verizon's Statement of the Case so far as it sets out parts of the procedural history of the case. On the other hand, the Commission rejects those statements on page 3 of Verizon's Brief that outline its argument on appeal. In addition, the Commission offers additional relevant procedural history as follows.

This case has a long and involved procedural history. It began on December 10, 1998, when a group of ALECs filed a petition with the Commission styled "Petition of Competitive Carriers for Commission Action to Support Local Competition in BellSouth's Service Territory." The petition requested several forms of relief, primarily that the Commission order BellSouth to conduct third party testing of its Operations Support Systems (OSS)[1] and that it conduct a generic UNE pricing proceeding for BellSouth. Order No. PSC-99-1078-PCO-TP, 99 F.P.S.C. 5:417 (1999). More specifically, the Competitive Carriers, as the ALEC groups were collectively called, asked that the Commission "determine cost-based pricing for UNE combinations, unbundled switching costs, non-recurring costs, and geographically deaveraged pricing for local loops." *Id*. at 417. This was necessary, they claimed, "to

[1]OSS constitutes the various data bases and other functions which provide information and access for such things as ordering and establishing service, etc. The Commission ordered third-party testing, but that matter is not directly relevant to the UNE pricing issues raised in this appeal.

allow all competitive carriers and BellSouth the opportunity to address issues that are critical to all parties' survival in the marketplace." *Id*. Such a proceeding would be designed to "dispel uncertainty and correct pricing problems in order to encourage investment by competitive carriers in the Florida local market." *Id*.

The Commission agreed to the Competitive Carriers' request for a generic UNE proceeding. It found that the time was right for such a proceeding for a variety of reasons: the Supreme Court had recently ruled in *AT&T Corp. v. Iowa Utilities Board*, 525 U. S. 336 (1999) that the FCC had jurisdiction over pricing issues and reinstated rules relating to UNE pricing and deaveraging; there had been little cooperation and agreement on pricing issues in the negotiation and arbitration of interconnection agreements between ILECs and ALECs; and a formal administrative hearing in which all affected parties were able to participate would provide the proper forum for setting UNE rates. *Id*. at 420-421.

The UNE proceeding was initiated as Docket No. 990649-TP, *In re: Investigation into Pricing of Unbundled Network Elements.* Order No. PSC-00-1486-PCO, 00 F. P. S. C. 8:166 (2000). A procedural schedule was developed which would require the three major Florida ILECs, BellSouth, Verizon (then GTE Florida, Inc.) and Sprint-Florida, Inc. ("Sprint") to file cost studies based on the FCC's

TELRIC methodology in support of their proposed UNE rates. Other parties were to file testimony on dates specified. The order also established hearing dates. *Id*.

The Commission's original schedule for the generic UNE pricing docket contemplated that all three ILECs would participate in the same hearing, and a hearing on certain issues common to all was held on July 17, 2000. However, in August, 2000, after various concerns had arisen about BellSouth's cost studies and the Eighth Circuit Court of Appeals on remand had invalidated the FCC's TELRIC methodology, Verizon filed a motion to bifurcate the proceedings and withdraw its cost studies and testimony. *Id*. Verizon sought the bifurcation out of concern that its TELRIC-compliant cost studies might not comport with the pricing methodology the FCC ultimately adopted necessitating revision of the cost studies. Sprint filed a similar motion. *Id*. at 167-169. The Commission granted Verizon's and Sprint's motions to bifurcate. *Id*. at 172-173. It later established Docket No. 990649B to accommodate the companies' separate UNE proceedings. Order No. PSC-01-2131-PCO-TP, issued October 29, 2001.

The BellSouth proceeding moved forward to a hearing held September 19-21, and October 20, 2000. Order No. PSC-01-1181-FOF-TP, 1 F. P. S. C. 5:377, 393-394 (2001). The final order in the BellSouth proceeding was issued May 25, 2001.

Id. at 377. The Commission, however, required BellSouth to resubmit certain cost studies and the matter was not finally resolved until the issuance of Order No. PSC-02-1311-FOF-TP, 02 F.P.S.C. 9:685, on September 27, 2001. A final motion for reconsideration was disposed of on December 9, 2001. Before the issuance of the reconsideration order, on November 19, 2002, MCI WorldCom Communications, Inc. ("WorldCom") proceeded to file a complaint in the U. S. District Court for the Northern District of Florida initiating appellate-style review of the BellSouth UNE Order under the judicial review provisions of the Telecom Act, 47 U. S. C. §252(e)(6). That case remains pending in the Northern District as Case No. 4:01cv492-SPM, *MCI WorldCom Communications, Inc. v. BellSouth Telecommunications, Inc.* MCI also filed a "placeholder" appeal of the BellSouth UNE Order in this Court on November 27, 2001. Proceedings in that appeal, No. SC01-2576, *MCI WorldCom, Inc. v. Jacobs*, have been stayed by this Court pending disposition of the federal appeal. Order issued February 13, 2002.

After various delays occasioned by requests of the parties for continuances and extensions of time, the Commission established the controlling dates for the Verizon/Sprint hearing and set out the issues to be heard. Order No. PSC-01-1592-PCO-TP, 01 F.P.S.C. 8:12. A final prehearing conference took place on April 19, 2002, and Prehearing Order No. PSC-02-0568-PCO-TP, 02 F.P.S.C. 4:348,

controlling the conduct of the hearing was issued April 25, 2002. The evidentiary hearing took place on April 29-30, 2002. Parties participating were Verizon; Sprint; the "ALEC Coalition" consisting of WorldCom; AT&T Communications of the Southern States, Inc. ("AT&T"); and Florida Digital Network ("FDN"); Covad Communications Company; Z-Tel Communications; KMC Telecom III, LLC.; Florida Cable Telecommunications Association, Inc. and Commission staff.

