Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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In the Matter of	)	
	)	CC Docket No. 93-193
1993 Annual Access Tariff Filings	)	Phase I
	)	
1994 Annual Access Tariff Filings	)	CC Docket No. 94-65
	)	
AT&T Communications	)	CC Docket No. 93-193
Tariff F.C.C. Nos. 1 and 2	)	Phase II
	)	
Bell Atlantic Telephone Companies	)	CC Docket No. 94-157
Tariff F.C.C. No. 1,	)	
Transmittal No. 690	)	
	)	
NYNEX Telephone Companies	)	
Tariff F.C.C. No. 1,	)	
Transmittal No. 328	)	

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GTE's REBUTTAL

GTE Service Corporation and its affiliated
domestic telephone operating companies

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September 28, 1995

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SUMMARY

In order to reach a decision on the merits of cost issues not previously addressed, the Commission seeks much of the same information it sought in 1992, and also requests certain additional information. The Direct Case filed by GTE on August 14, 1995 ("*GTE's 1995 Direct Case*") satisfies the Commission's request to refresh the record on issues surrounding exogenous treatment of certain Other Postretirement Employee Benefits ("OPEBs") costs.

It should have been no surprise to MCI that GTE refers to information filed previously. Since significant efforts are spent to maintain consistency in assumptions, plans and benefits, MCI should not have expected that new data would be available after only two years experience of an accounting treatment that will ultimately take approximately twenty years to evolve.

The statement by Andrew Abel, Ph. D. and Peter Neuwirth (*Abel/Neuwirth*), who prepared the Godwins study, filed by USTA in response to the previous FCC investigation of OPEBs, together with the current analysis, filed by USTA in its 1995 Direct Case ("*USTA's 1995 Direct Case*"), verifies that the Godwins study continues to be a valid and reliable means to estimate any potential impact of double counting under GNP-PI.

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GTE's REBUTTAL

GTE Service Corporation and its affiliated domestic telephone operating companies ("GTE") hereby submit their rebuttal to MCI with regard to the Commission's Order Designating Issues for Investigation (the "*1995 Investigation Order*"), DA 95-1485 (released June 30, 1995).

MCI opposes the Direct Cases submitted by Local Exchange Carriers ("LECs" or "exchange carriers"), (i) contending that the LECs provide no new evidence to support exogenous claims, and (ii) raising the same objections to the Godwins study it previously raised.

DISCUSSION

A. THE DATA RESUBMITTED BY EXCHANGE CARRIERS REMAINS VALID.

In the *1995 Investigation Order*, the Commission (at para. 15) seeks to "refresh" the record on issues related to OPEBs. In *GTE's 1995 Direct Case*,[1] GTE answers each of the Designated Issues and Specific Information Requirements set out in the *1995 Investigation Order*. The data presented supports the methods and procedures used in calculating the request for exogenous treatment in GTE's 1993 Annual Access Tariff Filings. Further, the 1995 analysis performed by *Abel/Neuwirth*[2] supports GTE's contention that costs included in the GNP-PI are not "double-counted" in the exogenous claim.

MCI (at 2) states that LECs' Direct Cases merely "restated the arguments which the Commission previously found to be inadequate." In making a decision on OPEBs initially,[3] the Commission rejected the LECs' requests for exogenous treatment of OPEBs costs without having investigated their underlying assumptions. Now, prodded

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[1] GTE's Direct Case, filed August 14, 1995, 1993 Annual Access Tariff Filings, CC Docket No. 93-193, Phase I, 1994 Annual Access Tariff Filing, CC Docket No. 94-65 ("*GTE's 1995 Direct Case*").

[2] *See USTA's 1995 Direct Case*, Attachment A, filed August 14, 1995.

[3] Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers Accounting for Postretirement Benefits Other than Pensions," CC Docket No. 92-102, Memorandum Opinion and Order, 8 FCC Rcd 1024 (1993) (the "*OPEB Order*"), *reversed and remanded*, Southwestern Bell Tel. Co. v. FCC, 28 F.3d 165 (D.C. Cir. 1994) ("*Southwestern Bell*").

by the court's reversal/remand[4] in *Southwestern Bell*,[5] the Commission is for the first time examining the exchange carriers' governing assumptions.

