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July 2, 1996

William F. Caton
Secretary
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Re: Ex Parte Presentation in
CC Docket No. 96-98

Dear Mr. Caton:

The original and one copy of this ex parte notice and two copies of a written ex parte presentation are submitted pursuant to Section 1.1206(a) of the Commission's rules. Today, representatives of GTE Corporation met with John Nakahata, Lauren Belvin, James Casserly, and Richard Metzger and his staff concerning the above-captioned proceeding. During those meetings, GTE made a presentation containing the positions it has previously placed in the record in this proceeding and provided the attached written material.

Please let me know if you have any questions.

Sincerely,

R. Michael Senkowski

R. Michael Senkowski
Counsel for GTE Corporation

Enclosure

cc(w/enc.): John Nakahata
Lauren Belvin
James Casserly
A. Richard Metzger, Jr.

SUMMARY OF
ECONOMIC EVALUATION OF VERSION 2.2 OF THE HATFIELD MODEL

By Timothy J. Tardiff
Vice President, National Economic Research Associates

The Hatfield Model is fundamentally flawed in a number of ways:

Economic Theory:

The Hatfield Model creates a fantasy world based upon a "scorched node" scenario in which a new entrant would instantly materialize and take advantage of all of the economies associated with serving known demand with perfectly sized facilities obtained at the maximum volume discounts.

This ignores the fact that real businesses add new investments to an existing network, rather than starting with a clean slate, and such additions must balance the advantages of the eventual lower per unit costs of bigger modules with the costs of carrying the unused capacity until such demand materializes.

The scorched node approach also ignores the fact that complete adoption of today's most modern technology, that would be outdated tomorrow, would not allow any firm to earn a return sufficient to justify the investments.

Input Prices:

The prices used are far below those currently experienced by incumbent local exchange carriers (ILECs), and in the case of switching equipment, are not real prices at all.

Model Process:

The model systematically uses calculation methodologies and engineering assumptions that produce unrealistically low costs. For example, the model produces loop costs that are understated by at least fifty percent, and local switching costs that are too low by at least a third.

Loops:

Relies on Benchmark Cost Model (BCM) that was only intended to measure the relative costs of serving different customers, not to determine the absolute or actual cost.

Models loops within Census Block Groups (CBGs) by assuming square geography, featureless plain topography, and uniform customer distribution.

CC Docket No. 96-98
Ex parte of GTE
June 27, 1996

Assumes single largest cable size ultimately needed, rather than recognizing the need for multiple cables sized to meet demand over several shorter planning horizons. Further, ignores situation wherein largest cable size is beyond what can be physically accommodated by support structures.

Calculates installation and support structure costs as a multiple of cable cost.

Uses unrealistically high utilization (fill) factors.

Switching:

Installs ultimate needed capacity at time of initial purchase, ignoring fact that ILECs buy both new switches and higher priced additional lines for existing switches.

Uses heavily discounted fictitious price for new switches developed by simplistically piecing together inconsistent and mis-matched information from various sources.

Conversion of Investment to Monthly Costs:

Uses unrealistically low cost of capital that fails to reflect the future competitive nature of the industry.

Uses extremely long depreciation rates (*e.g.*, 20 years for switching) that ignore rate of technological change, and are at odds with the levels used by today's competitive telecommunications firms.

Uses ratio of booked expenses to investment, rather than a forward-looking relationship.

Assumes decreases in initial investment level will also reduce future expense.

Conclusion:

The Hatfield Model's fundamental flaws render it useless for obtaining reasonable estimates of the costs of incumbent local exchange carrier network elements.

Adoption of its outputs would be anti-competitive because it would stifle the most effective type of competition (facilities based) and would force any captive customers that may remain on an ILEC network to subsidize the below-cost input prices for new entrants.