Post hearing briefs advocating the parties' positions on the issues were filed May 28, 2002, R.7-8:1242-1651. The Commission staff submitted its recommendation for disposition of the case on September 25, 2002, and the matter was considered by the Commission at a Special Agenda Conference held October 14, 2002, R.10-13:1754-2201; 15:2643-2774. The Final Order on Rates for Unbundled Network Elements Provided by Verizon Florida (UNE Order) on November 15, 2002. 02 F.P.S.C. 11:129 (2002); R15-17:2775-3137.

After the Commission issued its November 15, 2002, UNE Order for Verizon, parties AT&T Communications of the Southern States, Inc. (AT&T) and MCI WorldCom, Inc. (WorldCom) filed motions for reconsideration on December 2, 2002. Verizon filed a motion for stay of the UNE Order with the Commission on December 16, 2002 as well as its Notice of Appeal to this Court. The Commission heard

argument on the motion for stay on April 9, 2003. The motion was granted but an order has not yet issued.

On January 8, 2003, the Commission moved to abate the appeal on the grounds that it was premature considering the pending motion for reconsideration of the UNE Order filed by AT&T and WorldCom. The Court granted that motion by its Order of March 3, 2003.

On May 3, 2003, AT&T and WorldCom withdrew their Motion for Reconsideration of the UNE Order. Thereafter, on June 10, 2003, Verizon proceeded to file its Initial Brief, notwithstanding that it had asked the Court to establish a briefing schedule which had the Initial Brief due July 1, 2003. The Court granted the latter request on June 11, 2003.

On June 13, 2003, Appellee AT&T filed a motion for extension of time to file its answer brief. That motion was denied on July 24, 2003. The Commission had also filed a motion to toll time to file its answer brief which was granted on July 9, 2003.

STATEMENT OF THE FACTS

The Commission accepts Verizon's Statement of the Facts to the extent facts are presented, but rejects as improper argument statements in Verizon's Brief at page 5. There Verizon again argues its case, referring to its claims of error in the Commission's UNE Order. The Commission offers the following additional facts as

concerning implementation of the Telecom Act and its role as set out in the UNE Order:

> The Federal Telecommunications Act of 1996 (Act) made sweeping changes to the regulation of telecommunications common carriers in this country. Of particular importance, it provided for the abolition nationwide of the incumbent local exchange carriers' monopolies over the provision of local exchange service. The Act envisioned three strategies for firms to enter the local exchange services market: (1) through resale of the incumbent's services; (2) via pure facilities-based offerings, thus only requiring a competitor to interconnect with the incumbent's network; and (3) through a hybrid involving the leasing of unbundled network elements (UNEs) of the incumbent's network facilities, typically in conjunction with network facilities owned by the entrant.
>
> Although the Act generally spelled out the broad policy terms, the implementation details were left to the Federal Communications Commission (FCC). Specifically, the Act required that the FCC promulgate rules to implement the resale, interconnection, and UNE requirements within six months after passage of the Act. The rules subsequently established by the FCC provided detailed implementation requirements for pricing and provision of UNEs and services. Of importance to this docket, the FCC's Local Competition Order, released August 8, 1996, included in its pricing rules Rule 51.507(f), which requires each state commission to establish rate zones for UNEs, the deaveraging rule. That rule states:
>
> > State commissions shall establish different rates for elements in at least three defined geographic areas within the state to reflect geographic cost differences.
>
> Since their establishment, these pricing rules have been the subject of a number of court decisions and FCC actions, which have directly impacted this issue and its resolution.

. . . Sections 252(d)(1)(A) and (B) of the Telecommunications Act of 1996 (the Act) . . . states that network element rates

> (A) shall be - -
>
> (i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable), and
>
> (ii) nondiscriminatory, and
>
> (B) may include a reasonable profit.
>
> The appropriate methodology as determined by the FCC is set forth in 47 C.F.R. §51.505(b). Section 51.505(b) defines TELRIC as
>
> > . . . the forward-looking cost over the long run of the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such element, calculated taking as a given the incumbent LEC's provision of other elements.
> >
> > (1) . . . The total element long-run incremental cost of an element should be measured based on the use of the most efficient telecommunications technology currently available and the lowest cost network configuration, given the existing location of the incumbent LEC's wire centers.
>
> Section 51.505(b) further provides that a forward-looking cost of capital and economic depreciation rates must be used. Section 51.505(a)(2) provides that the forward-looking cost of a UNE should include "a reasonable allocation of forward-looking common costs. . . . "

UNE Order at 12-14; R. 2786-2788.

Such other facts as my be relevant to the matters addressed are set forth in the body of the Commission's argument.

SUMMARY OF THE ARGUMENT

The Commission's calculation of Verizon's forward-looking cost of capital is supported by competent substantial evidence and comports with the essential requirements of law. Cost of capital witnesses presented expert testimony supporting a wide range of cost of capital for Verizon's UNE rates. The Commission acted within its discretion to accept a 9.63% overall cost of capital based on the 11.24% cost of equity and 7.22% cost of debt calculated by staff witness Draper.

Verizon has gone to great lengths to exploit the minor confusion about the exclusion of SBC Telecommunications, Inc. from Mr. Draper's index of comparable companies, but minor confusion is all it has shown. There is no demonstrable "admission" of error by Mr. Draper nor any reliance by the Commission on non-evidentiary statements by Commission staff in making its recommendations. The Commission was well informed of the bases for Mr. Draper's calculation, including his use of AT&T Corporation and CenturyTel, Inc. in his proxy group of companies. The Commission exercised its proper role as the expert agency charged with evaluating the evidence before it. It was entitled to give the competing testimony of the experts whatever weight it saw fit. It would be improper for this Court to reevaluate the evidence based on the forced claims of irregularity in the decision-making process advanced by Verizon.