Specifically, the *1995 Investigation Order* requests actuarial and financial assumptions that were used to develop the exogenous requests. Further, the Commission asks for an updating of the record to include assumptions previously used (and provided) in addition to other data.

Thus, the *1995 Investigation Order* (at para. 15) says: "[T]his combined investigation seeks to determine whether the assumptions the individual LECs and AT&T made in calculating the costs of postretirement benefits are just and reasonable, in accordance with the Commission's rules and in the public interest." And it adds:

> We seek some of the same type of cost information sought in the initial *OPEB Investigation*. The *OPEB Order* did not reach the merits of the record on these cost issues for individual LECs because it determined that SFAS-106 amounts should not receive exogenous treatment generally. Because the record in that proceeding is also stale, we seek in the current investigation to refresh the record on the various issues designated below.[6]

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[4] The court stressed that the Commission "was bound to follow [its exogenous rule] until such time as it altered [that rule] through another rulemaking." *Southwestern Bell*, 28 F.3d at 169, *citations and footnotes omitted.*

[5] "*[A]ny* analysis of whether an exogenous change will be reflected in the GNP-PI will involve some unproven -- and likely unprovable -- assumptions.... If an agency can reject an econometric study merely by observing that it employed unproven assumptions (and that the outside party bore the burden of proof), then no party with the burden can ever prevail. `[A]ssigning the burden of proof is not a magic wand that frees an agency from the responsibility of reasoned decision-making.' ... To reject such a study, the Commission must at least express a reason for doubting some critical assumption." *Southwestern Bell*, 28 F.3d at 172, *citation omitted.* The court also found "quite illogical" the FCC's conclusion "that because the studies began with different assumptions, neither could be relied upon...." *Id.*

[6] *Id.*

Since the actual wording requesting the assumption data is almost identical in both the *OPEB Investigation Order*[7] and the *1995 Investigation Order*, it should not have surprised MCI that many LECs made reference to, and re-submitted, data filed previously. With significant efforts being applied to maintain consistency in assumptions, plans and benefits, it should not be expected that new data would be available after only two years experience of an accounting treatment that will ultimately take approximately twenty years to evolve.

GTE does not believe the Commission wanted a "rehashing" of arguments presented previously in support of exogenous treatment. *Southwestern Bell*, based on an established record, concluded that, under the current FCC rules, changes in OPEBs costs caused by the implementation of SFAS-106 do qualify for exogenous treatment. It is not necessary here to restate the same arguments. GTE did resubmit the data on which its assumptions were based, since this data remains valid and has not changed.

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[7] Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers Accounting for Postretirement Benefits Other than Pensions," CC Docket No. 92-102, Order of Investigation and Suspension, 7 FCC Rcd 2724 (1992) (by Chief, Common Carrier Bureau) ("*OPEB Investigation Order*").

[7] Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers Accounting for Postretirement Benefits Other than Pensions," Memorandum Opinion and Order, 8 FCC Rcd 1024 (1993) (the "*OPEB Order*"), *remanded*, Southwestern Bell Tel. Co. v. FCC, 28 F.3d 165 (D.C. Cir. 1994) ("*Southwestern Bell*").

B. THE GODWINS STUDY ALSO REMAINS VALID.

MCI (at 6) asserts that "the LECs have not met their burden of proof justifying their exogenous claims." The Attachment to the instant submission is a Supplemental Report prepared by Andrew B. Abel, Ph.D. and Peter J. Neuwirth ("*Abel/Neuwirth Rebuttal Supplemental Report*"). The *Abel/Neuwirth Supplemental Report* illustrates MCI's failure to understand the modeling and economic analysis in the Godwins Study, and clearly demonstrates that MCI's criticisms are baseless.