Verizon failed to provide adequate proof to show that the depreciation lives and salvage values proposed by its witness were appropriate for setting UNE rates. Verizon provided only scant support for some of the economic lives it was proposing and asked the Commission to simply adopt its financial reporting values. The Commission likewise did not have confidence in the ALEC Coalition's proposed use of the FCC's depreciation rates as a proxy. In this case the Commission did what it is charged with as the expert agency having responsibility to set competitive UNE rates. It chose the values in which it had confidence, i. e., those previously set for BellSouth Telecommunications, Inc. in the consolidated proceedings. Use of the BellSouth rates avoided a failure in the UNE rate setting process and provided a reasonable proxy, one by no means entirely unfavorable to Verizon's position. The Commission's depreciation decision was within its discretion and supported by the record.

The Commission was entitled to rely on the analysis of its staff in evaluating and testing Verizon's proposed loading factors for materials and engineering. It properly recognized the distortions that the linearity apparent in Verizon's loading factors would cause based on its experience with setting BellSouth's UNE rates. The problem with which it had to deal was again a lack of credible evidence. It was not bound to accept whatever Verizon offered. The loading factors it adopted took account of the

differences between BellSouth and Verizon. Its decision to move forward rather than initiate a second round of proceedings on the subject was based on sound reasoning favoring an immediate decision on Verizon's UNE rates and was a proper exercise of authority within its recognized range of discretion.

The Commission properly excluded Verizon's post-recommendation argument from the record. No rule or Commission policy gave Verizon the right to write a letter to the Executive Director addressing the staff recommendation before the Commission's decision, and the law is clear that it is the Commission's prerogative to decide when it will cut off post-hearing submissions.

Verizon's claims of error based on the assertions in its letter are speculation and untested assertions about what the Commission staff did or may have done. It would be improper for the Court to accept them as a valid claims undermining the Commission's UNE Order. Verizon essentially asks this Court to grant the reconsideration it forwent in rushing to bring this appeal. In the end, the Commission was faced with having to go with the best evidence before it at the time of decision, that provided by Verizon itself.

The Commission asks that this Court affirm its UNE Order in all respects.

STANDARD OF REVIEW

As this Court has said many times, orders of the Commission come to this court "clothed with the statutory presumption that they have been made within the commission's jurisdiction and powers, and that they are reasonable and just and such as ought to have been made." *Gulf Coast Electric Cooperative v. Johnson*, 727 So. 2d 259, 262 (Fla. 1999)(citations omitted). The Commission's interpretations of its statutes are entitled to great weight and a party challenging an order bears the burden of overcoming the presumption of validity by showing a departure from the essential requirements of law. Id. [citing *AmeriSteel Corp. v. Clark*, 691 So. 2d 473 (Fla. 1997)]. The Commission's findings will be upheld if they are based on competent substantial evidence and are not clearly erroneous. *Id.* The deference afforded the Commission's orders is appropriate given the agency's special expertise in the area of utility regulation. Id. [citing *Gulf Oil v. Bevis*, 322 So. 2d 30, 32 (Fla. 1975); *Public Service Commission v. Fuller*, 551 So. 2d 1210, 1212 (Fla. 1989)].

ARGUMENT

I. THE COMMISSION'S COST OF CAPITAL CALCULATION IS SUPPORTED BY COMPETENT SUBSTANTIAL EVIDENCE.

A. The Commission's cost of capital calculation was a proper exercise of its discretion based on expert testimony of record.

In its UNE Order the Commission relied on the testimony of staff witness David Draper to establish the cost of capital component of UNE rates. The results obtained by Mr. Draper were a 11.24% cost of equity and a debt cost rate of 7.22%. This translated into an overall forward-looking cost of capital of 9.63%. UNE Order at 78; R. 16: 2852. That result is well within the range recommended by three other testifying experts. Verizon's own witness, Dr. Vander Weide, recommended an overall cost of capital of 12.95% with a cost of equity at 14.75% and a cost of debt of 7.55%. Z-Tel witness Dr. Ford calculated cost of equity of approximately 10.0% to 10.1% and a cost of debt at between 6.10% and 6.25%. R. 16: 2862. ALEC Coalition witness, Dr. Ankum, did not provide specific calculations of equity and debt, but recommended that the cost of capital range be no lower than the 8.8% rate approved for Verizon in New Jersey and no higher than the 10.24% approved for BellSouth in its phase of the Commission proceedings. TR. 8: 1251 - 1253; R. 16: 2862.

Against this constellation of cost of capital rates from which the Commission had to choose, Verizon now invites the Court to focus on one single alleged error of

staff witness Draper in his selection of proxy telecommunications companies used in his cost of equity calculation. To make his case, Verizon must lead the Court away from the mass of evidence considered by the Commission and direct its attention to exchanges between the staff and the Commission at the special agenda conference when a vote on the staff recommendation in the case was taken. Contrary to Verizon's assertions, nothing that occurred at the agenda conference indicates that the Commission "relied upon the unsworn speculation" of its staff in accepting Mr. Draper's cost of capital calculation. Brief at 10. Verizon's claims are overstated and unsupported by the law.

This Court has said many times that it is "the prerogative of the PSC to evaluate the testimony of competing experts and accord whatever weight to the conflicting opinions it deems necessary". *Gulf Power Co. v. Florida Public Service Commission*, 453 So. 2d 799, 805 (Fla. 1984). Even when the Commission is confronted with testimony so at odds that neither alternative presented by the experts is acceptable it is not precluded by "statute and common sense" from reaching a decision consistent with its regulatory duties. *Id*.

This is a classic case in which the Commission's prerogative to evaluate competing testimony should be recognized. Collectively, the four witnesses presented hundreds of pages of testimony and exhibits detailing the methodology used for

calculating the cost of equity and debt and data supporting those calculations. Mr. Draper, whose job as a staff witness it was to provide the Commission with an unbiased analysis, was somewhere in the middle of the ranges advocated by the other cost of capital experts. Even if witness Draper had not testified, the Commission would have been within its discretion to have chosen a cost of capital somewhere in the range presented by the competing experts of Verizon, Z-Tel and the ALEC Coalition. It was certainly within the Commission's prerogative to also give whatever weight it chose to witness Draper's testimony with or without the omission of SBC from his proxy group, and that is precisely what it did.

This Court has recognized that the determination of the utility's cost of capital and is a function uniquely within the discretion of the Commission. As this Court noted in *Gulf Power Co. v. Wilson*, 597 So. 2d 270, 273 (Fla. 1992):

> What constitutes a fair rate of return for a utility depends upon the facts and circumstances of each utility, and this Court has expressly recognized that the Commission must be allowed broad discretion in setting a utility's appropriate rate of return. *United Tel. Co. v. Mayo,* 345 So. 2d 648 (Fla. 1977).

The discretion afforded the Commission in determining a utility's return on equity is inherent in the nature of the determination. Cost of equity presents not merely an issue of fact but of policy. The proposition was well stated in *Utilities, Inc. of Florida v. Florida Public Service Commission*, 420 So. 2d 331, 333 (Fla. 1st DCA

1982) where the Court reflected on the nature of the Commission's determination of the cost of equity capital. There the Court said:

> . . . the fair and proper rate of return on equity capital for a utility . . . was not one susceptible to ordinary methods of proof; instead it was essentially a matter of opinion which necessarily had to be infused by policy considerations for which the PSC has special responsibility. There was no question of either qualification or credibility per se of the expert witnesses. Rather, an analysis of the methods by, and the basis upon, which the experts had reached their respective opinions, was required to be made, a matter particularly within the range of the agency's putative expertise and specialized experience.

The fact that this proceeding involved the setting of UNE rates under the guidelines of the Federal Telecom Act is of no consequence for the underlying principles of agency discretion. Indeed, the Supreme Court in *Verizon Communications, Inc. v. FCC*, 122 S.Ct. 1646, 1676-1677 (2002), noted that the FCC's TELRIC methodology which the Commission was bound to follow in this case "prescribes no fixed percentage rate as risk-adjusted capital cost" and that the "FCC committed considerable discretion to state commissions" in determining what the cost of capital for UNE pricing should be. (*See also*, *Implementation of the Local Competition Provisions in the Telecomm. Act of 1996, First Report and Order*, 11 FCC Rcd 15499 (1996), ¶702).

1. The Commission properly relied on the testimony of witness Draper.

Against this background, Verizon has a heavy burden to demonstrate that the alleged error of which it complains is sufficient to warrant reversal of the Commission's decision on UNE cost of capital. Its arguments directed to witness Draper's testimony fail utterly for a number of reasons.

First, it must be noted that the Commission was well aware of the effect of witness Draper's omission of SBC from his proxy group. Witness Vander Weide in fact recalculated cost of capital using Mr. Draper's methodology with SBC included. Exh. 41. Staff member Mr. Lester, who Verizon's alleges "corrected" Mr. Draper's "mistake," passed out Mr. Vander Weide's exhibit at the special agenda conference for the specific purpose of showing the Commission what the effect of including SBC would be. TRA 69; R. 15: 2711.

The Commission did not chose to accept Dr. Vander Weide's revised version of Mr. Draper's calculation. At a minimum this shows that the Commission knew exactly what it is was doing when it voted for Mr. Draper's original cost of capital without SBC and that it was not inclined to accept the higher rate that resulted from the recalculation. It also suggests that as far as the Commission was concerned the inclusion of SBC in the index was not critical to its validity.

Second, the deposition testimony cited by Verizon for Mr. Draper's "significant mistake in his cost of capital computation" does not amount to an admission of error.

Nor is it correct that the only reason Mr. Draper excluded SBC was his belief that the company receives less than 75% of its revenues from telecommunications operations. Even Verizon notes that Mr. Draper in his deposition agreed with the attorney's assertion that SBC receives more than 75% of its revenues from telecommunications "subject to check". A logical conclusion would be that this was at best a conditional acknowledgment of a fact, not a definitive "admission."[2] One could further conclude that it is just as likely as not that Mr. Draper did in fact check and maintain his position that SBC was properly excluded from his proxy list. In any case, since all testimony was stipulated into the record and no cross examination was conducted at which the matter could have been clarified, Verizon's claim of a clear and unrebutted error on Mr. Draper's part is vastly overstated.

Mr. Draper never "admitted" that SBC received over 75% of its revenues from telecommunications as Verizon argues. Moreover, Verizon's claim that Mr. Draper never consulted the C. A. Turner Utility Reports in determining the SBC's revenues from telecommunications appears to be another unfounded and illogical assumption. In reference to questions about the capital structure that went into his weighted cost of capital, Mr. Draper did in fact say he consulted C. A. Turner Utility reports as well

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[2] *See*, TRA 73; 74-75; R. 2715-2727. Chairman Jaber and Commissioner Baez recognized that Mr. Draper had not "admitted" anything in stating he accepted the questioner's position "subject to check."

as Value Line. Exh. 37: 26-27. Indeed, his own index of companies footnotes C. A. Turner Utility Reports "Financial Statistics of Public Utilities, 2001" as a source of information for the companies chosen Exh. 6 (DJD-1). Thus, in the absence of further inquiry which was foreclosed at hearing by the fact of the stipulated testimony and depositions, it seems just as likely that Mr. Draper did in fact consult the document referred to by Mr. Lester and came to the same conclusion that Mr. Lester did. In any case, Verizon's claim that the C. A. Turner Utility Reports "was never relied upon by Mr. Draper when developing his proxy group of telecommunications companies" (Brief at 13) is again an overstatement based on conjecture. The statement from his deposition relied on by Verizon for this proposition again is at least ambiguous. At page 57 of his deposition referred to in Verizon's Brief footnote 27, p. 14, Mr. Draper was asked:

> Q. Did you rely exclusively on Value Line to determine which companies would be included in your index of telecommunications companies?
>
> A. For my analysis, yes.