Further, MCI -- which also uses arguments already on the record -- claims that unverifiable assumptions were used. MCI (at 4) continues to argue that because the Godwins study and the NERA study started with different assumptions, the Godwins study is not valid. This position was rejected in *Southwestern Bell*, which said it would be "quite illogical" to reject the Godwins study because of assumptions used or variance from other similar studies.[8] As the court observed, "*any* analysis of whether an exogenous change will be reflected in GNP-PI will involve some unproven -- and likely unprovable -- assumptions."[9]

C. GTE's PARTICIPATION RATE REFLECTS REALITY.

MCI (at 6) questions LEC estimates of participation rates, and goes on to make an unsubstantiated and erroneous claim that exchange carrier OPEBs programs are "overly generous."

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[8] *See* n.5 *supra*.

[9] *Southwestern Bell*, 28 F.3d at 172.

GTE defines participation as the number of employees eligible to receive post-employment benefits. Those GTE employees who are subject to collective bargaining agreements participate according to the individually negotiated contracts for the various bargaining units. Those GTE employees who are not subject to collective bargaining agreements are all eligible to receive post-employment benefits.

The important point is that both groups must meet significant eligibility requirements before receiving benefits. In most cases, these eligibility requirements involve the employee attaining retirement requirements. For example, generally an employee not subject to collective bargaining is required to have a minimum of 15 years of service and the sum of that employee's years-of-service and age must total at least 76, or age 65 with 5 years of service.[10] OPEBs do not vest. Thus, there are significant hurdles for an employee to receive retirement benefits. These factors significantly reduce the costs inherent in providing OPEBs.

Further, how the LECs' programs are structured has never been an issue. MCI has presented no evidence of any type to substantiate its claim that the LECs' programs are "overly generous" or that they "exceed both the industry norm, as well as the norm of today's economy."[11] All companies have benefits that allow them to attract the "best" individuals to bolster their work force. In addition, the majority of GTE's employees are covered under plans negotiated through the various bargaining units representing its employees, and these plans are likely to reflect the "industry norm." The Commission

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[10] At times, retirement requirements depend on negotiated conditions associated with purchases of other companies.

[11] MCI at 6.

should reject MCI's unsubstantiated allegations; and should recognize that, in a competitive workplace, a well-managed company does what is needed to hire and retain the best employees.

Respectfully submitted,

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Supplemental Report

Perspectives on Analysis of Impact of
SFAS 106 on GNP-PI

September 28, 1995

Towers Perrin

Introduction

Over the past four years, we have been working with various Price Cap LECs to analyze the impact of SFAS 106 on the GNP-PI. In February 1992, we issued our original report indicating that less than 1% of the Price Cap LECs' additional costs due to SFAS 106 would be reflected in the GNP-PI, and that approximately 85% of the LECs' additional costs would not be reflected in the GNP-PI or recovered through other macroeconomic effects.

Earlier this year, we were asked to provide an opinion as to the extent to which the findings of our original report, issued three years earlier, should still be considered valid. On August 14, 1995 we issued a report stating that we believe that the actual impact of SFAS 106 on the GNP-PI and the percentage of LECs' additional costs due to SFAS 106 that remain unrecovered were not materially different than indicated in our original report.

In September 1995, MCI submitted an opposition to our August 14, 1995 report. We find that MCI's criticisms in its opposition are completely without merit. There is nothing in MCI's opposition that would lead us to modify any of the findings in our original report or in subsequent reports we have prepared on this issue. This report provides a detailed response to MCI's submission.

Respectfully submitted,

Peter J. Neuwirth, F.S.A., M.A.A.A.

Andrew B. Abel, Ph.D.

Executive Summary

MCI's opposition is without merit and reflects a failure to understand the modeling and economic analysis in our reports. This report clarifies and further explains the motivation and implementation of the economic analysis underlying our reports. In addition, we discuss in detail MCI's various criticisms and show that they are baseless. The specific points discussed in the body of our report are summarized below.

1. Despite MCI's criticism of our model as a "what-if" model, the question of the impact of SFAS 106 on the GNP-PI is precisely a "what-if" question. To address this question quantitatively, we need to determine how much different the GNP-PI would have been if SFAS 106 had not been introduced.