Exh. 37: 57.

It appears that Mr. Draper was not responding to the question exactly as asked. Since he refers to "my analysis" one could logically assume, contrary to Verizon's assertions, that Value Line was used for the statistics necessary for his analysis but not

necessarily for the selection of the companies in the index. There is no reason to conclude that this means that he never consulted the C. A. Turner Utility Reports as Verizon would have the Court believe.

The bottom line on this point is that even if everything that Verizon says about SBC is true, it would still not prove that the omission of SBC from Mr. Draper's telecommunications index would force an unreasonable result. His recommended 11.24% return on equity was within the range of the 10.0-10.1% suggested by Dr. Ford and the 14.75% proposed by Dr. Vander Weide. Being fully informed on the subject, it was the Commission's call to give the testimony the weight it found appropriate, and its decision cannot be faulted for not having chosen the higher rate Verizon claims that inclusion of SBC might have produced.

The authorities cited by Verizon are not to the contrary. There can be no claim that the Commission "fabricated" its findings on cost of capital as the Court found in *General Development Utilities, Inc. v. Hawkins*, 357 So. 2d 408 (Fla. 1978), nor did it fail to adequately consider any established fact as in *Marco Island Utilities v. Public Service Commission*, 566 So. 2d 1325 (Fla. 1st DCA 1990).

2. The Commission Acted Within its Discretion in Accepting Witness Draper's Telecommunications Index Including CenturyTel and AT&T.

Mr. Draper stated in his testimony that he excluded companies which were "subject to an ongoing merger or acquisition". Exh. 37: 33, 54-55. Application of this criterion led him to include AT&T Corporation and CenturyTel, Inc. in his index even though these companies had been involved in one way or another in merger activities. Verizon purports to know better than Mr. Draper what he meant by this criterion and claims that CenturyTel and AT&T should have been excluded because they were "subject to" a merger or acquisition. Brief at 18.

The Commission staff reviewed Mr. Draper's testimony and concluded that his index was reasonable with AT&T and CenturyTel included. When questioned by Commissioner Bradley at agenda conference, Mr. Lester referenced the fact that Mr. Draper was questioned about including these companies at his deposition. Mr. Lester stated:

> And in his deposition he was asked questions regarding why he included AT&T and why he included CenturyTel. And he explained that - - well, in the case of AT&T/Comcast that was not a complete merger or merger of entire companies. And in the case of Century Tel, the information that he had gotten from Value Line was that the offer between ALLTEL and CenturyTel for them to merge would have had to increase by 20 or 30 percent for that merger to occurred. It is appropriate probably to eliminate companies that are merging because their stock price is going to be distorted relative to what analysts and investors expect the company to earn. And so be that [as it may] the staff witness had to make a judgment call and he chose to include AT&T and CenturyTel, because like I say, AT&T was not a complete company merger and in CenturyTel it was apparently a dying or non-existent merger.

TRA 62; R. 15: 2704.

Mr. Lester's statements correctly reflect Mr. Draper's testimony in his deposition. Exh. 37: 32-35; 54-55. Mr. Draper's testimony was inserted into the record without objection to his qualifications as an expert, and Mr. Lester's characterization of his exercise of judgement is correct. Based on the criteria that he developed, Mr. Draper reasonably concluded as an expert that circumstances surrounding the merger activities of AT&T and CenturyTel were such that they should not be excluded. It was the Commission's prerogative as the evaluator of expert testimony to accept or reject Mr. Draper's inclusion of AT&T and CenturyTel in his index. The Commission certainly was acting within its discretion to take the word of the witness for why he excluded AT&T and CenturyTel over the contrary arguments of witness Vander Weide of Verizon.

In the final analysis, Verizon's argument on this point is simply an invitation for the Court to step in and re-evaluate the evidence presented to the Commission. It was the Commission's judgment that Mr. Draper knew how to apply his criterion excluding companies "subject to" a merger or acquisition and that he did so reasonably. There is certainly no reason to believe that the Commission committed reversible error or that Draper's index was fatally flawed by including these companies.

B. The Commission's Decision to Adopt the Depreciation Lives Approved for BellSouth in the Earlier Phases of the Proceeding was Within its Discretion and is Supported by the Record.

Verizon also decries the Commission's approval of depreciation inputs for the ICM-FL model as based on evidence outside the record and otherwise inconsistent with the Commission's prior decisions. Brief at 20-26. That position fails to address the real issue in the case which was the failure of Verizon's witness to present credible evidence in support of the company's position that the inputs for depreciation lives and salvage should be the same as those reported by Verizon for financial purposes. At the end of the day, the Commission found itself with no reasonable alternative but to apply the depreciation lives and salvage values that it had approved for BellSouth based on a competent depreciation study. As it stated in its UNE Order:

> We are in a quandary regarding depreciation inputs. On one hand, Verizon has not provided sufficient evidence that its proposed inputs are appropriate. Indeed, Verizon only offered support regarding the economic lives of the technology-sensitive accounts. On the other hand, we are hesitant to rely solely on the FCC-approved life and salvage ranges as proposed by the ALECs. On balance, we believe the ALEC Coalition's alternative proposal, to use the deprecation inputs approved for BellSouth by Order No. PSC-01-1181-FOF-TP, represents a good compromise.