2. Using a set of five criteria outlined in our original report, we decided to use a quantitative general equilibrium model to analyze the impact on the GNP-PI of the introduction of SFAS 106. The numerical values of the model's parameters were chosen by a method known as calibration, which uses existing econometric estimates to determine the numerical values of some parameters, and chooses the values of other parameters so that the values of certain variables in the model match the actual values of these variables in the economy. MCI's criticism of the choice of numerical values for parameters reflects an ignorance of calibration in quantitative general equilibrium models, a method that is widely used in modern macroeconomic analysis.

3. The specification and calibration of the macroeconomic model was guided by a conservative philosophy which, in this context, guards against understating the impact of SFAS 106 on the GNP-PI. It also guards against overstating the percentage of LECs' additional costs due to SFAS 106 that remain unrecovered after taking account of the GNP-PI and other macroeconomic effects.

4. The extensive sensitivity analyses performed earlier produce a wide range of numerical results, but the most extreme results are based on combinations of parameter values that are too implausible to be taken seriously. The sensitivity analyses support the conclusion that only a small fraction of LECs' increased costs due to SFAS 106 are recovered through the GNP-PI, and even taking account of other macroeconomic effects, the majority of additional costs will be unrecovered.

5. Despite the fact that the NERA study and our original report used different assumptions about the extent to which the accrual of future OPEB's is a factor in the determination of prices in the absence of SFAS 106, our model can be extended to include the NERA assumption. This extension was implemented in the March 1993 Supplemental Report. Despite some quantitative differences in the findings using the two assumptions, the results are consistent with each other in that for both sets of assumptions the effect on GNP-PI is tiny and a very large fraction of LECs' increased costs due to SFAS 106 remains unrecovered. Although MCI criticizes our model for its ability to incorporate the NERA assumption, we regard this flexibility and the

similarity of substantive findings as reinforcing the results in our original report.

6. In light of the findings above, the criticisms raised by MCI are entirely without merit and would not lead us to modify any of the conclusions of our previous reports.

Rebuttal to MCI

MCI Telecommunications Corporation's Opposition to Direct Cases reflects a continued misunderstanding of the basic economic approach underlying our original report and of quantitative economic analysis in general. In this report, we discuss the basic methodological issues underlying our original report and explain why MCI's criticisms of the methodology are confused and without merit.

"What-if" Analysis

A glaring example of MCI's misunderstanding is the criticism of our model as a "what-if" tool [1]. As we have emphasized elsewhere,[2] a "what-if" analysis is the only way to calculate the impact of SFAS 106 on the GNP-PI. The impact of SFAS 106 on the GNP-PI equals the actual value of the GNP-PI in a given year after the introduction of SFAS 106 minus the value of the GNP-PI that would have been observed in that same year if SFAS 106 had not been introduced. To estimate the value of GNP-PI that would have been observed in the absence of SFAS 106 we must ask "What would have been the value of the GNP-PI if SFAS 106 were not introduced?" This is precisely the sort of "what-if" exercise that is criticized by MCI. Although MCI seems to prefer the use of an econometric model, it appears oblivious to the fact that using an econometric model to address the impact of SFAS 106 on the GNP-PI is also a "what-if" exercise.

The Roles of Modeling and Econometrics

Any quantitative study of the impact of SFAS 106 on the GNP-PI must make a methodological decision about the type of model to use. In our original report we listed a set of five criteria to guide the choice of a model, and we explained why these criteria led us to use a quantitative general equilibrium model[3]. As explained elsewhere, large-scale econometric models fail to satisfy two of these criteria[4], and thus these models were deemed inappropriate for our study. Because MCI continues to criticize our model for not being "an econometric model capable of determining with some degree of statistical confidence the impact of SFAS 106 on GNP-PI,"[5] we will revisit the issue of model design from a fresh perspective.

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[1] MCI, p. 5

[2] Analysis of Impact of FAS 106 Costs on GNP-PI, Supplemental Report: Responses to Objections Raised Regarding Original Study, July 1992, p. 23.