UNE Order at 75; R. 16: 2849.

The Commission's decision to adopt the BellSouth inputs for Verizon's ICM model was both supported by the record and within the Commission's authority. In

the first place, the ALEC coalition witness, Dr. Ankum, testified that if the Commission did not accept his suggestion that FCC depreciation lives be adopted, it should adopt the lives approved for BellSouth. Tr. 8: 1256. Dr. Ankum reiterated that proposition in his deposition. Exh. 29: 7, 9, 26.

Verizon's claims that the use of BellSouth's lives was no more supported by the record than the proposals of its own witness to use financial accounting lives is misplaced. Verizon effectively misses the point. The weakness perceived by the Commission in the testimony of Verizon's witness was fundamentally that neither the witness's testimony that financial reporting depreciation lives should be used nor his suggestion that competitors' depreciation lives be used as a benchmark was supported by any kind of competent depreciation study or analysis. Lack of supporting studies was the basic reason the Commission had earlier in the BellSouth Order stated that competitors' depreciation lives should not be used as a benchmark. It was not simply because they were competitors, but because of the lack of studies to confirm that the companies should be considered comparable for depreciation purposes. BellSouth Order, 01 F. P. S. C. 5:494-495. In the BellSouth case, the Commission did have a cost study to support its determination of BellSouth's depreciation lives. It could thus reasonably conclude based on its prior order that they could be applied as proposed by Dr. Ankum and staff. UNE Order at 75; R. 16: 2849.

This Court has never said that the Commission is unable to take recognition of its prior actions embodied in its orders, certainly not in a situation like this.[3] See, *Gulf Power*, 453 So. 2d 799, *supra*. Moreover, an administrative agency like the Commission is certainly able to recognize its own actions and orders and rely on them. *Health Quest Realty XII v. Dept. of Health and Rehabilitative Services*, 477 So. 2d 576, 577-578 (Fla. 1st DCA 1985).

II. THE COMMISSION'S ADJUSTMENTS TO VERIZON'S LOADING FACTORS WERE REASONABLE AND SUPPORTED BY THE RECORD.

It was Verizon's burden in the UNE proceeding to support its cost model inputs with convincing evidence. Where the Commission found such evidence lacking, it was not bound to accept Verizon's position as reasonable simply because there was no contrary testimony from other witnesses. The Commission is entitled to rely on its staff to "test the validity, credibility, and competence of the evidence presented" and to accept or reject the company's position based on that evaluation. *South Florida Natural Gas Co. v. Public Service Commission*, 534 So. 2d 695, 698 (Fla. 1988). *See also*, *Florida Power Corp. v. Cresse*, 413 So. 2d 1187 (Fla. 1982) (demonstration that

[3]As the UNE Order reflects at p. 76, R. 16: 2850, not all lives approved by the Commission were adverse to Verizon's position. Some were in fact equal to or shorter than those proposed by Verizon.

fuel costs were incurred by electric utility was not proof of their reasonableness and it was not the Commission's burden to present evidence to show that the costs were unreasonable).

In this case, only Verizon presented testimony on the loading factors by which it adjusted the inputs to its material unit cost. These factors were of two types, a material loading factor which primarily includes the cost of freight, sales tax and provisioning expense, and an engineering loading factor which includes such things as the cost to plan, engineer and order equipment additions. R. 11: 1998, 2001.

In analyzing Verizon's loading factors, the Commission staff concluded that some suffered from the same fundamental flaw that the Commission recognized in the BellSouth proceeding. That is, the loading factors applied to certain equipment such as copper and fiber cabling, conduits and poles were applied with no adjustment for size. The Commission reasonably concluded that this approach could lead to unrealistic costs estimates. As explained in its UNE Order:

> It appears to us that Verizon's material and engineering loading factors are linear - that is, no adjustment is made for size. For example, Verizon's engineering loading factor for aerial copper is 50 percent. This factor is the same whether it is applied to the smallest increment or to the largest size of aerial copper cable. Similarly, the material loading factor is not differentiated between size or type of cable.
>
> As we found in Order No. PSC-01-1181-FOF-TP for BellSouth, the use of linear factors "can generate questionable results, especially in light of

> deaveraged rates". Order No. PSC-01-1181-FOF-TP, p. 222. For example, Verizon's actual base material costs for aerial copper cable, as a percentage of total loaded cost, are constant at about 34 percent no matter whether the cable is 25-pair or 900-pair. Thus, the total material cost of the cable is always about three times the actual material base cost. No economies of scale for minor material or engineering occur. However, it seems unlikely that no economies are generated as cable sizes grow larger.

UNE Order at 176; R. 16: 2950.

Verizon can hardly contest the Commission's raising of the linearity issue since it was a failure of Verizon to adequately respond to discovery and explain the deviation of its factors that put the Commission in the position of having to make the adjustments. As the staff noted in its recommendation to the Commission:

> As part of discovery, Verizon was asked to provide all supporting documentation and reports showing how each individual ICM investment amount was calculated by account and item. The company's response refers only to the documentation and program code provided with the filing. (Exh. 19, p. 40) If Verizon had been more responsive to discovery, staff and ALEC concerns with Verizon's loading factors may have been resolved.

R. 12: 2003.

The loading factor adjustments of which Verizon now complains is a dilemma of its own making based on failure to provide adequate proof. It put the Commission in the position of having to choose the best way to move the case forward to establish UNE rates which Verizon and the competitor ALECs could rely. The Commission

recognized that it might order Verizon to refile its cost studies with adequate support. TRA 106; R. 15: 2748. However, the Commission staff felt there was inadequate testimony in the record to suggest what alternative methodology the Commission might direct Verizon to apply. *Id.* In any case, the Commission stated in its order that it rejected this alternative in part because of the additional proceedings and delays it would produce. UNE Order at 178; R. 16: 2952.