[3] Analysis of Impact of FAS 106 Costs on GNP-PI, February 1992, pp. 26-27.

[4] Response to Paragraph 16 of FCC Order of Investigation and Suspension, May 26, 1992, pp. 1-2.

[5] MCI, p. 4

To see why MCI's criticism is misguided, it is helpful to understand the role of modeling and the role of econometrics in addressing the question of the impact of SFAS 106 on the GNP-PI.

The Role of Modeling. In order to determine the effect of SFAS 106 on the GNP-PI we need a macroeconomic model that takes account of the interactions of the demand for goods, the production function, and the supply and derived demand for labor, and uses these interactions to simultaneously determine prices, wages, and other labor costs. A model is a set of equations that represent various aspects of economic behavior. The general mathematical form of our model is presented in detail in Appendix C of our original report.

The Role of Econometrics. Once a general mathematical model is formulated, the numerical values of the model's parameters need to be selected. Econometric estimation is a statistical technique to choose these numerical values. Our original report does not produce its own econometric estimates of the parameters. Instead the report relies on the results of previous econometric studies in the literature for guidance in choosing the values of parameters. As discussed in our original report,[6] the value of the elasticity of labor supply was chosen based on a survey of the econometric literature on labor supply in Labor Supply by Mark R. Killingsworth. The value of the price elasticity of demand was chosen to be very conservative based on the summary of econometric estimates of price elasticities of demand reported in Economics by Michael Parkin[7].

There are two advantages to using previous econometric studies rather than producing a new set of econometric estimates for calculating the impact of SFAS 106 on the GNP-PI. First, these previous studies can be viewed as being truly unbiased with respect to the issue of the effects of SFAS 106 on the GNP-PI because they were conducted without any reference to this issue. Second, rather than rely on the results of any single econometric exercise, we have based our choices of parameters on a body of research comprised of many studies. Moreover, in using these previous econometric studies to determine the values of parameters, we have been conservative in the sense discussed in the next section.

As we have just discussed, our original report does not perform its own econometric analysis and the model used in that report is not an econometric model, though the model does rely on econometric estimates for some of its parameter values. The numerical values of other parameters are chosen so that the model produces values for some variables that

[6] Analysis of Impact of FAS Costs on GNP-PI, February 1992, p. 30.

[7] A brief summary of the findings reported by Parkin is contained in footnote 4 on page 12 of Analysis of Impact of FAS 106 Costs on GNP-PI, Supplemental Report: Additional Sensitivity Analysis, March 1993.

match the actual values in the economy. For instance, the parameters of the production function are chosen so that the share of labor cost in total cost in the baseline calculation matches the share of labor cost in total cost in the U.S. economy. This approach to choosing numerical values of parameters, which uses both previous econometric estimates and parameter values that allow the model to match certain data, is known as *calibration*[8]. Calibration is commonly used in modern macroeconomic analysis to select parameter values in quantitative general equilibrium models.

The Conservative Approach

As we have discussed, calculation of the impact on the GNP-PI of the introduction of SFAS 106 is a "what-if" exercise. This calculation necessarily involves estimation of how much different the GNP-PI would have been if SFAS 106 had not been introduced. Because we cannot rerun history and alter it to exclude SFAS 106, nor can we run a controlled experiment, any calculation of the impact of SFAS 106 is an approximation rather than an accurate and precise determination of the exact impact. Recognizing the approximate nature of any such calculation, we adopted a conservative approach to guide the analysis in our original report. In this context, "conservative" means that our calculations tend to overstate the impact on the GNP-PI and thus to understate the fraction of LECs' additional costs due to SFAS 106 that remain unrecovered.

The conservative approach guided both the actuarial and macroeconomic analyses in our original report.[9] The baseline findings of the original report are that ultimately the increase in GNP-PI (0.0124%) caused by SFAS 106 will provide recovery of 0.7% of the LECs' increase in costs due to SFAS 106, and that taking account of additional macroeconomic effects that might occur, 84.8% of the increase in costs remains unrecovered. The March 1993 Supplemental Report also presents a "best estimate" set of results, which are not subject to the conservative influence guiding the baseline calculations. For example, according to our best estimates, only 0.3% of the increase in LECs' costs due to SFAS 106 are recovered through the GNP-PI. Furthermore, a comparison of the "best estimate" and "baseline" findings supports our original report in two ways. First, the two sets of findings are not very different from each other. Second, the baseline calculations featured in our original report are indeed conservative relative to our best estimates.

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[8] Calibration is discussed in Analysis of Impact of FAS 106 Costs on GNP-PI, Supplemental Report: Responses to Objections Raised Regarding Original Study, July 1992, pp. 40-41. Response to Paragraph 16 of FCC Order of Investigation and Suspension, May 26, 1992, pp. 3-5, gives a complete description of the calibration of the parameters in our model.

[9] The conservative approach is explained in Analysis of Impact of FAS 106 Costs on GNP-PI, Supplemental Report: Responses to Objections Raised Regarding Original Study, July 1992. See footnote 4 on page 16 of that report for a discussion of conservatism in the actuarial analysis, and see page 32 of that report for a discussion of conservatism in the macroeconomic analysis.

The Role of Sensitivity Analysis

In addition to comparing the best estimate and baseline results, we have performed extensive sensitivity analyses.[10] Our August 14, 1995 report[11] discusses the purpose of sensitivity analysis and explains why many of the calculations in our sensitivity analyses should be ignored because they were based on combinations of implausible parameter values. This report clearly and emphatically states that the range of parameter values used in the extensive sensitivity analysis was chosen to make sure that all plausible combinations of parameter values were included, with the recognition that many of these combinations were implausible and should be ignored. It is important to keep in mind that the purpose of the sensitivity analysis is not to delineate the set of plausible combinations of parameter values, but is instead to explore the robustness of our findings and to illustrate the quantitative impact on our findings of various changes in the numerical values of the inputs. Despite this discussion, MCI continues to criticize our findings because they present "extremely wide ranging results of GNP-PI effects".[12] However, this criticism has already been addressed by the detailed discussion of this issue on pp. 4-5 of the August 14 report. Nothing in the MCI opposition addresses any of the substantive arguments on pp. 4-5 of that report, so there is no point in repeating the details of that argument, except for the closing sentence: "To reiterate, our sensitivity analysis presents the results for all combinations of parameter values, including many combinations too implausible to merit any attention."

Reconciliation with NERA's Analysis

MCI points out that our original report and the NERA study start with different assumptions about the pricing behavior of competitive (unregulated) firms[13]. The difference between the two studies relates to the extent to which firms take account of the current accrual of future OPEB's (other postretirement employee benefits) when pricing their products. To the extent that firms understand and calculate the actuarial value of future OPEB's, the accrual of these OPEB's would be factored into prices by rational forward-looking competitive firms. NERA has chosen to follow the conventional economic assumption that competitive firms are rational and forward-looking and thus assumes that prices would reflect the accrual of future OPEB's even without SFAS 106. However, many workers producing output on any given date will not receive OPEB's until decades later. The calculation of the accrual of these OPEB's is a detailed actuarial task, and some firms may not have the expertise, foresight or inclination to compute and take account of these far-off costs in the absence of SFAS 106. The introduction of SFAS 106 may force such firms to only then factor these costs into their

[10] Our original report contains a sensitivity analysis, and the March 1993 Supplemental Report contains a much more extensive sensitivity analysis.

[11] "Perspectives on Analysis of Impact of SFAS 106 on GNP-PI".

[12] MCI, p. 3

[13] MCI, pp. 3-4

pricing decisions. Consistent with the conservative approach, our original report is based on the assumption that firms ignore the accrual of OPEB's before SFAS 106 and take account of these accruals when SFAS 106 is introduced. Relative to the assumption adopted by NERA, this assumption leads to a larger (i.e., more conservative) impact of SFAS 106 on the GNP-PI and to a lower percentage of the LECs' increase in costs due to SFAS 106 that remains unrecovered.