In the end, the most reasonable approach was for the Commission to try to make adjustments to Verizon's loading factors to bring it more in line with BellSouth's factors in which the Commission had more confidence. Indeed, the fact is that the BellSouth proceeding and the knowledge gained in setting UNE rates for a large ILEC informed the entire proceeding to some degree. The Commission was entitled to rely on its expert staff to recommend adjustments which would bring Verizon's loading factors more in line with those approved for BellSouth. Moreover, as the Commission said in its order, these adjustments were made "recognizing that Verizon will not have the same economies of scale as BellSouth". UNE Order at 178; R. 16:2952. Consequently, the loading factors approved for Verizon were higher than those approved for BellSouth and based on recognition of the differences of the company's operations.

The bottom line is that the Commission was forced into a situation where, in its judgment, it needed to act on the best information available. It made its choices based on the evidence Verizon provided and the informed advice of its expert staff. This Court has never held that the Commission is prohibited from following this course. *South Florida Gas, Gulf Power, 453 So. 2d 799, supra.*

III. THE COMMISSION PROPERLY EXCLUDED VERIZON'S POST-RECOMMENDATION ARGUMENT FROM THE RECORD.

After the Commission staff filed its 489 page recommendation, but before the Commission had taken a vote in the matter, Verizon sent a letter to the Commission's Executive Director, Dr. Mary Bane, complaining of "errors" in the staff's recommendation. The ALEC coalition responded with a motion to strike that was granted at the beginning of the special agenda conference where the recommendation was taken up. TRA 4-7; R. 15: 2646-2647. The Commissioners never saw nor considered the letter. To the extent that Verizon now tries to impeach the Commission's decision based on its contents, that attempt is improper and should be ignored by this Court.

As Verizon is well aware, the Commission does not entertain post-recommendation filings or argument on the staff's final recommendation. Verizon was given an opportunity to present evidence and conduct cross-examination to the extent

it desired to do so and to file a post-hearing brief summarizing its positions and arguments. Verizon has no due process right to go on arguing with the staff after a recommendation is filed. *Op. Att'y. Gen. Fla.* 75-190 (1975) (Right of Public Counsel to cross examine staff witnesses ended with the conclusion of the hearing and there was no due process right to cross examine staff recommendations made after the conclusion of the hearing). *See also*, Rule 25-22.0021, Florida Administrative Code, Agenda Conference Participation, which does not allow written or oral presentations by parties "when a recommendation is presented and considered in a proceeding where a hearing has been held." Nor do Commission staff's advisory recommendations constitute proposed orders to which exception may be taken. *Legal Environmental Assistance Foundation, Inc. v. Florida Public Service Commission*, Case No. 93-2956RX, 93 ER F.A.L.R. 127, (DOAH, August 26, 1993), *aff'd. per curiam, Legal Environmental Assistance Foundation, Inc. v. Florida Public Service Commission*, 641 So. 2d 1349 (Fla. 1st DCA 1994).

Verizon would have the Court believe that the filing was an innocuous attempt to point out simple errors in the staff's calculation. However, that was not the view of staff. As staff attorney Ms. Keating noted at the special agenda conference, to the extent that things like typographical errors were pointed out, they were taken into account. However, Ms. Keating stated that

> . . . the bulk of the letter submitted by Verizon was essentially argument against staff's recommendation. Philosophical points, not just the mere identification of something like 2 plus 2 is 8. They were philosophical disagreements, and we believe they would be more appropriate in another pleading, perhaps a motion for reconsideration or something like that.

TRA 4-5; R. 15: 2646-2647.

As Ms. Keating noted, the letter was not filed in the docket or recognized by the Commission at hearing. TRA 5; R. 15: 2647. Chairman Jaber made the exclusion of the letter from the record explicit in the Commission's vote:

> Commissioners, I think it is probably just cleaner to grant the motion to strike so that to the degree that anyone questions whether the letter became part of the record, we have clarified that it is not, never was, and will not be.

TRA 6; R. 15: 2648.

The letter and its multiple attached schedules are contained at R. 15: 2620 - 2630 of the record on appeal. However, since it was not considered by the Commission nor made part of the record in the proceeding, Verizon cannot rely on its content to support its merits argument before this Court. Verizon certainly would have had an opportunity, as Ms. Keating stated, to file for reconsideration if it believed that the Commission had made mistakes of fact or law in the UNE Order based the staff's recommendation. TRA 5; R. 15: 2647. However, Verizon chose to abandon that course and to proceed directly to this Court even before other parties' pending

motions for reconsideration were taken up by the Commission. As a consequence of this failure, Verizon is now before the Court asking it to indulge its speculation about what the staff may or may not have done based on extra-record material obtained from the staff after the decision. Brief at 36.

The only legitimate question before this Court is whether the Commission acted within its discretion in striking Verizon's unauthorized post-recommendation letter to Dr. Bane. Clearly it was, as this Court recognized under similar circumstances in *Florida Bridge Company v. Bevis*, 363 So. 2d 799, 801 (Fla. 1978). In that case, the Commission refused to consider supportive evidence tendered by Florida Bridge Company after hearing, but before the Commission's final decision. The Court stated:

> We have previously held that the Commission has discretion to terminate its data-gathering function, and we find no abuse of that discretion here. The reports which Florida Bridge tendered to the Commission after the hearing were newly prepared and had not been subjected to examination by the Commission and its staff, cross-examination or other evidentiary evaluation. [Citing *United Tel. Co. v. Mayo*, 345 So. 2d 648, 651-652 (Fla. 1977)].

Id.

The nature of Verizon's argumentative post-hearing letter may be somewhat different than the reports submitted by Florida Bridge, but the applicable principle is the same. The Commission has the discretion to draw the line after the hearing

process is complete, as it was in this case, and to not consider unauthorized post-hearing evidence and argument.

A. The Commission Correctly Calculated the Common Cost Allocator Based on the Evidence Verizon Presented.

As Ms. Keating pointed out, consideration of Verizon's post-recommendation letter would have given rise to a further round of contentious pleadings between the parties. TRA 5; R. 15: 2647. If the Commission were inclined to consider criticism of the staff recommendation before it voted, it would have had to have provided the other parties an opportunity to respond. Given the contentious nature of the UNE proceeding, it is certain that the other parties would have opposed Verizon's positions. In any case, the claimed computational errors, whatever their real basis, would properly been addressed in a motion for reconsideration. Verizon forewent that opportunity and it should not be allowed to make its presentation for reconsideration in this Court.

Verizon is essentially asking this Court to put itself in the place of the Commission and evaluate these claimed errors on the basis of speculation and arguments founded on extra-record materials, e. g., the staff's work papers it obtained after the decision was rendered. Brief at 34. Verizon would have the Court substitute its judgment for that of the Commission in the first instance. It is one thing for Verizon

to ask the Court to review the Commission's order based on a competent substantial evidence standard, it is quite another for Verizon to ask the Court to undo the Commission's decision based on Verizon's untested assertions of error.

Verizon acknowledges that the Commission accepted the company's basic common cost allocation methodology but again complains of errors in the staff's application of that methodology. Verizon essentially makes the same arguments that it made in its unauthorized communication to Dr. Bane. Thus, on page 34 of its Brief it notes that "in reviewing the cost results and staff's workpapers, Verizon requested after the decision, it appears that the Commission's common cost allocations assume an investment amount 60% higher than the amount reflected in Verizon's filing . . . ." It is clear that what Verizon is asking this Court to do is to accept its interpretation of the results of its enormously complicated ICM-FL model based on extra record materials. That is simply not the proper role for the Court. Nor should the Court accept Verizon's speculation that "[t]he discrepancies between the Commission's inputs and assumptions and its cost results are not explained anywhere in the order or elsewhere in the record, so they must be mistakes". Brief at 37. Such arguments do not provide the basis for this Court to reverse the Commission's order in this case.

The staff's recommendation and the resultant UNE Order, to the extent that the staff's recommendations were adopted, was based on the evidence that Verizon and

the other parties presented. For example, the staff noted in its recommendation to the Commission that the ICM-FL model did not adjust the common cost factor to reflect adjustments proposed by staff. R. 12: 2021. The problem arose because the common cost allocator contained in the ICM-FL model was based on revenues not expenses. Verizon proposed expenses as the basis for its common cost allocator and the Commission accepted that position, but the actual common cost calculator based on expenses was completely external to the model. It was only obtained after staff sought to obtain it through interrogatories. Ex. 18: 442. As noted in the UNE Order, that fact gave some concern because of the mismatched cost allocators. However, in the end, the staff had to make its calculations using what Verizon had provided and made its recommendation to the Commission accordingly. UNE Order at 188; R. 16: 2962.

The long and short of this issue is that the staff was working with what Verizon produced through the course of the evidentiary proceeding. The Commission was entitled to rely on its staff for a recommendation based on that evidence, and to cut off further evidence and argument at some point. *Florida Bridge, supra*. It is certainly not this Court's role to take up Verizon's case and effectively grant a motion for reconsideration of the Commission's order based on speculation and untested

material that the Commission has not considered and that is not part of the evidentiary record in this case.

B. The Commission's Computation of Verizon's UNE-P Rates is Based on the Evidence Verizon Presented.

In determining rates for Verizon's UNE-P combinations, the Commission accepted Verizon's optional proposal of using the "integrated digital loop carrier" ("IDLC") technology which resulted in a lower price than use of the "universal digital loop carrier" ("UDLC") technology. The resultant savings were calculated at a $1.39 per month by Verizon's witness, Mr. Tucek. Tr. 5: 786. That is the figure that the Commission used in its order. UNE Order at 281; R.17: 3055. The Commission made no finding as to whether the figure should be adjusted based on other adjustments in the staff's recommendations. Again, the Commission was forced to rely on the quality of evidence it was presented up to the time of the decision. When asked by Commissioner Deason at the special agenda conference whether other staff adjustments would affect the $1.39 figure, staff witness King replied:

> Yes sir. In theory, the amount would change. When we asked Verizon to explain - - and the Verizon witness said that you can go into the model and make - - choose to use IDLC technologies for these loops/port combinations. Staff followed the directions that were provided by Verizon both in Witness Tucek's testimony and in, I believe, it was Interrogatory No. 239 that Verizon provided that response, and they provided us a zip disk. When we ran through all the steps they told us

> to run through, we got a blank result. So the best information we had on the record was the $1.39.

TRA 118; R. 15: 2760.

It was not the staff's responsibility to keep trying to get accurate information from Verizon. The Court should certainly not take it on faith based on Verizon's speculation and extra-record commentary that the Commission made an error in its calculation. It was hardly arbitrary for the Commission to rely on the best evidence it had before it, namely that which was provided by Verizon's own witnesses.

CONCLUSION

The Commission's orders come to this Court with a presumption of validity, and a challenger has a heavy burden to overcome that presumption on appeal. *Pan American World Airways, Inc. v. Florida Public Service Commission*, 427 So. 2d 716 (Fla. 1983); *Florida Interexchange Carriers Association v. Clark*, 678 So. 2d 1267 (Fla. 1996). Verizon has not met its burden to show that the Commission committed reversible error in this case. UNE Order was made consistent with the agency's expertise and discretion and fails neither from a lack of record support nor other procedural irregularity. The UNE Order setting UNE rates for Verizon should be affirmed in all respects.

Respectfully submitted,

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