While NERA's study and our original report used diametrically opposed assumptions about pricing behavior in the absence of SFAS 106, one might reasonably assert that the actual behavior of firms lies somewhere between these extremes. Our March 1993 Supplemental Report[14] recognizes that the assumptions used by NERA and by us are at opposite ends of a spectrum and presents calculations of the impact of SFAS 106 for assumptions at both ends of the spectrum (corresponding to the NERA assumption and our assumption) as well as for various intermediate assumptions. If the actual behavior of firms is somewhere between the opposite assumptions used by NERA and by us, then these intermediate assumptions may better reflect the actual behavior of firms. However, one must not lose sight of the conservative approach guiding our original report. According to our approach, when we are unsure about which of a set of potential assumptions to adopt, we will adopt the one that leads to the largest calculated impact of SFAS 106 on the GNP-PI. The results reported on page 5 of the March 1993 Supplemental Report illustrate that the assumption used in our original report is indeed conservative relative to the assumption used by NERA and relative to intermediate assumptions.

MCI (pp. 4-5) mentions the calculations in the March 1993 Supplemental Report that use the NERA assumption about pricing, and criticizes these calculations because they illustrate that our model is a "what-if" model. This criticism is entirely off target. First, we have already explained why a "what-if" model is needed to calculate the impact of SFAS 106 on the GNP-PI. Moreover, these calculations can be viewed as adding an extra dimension to the sensitivity analysis. Recall that a sensitivity analysis indicates the quantitative impact on the results of changing various parameters or equations in a model. The calculations reported on p. 5 of the March 1993 Supplemental Report constitute a sensitivity analysis focusing on the assumption underlying pricing behavior. This sensitivity analysis reinforces the major quantitative findings of our original report: the introduction of SFAS 106 has a minuscule effect on the GNP-PI; and an overwhelming share of LECs' additional costs due to SFAS 106 remain unrecovered. Rather than being a point of vulnerability, these calculations are a source of strength and reinforce the findings in our original report.

[14] Analysis of Impact of FAS Costs on GNP-PI, Supplemental Report: Additional Sensitivity Analysis, March 1993, pp. 3-5.

Conclusion

The criticisms raised by MCI are entirely without merit. There is no serious argument in MCI's statement that would lead us to modify any of the findings in our original report or in any of our subsequent reports. MCI's characterization of the calculations in that report as "nothing more than a random and indiscriminate exercise" is irresponsible and reckless and reveals complete ignorance of the state of quantitative general equilibrium models that are an important part of modern macroeconomics.

Our original report was designed to answer a "what-if" question: How much different would the GNP-PI have been if SFAS 106 were never adopted? As explained in our original report, the choice of a model was thoughtfully and deliberately based on a set of desirable criteria for a quantitative macroeconomic model. These criteria led to a quantitative general equilibrium model rather than a large-scale econometric macroeconomic model, and econometric estimates were taken from the economics literature to calibrate some of the key parameters of the model.

The philosophy that guided development and implementation of our model was one of conservatism. Recognizing the difficulty of precisely and accurately determining the exact effect of SFAS 106 on the GNP-PI, our model was designed to guard against understating the impact on the GNP-PI. Thus the baseline finding that the increase in the GNP-PI (0.0124%) will provide recovery of only 0.7% of increased costs due to SFAS 106 is designed to be an overestimate of the actual impact on the GNP-PI, and the baseline finding that 84.8% of the LECs' additional costs due to SFAS 106 remain unrecovered is meant to be an underestimate of the actual percentage.

Finally, MCI has pointed out that our August 14, 1995 report contains no new evidence. We did not present any new evidence because the conservatism in our original report was designed to guard against understating the impact of SFAS 106 on the GNP-PI even if new data turned out to be moderately different from the assumptions used in the study. Moreover, MCI has produced no substantive argument that would lead us to modify our findings in any way.

Certificate of Service

I, Judy R. Quinlan, hereby certify that copies of the foregoing "GTE's Rebuttal of MCI" have been mailed by first class United States mail, postage prepaid, on the 28th day of September, 1995 to the parties on the enclosed list.

Judy R. Quinlan

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